

From Protest to Progress

**Addressing Labor
and Environmental
Conditions Through
Freer Trade**

**A Statement by the
Research and Policy
Committee of
the Committee for
Economic Development**

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RESPONSIBILITY FOR CED STATEMENTS ON NATIONAL POLICY

The Committee for Economic Development is an independent research and policy organization of some 250 business leaders and educators. CED is nonprofit, nonpartisan, and nonpolitical. Its purpose is to propose policies that bring about steady economic growth at high employment and reasonably stable prices, increased productivity and living standards, greater and more equal opportunity for every citizen, and an improved quality of life for all.

All CED policy recommendations must have the approval of trustees on the Research and Policy Committee. This committee is directed under the bylaws, which emphasize that "all research is to be thoroughly objective in character, and the approach in each instance is to be from the standpoint of the general welfare and not from that of any special political or economic group." The committee is aided by a Research Advisory Board of leading social scientists and by a small permanent professional staff.

The Research and Policy Committee does not attempt to pass judgment on any pend-

ing specific legislative proposals; its purpose is to urge careful consideration of the objectives set forth in this statement and of the best means of accomplishing those objectives.

Each statement is preceded by extensive discussions, meetings, and exchange of memoranda. The research is undertaken by a subcommittee, assisted by advisors chosen for their competence in the field under study.

The full Research and Policy Committee participates in the drafting of recommendations. Likewise, the trustees on the drafting subcommittee vote to approve or disapprove a policy statement, and they share with the Research and Policy Committee the privilege of submitting individual comments for publication.

The recommendations presented herein are those of the trustee members of the Research and Policy Committee and the responsible subcommittee. They are not necessarily endorsed by other trustees or by non-trustee subcommittee members, advisors, contributors, staff members, or others associated with CED.

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Purpose of This Statement

From the date of its founding during World War II, the Committee for Economic Development (CED) has concerned itself with international economic institutions and policies designed to foster steady economic growth at high employment and reasonably stable prices, increased productivity and living standards, greater and more equal opportunity for every citizen, and improved quality of life for all.

This dedication to international economic policies to further economic well-being is evidenced by CED policy statements such as: *Transnational Corporations and Developing Countries* (1981), *Finance and Third World Economic Growth* (1987), *Breaking New Ground in U.S. Trade Policy* (1990), *The United States in the New Global Economy* (1992), *U.S. Trade Policy Beyond the Uruguay Round* (1994), and *Improving Global Financial Stability* (2000).

In early 2001, a CED subcommittee was formed to focus on the subject of further economic globalization, as reflected in both international trade and foreign direct investment. However, it quickly became apparent to this subcommittee that there was a more urgent need for a new CED policy statement supporting the resumption of multilateral trade negotiations and addressing the consequences of continued inaction.

CED's goal in authoring this paper is to cut through the knot of social issues that have eroded the domestic constituency for international trade, to help lead the discussion toward a more successful approach, and to support the granting of trade negotiation authority to the President. A CED policy statement on the broader issues of economic globalization and its potential for enhancing economic welfare will follow at a later date.

ACKNOWLEDGMENTS

This policy statement was developed by the committed and knowledgeable group of business, academic, and policy leaders listed on page vi. We are grateful for the time, effort, and care that each put into the development of this report.

Special thanks go to the subcommittee co-chairs, Edmund B. Fitzgerald, Managing Director of Woodmont Associates, and Paula Stern, President of the Stern Group, Inc., for their guidance and leadership. We are also indebted to Elliot Schwartz, Vice President and Director of Economic Studies at CED; Van Doorn Ooms, CED's Senior Vice President and Director of Research; and Isaiah Frank, CED's Advisor on International Economic Policy, for their contributions, and to Tarek Anandan and Michael Berg for research assistance.

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Executive Summary

This paper addresses U.S. trade policy and the need for new authority to negotiate trade agreements. The time has come for the United States to renew its commitment to the global trading system and to lead the international community in resolving issues that block the path to more open markets and greater prosperity. While other countries have signed preferential bilateral and regional trade agreements, the United States has sat on the sidelines in recent years. Trade promotion authority is an important signal to other nations that the United States is committed to the multilateral trading system and to negotiations to lower trade barriers further. The U.S. Congress should therefore grant the President the trade promotion authority he needs to negotiate new trade agreements.

Open markets for trade and investment significantly improve economic well-being both in the United States and in other countries. The reduction of trade barriers has played a key role in helping countries around the world to increase economic growth and reduce poverty. In the United States, enhanced access to global markets has meant better jobs, higher wages, and improved living standards.

Poverty, harsh working conditions, and environmental problems are prevalent in low-income countries and in sectors of the developed world. In every country that opens its borders, the issues of trade and foreign investment are superimposed on these existing problems and draw public attention to them. But while trade and investment are not universal remedies for social ills, they are not the cause of those endemic problems. Indeed, trade and investment offer low-income countries, especially those with sound domestic policies, a major opportunity to reduce those

problems through economic development. Developing economies open to trade and investment that follow sound economic policies typically enjoy higher wages and significantly better labor and environmental standards. Experience shows that living conditions in developing countries improve and labor and environmental standards are raised as income rises.

To break the domestic political stalemate that has emerged and move forward, the United States must take the lead in promoting solutions to economic and social problems that many trade opponents associate with trade and foreign investment, notably unsatisfactory labor and environmental conditions. Even if a country pursues all the appropriate policies—open trade, sound macroeconomic policies, good governance, and sound safety-net programs—social improvements take time. In addition, economic development may highlight and even temporarily aggravate existing problems. Thus, the United States, working through appropriate international institutions, should fulfill President Bush's pledge that, "Our commitment to open trade must be matched by a strong commitment to protecting our environment and improving labor standards." Furthermore, as CED has observed in previous policy statements, we need to do more at home to ease the economic adjustment of the small proportion of American workers who sustain material and enduring losses from job displacement.

CED specifically recommends the following:

- **The President and other government and private-sector leaders should visibly and vigorously communicate the vital role played by global trade in increasing stan-**

dards of living at home and abroad. They should also make clear and effective their support for continual worldwide improvements in labor and environmental conditions and the reduction of poverty. In this context, Congress should grant the President authority to negotiate new trade agreements under fast-track rules.* (See page 13.)

- **Formulation of policies for trade, labor, and environmental issues, and enforcement of agreed actions, should lie within the purview of the relevant national and international bodies. Trade issues belong in the World Trade Organization (WTO), labor issues in the International Labor Organization (ILO), and non-trade environment issues in the United Nations Environment Program (UNEP) and similar forums. To deal effectively with such issues, those agencies should be strengthened and supported through U.S. leadership and funding. (See pages 13-14.)**
- **International economic organizations should increase their openness and transparency to the public. In particular, the WTO dispute-resolution process should be opened to public scrutiny. (See page 14.)**
- **Developing countries should be allowed to pursue their own labor and environmental standards, which are likely to rise as their incomes rise. However, they should be encouraged to enforce those standards, to raise them to internationally recognized levels, and to adhere to relevant agreements. Trade agreements should incorporate the principle that countries will not weaken their existing labor and environmental rules or their enforcement to gain an advantage in**

international trade or investment. (See page 14.)

- **Specialized international agencies (ILO and UNEP) should strengthen the promotion of internationally recognized standards to which countries can subscribe, taking account of differences in levels of development. These standards should be enforced by means that do not diminish trade and its potential to support economic development. Enforcement could proceed first through public disclosure and then through a menu of economic remedies, which should include positive inducements as well as disciplinary measures such as fines. (See pages 14-15.)**
- **Policy makers should avail themselves of opportunities, such as those presented by the bilateral agreement with Jordan, negotiations with Chile and Singapore, and multilateral negotiations for a Free Trade Area of the Americas, to take incremental and experimental steps to resolve policy conflicts between trade, labor, and environmental issues. (See pages 15-16.)**
- **To reduce worker anxiety about economic change, the United States should adopt a modest system of temporary supplemental wage and health assistance along the lines suggested by the U.S. Trade Deficit Review Commission. The program should be open to workers who are “displaced” based on Department of Labor criteria and re-employed at less than their previous wage. It should be capped at an appropriate level and percentage of lost income. It should apply to all job displacement, not just that related to trade. The system should be administered by the states and funded from general federal government revenues rather than by payroll taxes. (See pages 16-19.)**

*See memorandum by COLETTE MAHONEY (page 21).

Introduction



International trade and investment improve global economic welfare through specialization, increased competition, economies of scale, and smoother economic adjustment. Changes in the technologies of communication, transportation, and information processing have made the world seem smaller and have accelerated the effects of economic decisions. The case for global economic integration based on policies that support open markets for trade and investment is formidable and, to us, compelling. This paper addresses one aspect of globalization, international trade. International trade and trade negotiations have become targets for those who either wrongly perceive them to be detrimental to labor and the environment or significantly undervalue their contributions to social improvement. In addition, some opponents of trade think that dampening economic competition would better advance their social concerns.

We share many of the same social goals and objectives as the opponents of trade. As business and educational leaders, we have long recommended policies to promote economic growth with greater opportunity and an improved quality of life for all. More open and competitive markets advance those goals. High employment and increasing incomes are much more likely to be achieved by a country that has markets open to international competition than by one that impedes economic progress by protecting domestic firms. Social goals of freedom, self-determination, equal opportunity, and enhanced quality of

life are more likely to be fulfilled in a country that allows its citizens the right to choose among all of the world's products and services than one that narrows the set of choices by imposing rules to favor domestic producers. Those concerned that foreign nations or international organizations will somehow gain an ability to undermine domestic policies or dictate the scope of U.S. laws and regulations, including those protecting domestic labor and environmental standards, should recognize that international trade and the rules that govern it cannot in themselves have that effect. Only the United States has the power to alter its own domestic laws and regulations.

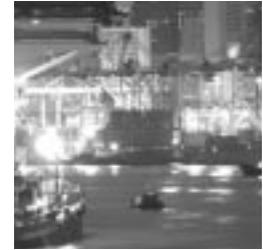
President Bush has called for authority to negotiate new trade agreements under so-called fast-track authority (now renamed "trade promotion authority"), a legislative procedure that allows the President, after many consultations with public advisory commissions and congressional committees, to submit a bill to the Congress for an up or down vote (without amendment). Trade promotion authority is an important signal to other nations that we are committed to the multilateral trading system and to successful and productive trade negotiations.

International trade and the institution that governs it, the World Trade Organization (WTO), have become contentious political issues in the United States. Over the last several years, disagreement over the relationship of labor and environmental concerns to trade has stymied efforts to authorize trade

negotiations and fast-track procedures. While other nations have benefited from the pursuit of bilateral and regional free trade agreements, the United States has not. Although we believe strongly that the case for a liberal trade policy can be made on its own merits, we recognize that we must also demonstrate more clearly how trade interacts with and improves labor and environmental conditions and engage in constructive dialogue with those who believe otherwise.*

*See memorandum by HARRY L. FREEMAN (Page 21).

The Benefits of Trade and Its Relationship to Social Concerns



We support expansion of trade through multilateral negotiations such as those under the auspices of the World Trade Organization (WTO) because of the clear and convincing evidence that trade is good for both the United States and the countries with which we trade. The multilateral trading system under the WTO and its predecessor, the General Agreement on Tariffs and Trade (GATT), has played a key role in reducing trade barriers, strengthening the rule of law, and encouraging economic development in low-income countries. We recognize that many other issues related to trade and economic growth remain to be addressed, including the need for improvements in the ways both national and international institutions function (including their transparency), the treatment of international labor and environmental concerns, and the ease with which adjustment to all sources of economic change occurs within the United States. The United States is the world's largest economy and leading trader in goods and services, and the stakes for U.S. businesses, workers, and consumers in the global economy have never been greater.

The United States must lead the international community in resolving the issues that are blocking the way toward more open markets and greater prosperity. That effort requires rebuilding a domestic constituency for liberal trade based on a better understanding of the value to the United States of the global trading system.

THE ECONOMY OVERALL

The benefits of trade in general and trade across political boundaries in particular have been recognized for a very long time. The principles of specialization and comparative advantage are well known and verified by experience. Each of us does not have to produce all of the goods and services he or she consumes. Neither does each country need to be self-sufficient. Differences in resources and the capacity to use them make it most efficient for workers, businesses, and nations to specialize in the activities that they do best and trade with others for remaining needs. The output that can be generated through trade among specialized economies is substantially greater than if nations were to attempt to be self-sufficient. Perhaps most important, global competition promotes efficiency, innovation, and capital investment as domestic firms strive to become more efficient than their foreign rivals. Global competition has driven advances in technology and improvements in productivity, which underlie increases in incomes and higher standards of living.

In the last 50 years, U.S. barriers to international trade have fallen steadily. Today, most imports either enter the United States duty-free or are subject to very low tariffs. Other nations have lowered their barriers as well. But much more remains to be done. The developing countries in particular have much to gain from expanding trade and gaining greater access to developed country markets. Because trade benefits both parties,

another country's gain is not our loss. We also are better off when other countries prosper.

Expanded trade and economic growth, which have gone hand-in-hand, have directly benefited both consumers, who have gained a wider selection of goods and services at lower prices, and producers, who have expanded markets, lowered costs, and increased incomes. The direct advantage of trade to workers in the United States is evident in the wage premiums that workers in export industries earn; workers in jobs related to exported goods earn approximately 15 percent more on average than other workers.¹

The value of trade is clear to the developing countries; over 100 of them have chosen to become members of the WTO, and another 29 countries, including China and Russia, seek membership. Developing countries have learned through experience that economic growth comes through expanded trade. Empirical research in the past decade has shown a positive and strong association over very long periods between openness to trade and economic growth.² Although many factors are at work, countries that are strongly outward-oriented have had significantly higher rates of growth in the past quarter-century, while the most inward-oriented countries have suffered real income losses. In countries that grew rapidly, openness to trade was an important element in a comprehensive set of policies, including investment of a high percentage of GDP, maintenance of macroeconomic stability, and strengthened political institutions to promote good governance and

1. Council of Economic Advisers. *Economic Report of the President: 1998*. Washington, D.C.: Government Printing Office. February 1998. p. 241.

2. A good summary of the link between trade and growth, including a bibliography of research on this topic can be obtained at <www.worldbank.org/wbiep/tradeTradePolicy.htm>. See also International Monetary Fund. *World Economic Outlook*. Washington, D.C.: IMF. May 1993. p. 75.

root out corruption.³ Without sound economic policies and domestic institutions, the potential benefits of increased trade would likely go untapped.

Foreign trade and investment have played key roles in helping less-developed nations emerge from poverty and improve living conditions. Trade and investment give such nations access to goods and services, such as intermediate inputs and business services, that they would otherwise lack or have available only at much higher cost. Most significantly, the same forces of competition that benefit the advanced economies apply with at least equal strength in less developed economies; small nations in particular can gain from economies of scale due to the availability of export markets. Moreover, openness to the world economy increases the incentives for developing countries to create more transparent political processes, establish more predictable and reliable legal systems, clean up government corruption, and invest more in education, health care, and the environment. Those steps help make a country more attractive to foreign investors and its industries more efficient and competitive in world markets.

ECONOMIC AND SOCIAL CONCERNS

Trade and foreign investment have become the focal points for complaints about economic and social conditions domestically and worldwide. Although trade is a powerful economic force, it is not the source of poverty and unsatisfactory labor and environmental conditions. These problems are very real, but reducing trade will not resolve any of them and, in fact, is likely to exacerbate them. In the United States, skill-biased tech-

3. Rodrik, Dani. *The New Global Economy and Developing Countries: Making Openness Work*. Overseas Development Council. Policy Essay Number 24. January 1999.

nological change is a far greater source of economic dislocation and income disparity than is trade. In the developing countries, poverty is endemic. The economic and social changes associated with expanded trade may temporarily aggravate such problems but, in time, those changes will both reduce poverty and improve social conditions. In most cases, these issues should be viewed in the overall context of economic development, of which trade is only a part.

Workers and Working Conditions

Two distinct issues dominate concerns for workers. First, a significant issue in the United States is the adjustment of workers to changes in market conditions outside their control. This concern extends to worker displacement generally, not only that related to trade. Second is the problem of labor conditions and the setting and enforcement of labor standards in developing countries. This issue relates to both the specific conditions of work in low-income countries and the effect that those conditions might have on workers in the United States.

Domestic adjustment. Although trade benefits most workers and leads directly to a rise in average income, it affects different workers differently. Nor are the benefits always immediate or achievable without costs. Some workers lose their jobs in the short run, and many have to make new investments in their education or skills training before they find reemployment.

In the large and dynamic U.S. economy, enormous numbers of jobs are both created and destroyed by economic change. In 2000, the U.S. economy employed about 135 million people, 20 million more than ten years earlier. The average net addition of about two million jobs per year during the 1990s, however, occurred in a labor market in which, on average, approximately 16 million jobs disappeared while 18 million new jobs were created each year. Job change is far

more common than most people realize. In 2000, one-quarter of all workers had been with their current employer 12 months or less, and the median tenure of employment was about 3.5 years.⁴ Over one-third of all workers—nearly 45 million individuals—either change employers or enter or leave employment each year, excluding changes like short-term layoffs that are reversed during the year.⁵ International trade is but one of many causes of such economic change in the United States. Technological change, which shifts the demand for labor in the direction of high-skilled workers, causes a much larger percentage of such job change.⁶

A little more than 18 percent of the workers whose jobs disappeared, or an estimated three million people annually, are classified by the U.S. Department of Labor as “displaced workers—those who lost or left jobs because their plant or company closed or moved, there was insufficient work for them to do, or their position or shift was abolished.”⁷

For some displaced workers the process of finding reemployment is slow, difficult, and costly. Data on the reemployment of displaced workers show that about one-quarter of workers displaced from all causes are unable to find reemployment within two years of losing their job.⁸ Less-educated and older workers are particularly affected by job

4. U.S. Department of Labor, Bureau of Labor Statistics. “Employee Tenure in 2000,” BLS Press Release. August 29, 2000. <stats.bls.gov/newsrels.htm>.

5. See Committee for Economic Development, *American Workers and Economic Change*, 1996, p.5. Based on research by Davis, Stephen J. and Haltiwanger, John. “Measuring Gross Worker and Job Flows.” National Bureau of Economic Research. Working Paper Number 5133. May 1995.

6. See Council of Economic Advisers, *Economic Report of the President: 1998*, p. 244.

7. The annual stock of displaced workers is about eight million people who were separated from their jobs sometime in the previous three years.

8. U.S. Department of Labor, Bureau of Labor Statistics. Displaced Worker Survey. February 2000. <ferret.bls.census.gov>.

displacement. Nearly two-thirds of those who find reemployment accept a lower initial wage than in their previous job. Reemployed manufacturing workers, for example, lose an average of 16 percent of weekly earnings.⁹ Moreover, when large numbers of workers become unemployed and plants or entire businesses close, the consequences for local communities can be severe. Economic losses easily spill over to businesses that rely on the local base of commerce, and government resources become strained as demands on social services increase while revenues are falling.

In a growing economy, those losses are more than offset by gains elsewhere, and measures to limit the losses by protecting markets and impeding adjustment reduce those gains. The unemployment rate in the United States fell from 7.5 percent in 1992 to 4.0 percent in 2000 despite technological changes, corporate mergers, and trade expansion that displaced millions of workers. When a firm is unable to compete successfully in the marketplace, it may lay off workers or go out of business completely. When that happens, the labor and capital that are released can be redeployed to more valuable activities. This process of resource redeployment is essential to economic growth. In the end, it leads to better jobs in more successful industries and higher incomes with better standards of living. These gains for the society at large make it both equitable and possible to assist those displaced by economic change.

Standards in developing countries. Developing nations gain from trade through both increases in income and improvements in labor conditions. In fact, the relationship between trade, income, and labor conditions

9. Kletzer, Lori and Robert Litan. "A Prescription to Relieve Worker Anxiety." *Brookings Policy Briefs*. Number 73. March 2001.

is strong. Although working conditions in export-related industries in developing countries appear harsh by U.S. standards, jobs in the export sector generally pay better and offer better working conditions than alternative employment opportunities, especially in subsistence agriculture and services.¹⁰

Income growth goes hand in hand with improved working conditions, including a shortening of the workweek and easing of the most onerous forms of work. As nations become wealthier, their children go to school, their working conditions improve, and the social standards that govern labor and employment norms rise. Employment of children (aged 14 and under) is most prevalent in the least developed economies; it is as high as 49 percent in Burundi which has a GDP per capita of \$105, and relatively rare in economies where GDP per capita exceeds \$5000.¹¹ Since opening its economy to international trade, China has experienced a rate of decline in child labor, especially in export industries, faster than it had previously and faster than other developing countries.¹² Research on the relationship between economic development and working conditions shows that in the high-growth East Asian countries (Hong Kong, South Korea, Singapore, and Taiwan), working conditions—measured in terms of unemployment, composition of employment, real earnings,

10. Aggarwal, Mita. *International Trade, Labor Standards, and Labor Market Conditions: An Evaluation of the Linkages*. Office of Economics Working Paper 95-06-C. Washington, D.C.: Office of U.S. International Trade Commission, 1995, as cited in Carnegie Endowment for International Peace and Inter-American Dialogue. "Breaking the Labor-Trade Deadlock." *Carnegie Endowment Working Papers*. Number 17. February 2001.

11. Krueger, Alan B. "Observations on International Labor Standards and Trade." National Bureau of Economic Research. Working Paper Number 5632. June 1996; Source of Burundi GDP calculation: World Bank. World Development Indicators Database. 2000. <www.worldbank.org>.

12. Lindert, Peter and Jeffrey Williamson, "Does Globalization Make the World More Unequal?" National Bureau of Economic Research. Working Paper Number 8228. April 2001. p. 30.

and absolute poverty—generally improved as income grew.¹³

One motivation for concern over labor standards in developing countries comes from those in the United States and other developed countries who fear that lax standards in low-wage countries will undermine conditions in their own countries. Some cite evidence of actual or threatened plant closings to support their concerns. Employers do, of course, sometimes close domestic plants and open foreign ones. However, a great many factors go into such decisions, and the outcome is rarely determined by labor standards. Most significant are wage and productivity differentials, transportation and communication costs, proximity either to fast growing markets or materials used in production, natural advantages such as nearness to a harbor, and conditions of governance. In addition, most foreign investment by U.S. companies goes to other advanced nations, which have labor and environmental standards comparable to those in the United States, if not more stringent. Neither economic theory nor empirical investigations indicate that U.S. workers as a whole would be significantly helped by the adoption of higher labor standards in developing countries.¹⁴

Rising incomes, better working conditions, and more responsive political institutions make possible the institutionalization of higher labor standards. The International Labor Organization (ILO) has played an important role in establishing a set of core

13. See "Promoting Worker Rights in Developing Countries: U.S. Policies and Their Rationale." Congressional Budget Office. April 1997. p. 16, and Fields, Gary. "Employment, Income Distribution and Economic Growth in Seven Small Open Economies." *Economic Journal*. Volume 94. Issue 373. March 1984. pp. 74-83.

14. See, "Promoting Worker Rights in Developing Countries: U.S. Policies and Their Rationale," p. 11; and in particular, Krueger, "Observations on International Labor Standards and Trade."

labor standards that have been recognized by many countries. These standards have helped countries to institutionalize safeguards for workers. The standards focus on four topics: freedom of association and collective bargaining, elimination of forced or compulsory labor, abolition of child labor, and elimination of employment or occupational discrimination. Each of the core standards is comprised of two fundamental conventions. We recognize that ratification by itself does not guarantee that a country will enforce a convention. Neither does its failure to ratify mean that a country, such as the United States, does not maintain standards as least as high as those embodied in the convention. Nevertheless, ratification does signal some degree of acceptance of a convention and recognition of its value. As of April 2001, 43 nations, including 31 non-OECD economies, had ratified all eight of the fundamental conventions, and an additional 50 nations had ratified seven.¹⁵

The Environment

Environmental concerns about international trade take several forms. Some are focused on economic growth, which often uses more raw material inputs and creates more by-product outputs. Another concern, similar to that regarding labor conditions, is that competition among countries to attract investment and expand exports will drive a "race to the bottom" that reduces environmental standards worldwide. Finally, many environmentalists have expressed the concern that the WTO dispute-resolution process undermines environmental regulations when they conflict with trading rules.

Environmental issues are already recognized by the WTO in several ways, and many

15. International Labor Organization. "Ratifications of the ILO Fundamental Conventions." International Labor Standards Department. April 2001. <www.ilo.org>. The United States has ratified two of the fundamental conventions.

environmental agreements recognize the importance of trade. Article XX of the WTO allows restrictions on trade based on “measures to protect human, animal or plant life or health” and “relating to the conservation of exhaustible natural resources.” In addition, specific agreements under the WTO contain environmental provisions, notably the agreements on Technical Barriers to Trade and on Sanitary and Phytosanitary Standards and sections of agreements on agriculture, trade in services, trade-related investment measures, government procurement, and intellectual property rights. Moreover, WTO has established a Committee on Trade and the Environment to investigate the relationship between trade and environmental measures and make recommendations as appropriate. Within the United States, the White House Council on Environmental Quality ensures consideration of the environmental impacts of trade agreements and identifies complementary policies that address trade and environmental objectives.

Economic growth. Environmental issues involve questions of priorities and the timing of costs and benefits. Trade can have a positive effect on the environment over time by facilitating economic development and creating both the income and the institutional structures to address environmental issues. As income increases, the capacity and willingness of societies to sacrifice consumption for environmental protection tends to increase. Higher incomes, better functioning markets, and stronger political institutions improve people’s ability to secure a better environment by purchasing environmentally favorable products and lobbying their governments for improved environmental conditions.

In the short run, however, economic growth can create environmental problems. A growing economy puts pressure on the environment both by using more resources as

inputs in production and by creating agricultural and industrial waste and other by-products. But it is hardly surprising that for millions of people living close to subsistence, environmental protection is of necessity a lower priority than basic food, clothing, and shelter. In our view environmental improvements are more likely to occur—and to occur faster—in a developing economy with growing income.¹⁶

In addition, trade can produce some short-run environmental benefits. Increased trade allows the transfer of environmentally friendly goods and technologies from advanced economies to the developing countries and induces developing countries to produce exports that meet the more stringent environmental standards of the economically advanced countries. Imported industrial equipment and processes can help control the creation of industrial by-products, including waste, water and air pollution, and toxins and hazardous materials. Smokestack “scrubbers” can minimize sulfur dioxide (SO₂) and nitrogen oxide (NO) emissions, and fuel cells and solar power equipment can reduce the use of oil, natural gas, and coal. Trade also makes it easier for developing countries to adopt policies and programs that have been successful in minimizing environmental problems elsewhere. The combination of improved economic policies and the importation of innovative technologies can help address many of the environmental threats faced by developing countries, such as deforestation, over-fishing and -harvesting, and excessive fuel use.

Lowering environmental standards.

Although the claim has been made repeatedly that competition for economic activity

16. Some empirical evidence supports the existence of an “inverted-U” shaped curve, which describes environmental impact as a function of per capita income. See World Bank. *World Development Report: 1992*. New York: Oxford University Press. 1992, and World Trade Organization. *Special Studies 4 - Trade and Environment*. Switzerland: WTO. 1999. pp. 35-46.

leads countries to lower their environmental standards, very little evidence exists to support that contention. As indicated previously, firms locate in specific sites for a variety of reasons. Environmental regulations are a very small consideration. There is little evidence that polluting industries migrate from developed to developing countries to reduce environmental compliance costs, although there are occasional exceptions.¹⁷

Economic integration can be credited, in part, with encouraging greater international cooperation in environmental matters. Nations have gradually become engaged in cooperative multilateral environmental agreements (MEAs), which deal with environmental concerns that transcend geographic boundaries, such as water and air pollution. Over 200 MEAs already exist, including the Montreal Protocol (ozone layer protection), the Basel Convention (transportation of hazardous materials across international waters), and the Convention on International Trade in Endangered Species (CITES).¹⁸ About 20 of these agreements include provisions related to trade, for example allowing a ban on trade in products under the purview of the agreement.

Dispute Resolution. Many of the complaints about the trading system in general, and the WTO in particular, derive from trade

disputes that have involved environmental issues. Objections have been voiced to the results of those disputes, which have undercut some environmental regulations, as well as to the secretive process by which the WTO resolution procedure works. An examination of some of the key cases that have angered environmentalists, notably the U.S. ban on tuna caught in nets that kill dolphins, indicates that the WTO (at that time, the GATT) has accepted the validity of some environmental policies. Specifically, in the tuna-dolphin case, GATT endorsed product labeling to notify consumers that the tuna was “dolphin safe,” although it concluded that U.S. policies discriminated against imports by imposing U.S. regulation of a production process on foreign producers. In this and other cases, the international trade agencies have unleashed a storm of protests by appearing to put international trade rules above domestic environmental policies.

Although international agreements cannot overturn U.S. law, they do create a need to reevaluate laws, such as those in the tuna-dolphin case, in a broader economic context. What was once a settled domestic issue can now be reopened because of a WTO ruling, and political forces can be significantly different when the issue is readdressed. The United States, of course, can choose to ignore a WTO ruling and submit to a trade sanction rather than change its law. However, this option does not change the fact that the political system will be required to choose between the conflicting goals of trade benefits and environmental benefits.

17. World Trade Organization, *Special Studies 4 - Trade and Environment*, p. 5.

18. “Beyond the Agreements: The Environment—A New High Profile.” World Trade Organization. April 2001. <www.wto.org>.

Addressing Trade and Social Concerns



The recent polarization of attitudes toward international trade has stymied efforts to renew the President's authority to negotiate trade agreements and submit them for fast-track approval. That authority is of critical importance because other countries are usually uninterested in negotiating with the United States unless the President has authority to reach agreements that cannot be amended later by the Congress (although they can be voted down). In addition, the lack of such authority puts U.S. negotiators in a weak position, since it reflects a lack of public and congressional support for market-opening measures. Finally, the lack of such authority puts U.S. exporters at a disadvantage in many of the world's markets, since the European Union and others have moved ahead to negotiate preferential trade deals and we have not.

Since the conclusion of Uruguay Round trade negotiations in 1994, over 100 regional trade agreements have been completed. In all, over 130 free trade agreements currently exist, with the United States a member in only two: the North American Free Trade Agreement (NAFTA) and the U.S.-Israel Free Trade Agreement. (A third, the U.S.-Jordan Agreement, still awaits congressional approval.) U.S. exporters and their workers are put at a competitive disadvantage in every preferential trade agreement to which the United States is not a party. In those markets, foreign-based firms gain improved market access, while U.S. producers remain subject to discriminatory practices, including quotas and tariffs.

POLITICAL ENGAGEMENT AND CONSTRAINTS

As a nation, we need to engage the political process more actively to narrow the differences between those who, like us, see trade as promoting economic and social gains, and those who see trade as part of the problem rather than the solution. The constraints imposed by domestic and international political realities, existing law, and international agreements make the achievement of any gains in launching new trade negotiations extremely difficult—but not impossible. The revival of U.S. support for global trade is needed for the United States to reassert leadership in shaping the rules that govern global markets and to benefit from trade liberalizing measures in other countries.

The domestic politics of trade have become extraordinarily polarized. On one side, labor and environment interests have blocked a needed granting of trade promotion authority to the President unless the authorization includes provisions for enforceable labor and environment provisions in the trade agreement. On the other side, free-trade interests, including prominent business groups, have blocked the same granting of authority when it has included such provisions. The result has been a seven-year deadlock between these powerful political forces and a lack of progress in opening a new round of negotiations under the WTO and in concluding a regional pact for the Free Trade Area of the Americas (FTAA).

Internationally, the problem is almost as deadlocked. Developing countries understandably are adamantly opposed to efforts to tie labor and environmental standards to trade agreements or to use trade sanctions as a means of enforcing non-trade agreements. They regard these efforts as a unilateral attempt by the advanced nations to take back or undermine market-access provisions they bargained for and won in the Uruguay Round. If developed-world labor standards were applied to much poorer developing countries, it could create a significant economic disadvantage for them because it would substantially add to their costs of production, making their exports less competitive. In addition, raising the cost of employing low-productivity workers will increase unemployment if employers substitute capital for more expensive labor or if export sales decline. Similarly, imposing developed-world environmental standards can lead to higher costs, reduced exports, and higher unemployment.

Because trade is such a powerful and beneficial economic force, many advocates of various social causes rightly regard the denial of access to markets as a powerful political tool that can be used to further their goals. In the international setting, trade sanctions are often proposed as the “stick” to be used to discipline deviant countries. In particular, some have suggested that developing countries that fail to adhere to international labor standards should be denied the benefits of trade agreements or that new agreements should not be forged with such countries. Since 1984, the Generalized System of Preferences (GSP) program, which significantly lowers U.S. tariffs on imports from the least developed countries, has contained a provision to deny trade preferences to countries that fail to meet certain labor standards. But those preferences are granted unilaterally, which is very different from negotiating rights under an international agreement.

Aside from the direct economic consequences of a sanction, two issues concern us. First, it is often unclear that a trade sanction will achieve the social policy goal for which it is being used. A sanction may impose costs without necessarily producing commensurate benefits. Consider the threat of a trade sanction that persuades a country to increase or better enforce restrictions on child labor. What happens next depends a great deal on other conditions in the country. One should not assume that unemployed children begin going to school; in some cases, they may turn to more hazardous unsanctioned, or even illegal, occupations.¹⁹ In other cases, they and their families may be impoverished because adults are unable to replace the lost income from the child’s work.

Second, we view the use of trade sanctions for non-trade goals as inappropriate for the WTO as an institution. Its value in facilitating trade could easily be lost if we were to overburden it with other goals. This sentiment was put best by its former director general, Renato Ruggiero:

“We cannot—and should not—ask the WTO to also become a development agency, an environmental policeman, or a watchdog for labor and human rights. This organization cannot be allowed to gradually drift away from its trade vocation. It would serve neither the WTO nor any other cause if it were to pretend it could offer solutions to every nontrade issue.”²⁰

A significant problem with trade sanctions is that they can too easily be misused as a protection against competition from imports, rather than for their stated goal. We do not doubt that many supporters of raising labor

19. See Lindert and Williamson, “Does Globalization Make the World More Unequal?”

20. Ruggiero, Renato. “Reflections from Seattle.” Forward to *The WTO After Seattle*. Schott, Jeffrey, Ed. Washington, D.C.: Institute for International Economics. July 2000.

standards in developing countries are motivated by the deplorable conditions under which many workers in those countries toil. We also recognize, however, that some hope that the imposition of higher costs on exports from developing countries will undermine their competitiveness in world markets and benefit competing firms and workers in advanced nations. The suspicion that such standards are being promoted as a means of hobbling foreign competition was aptly captured by the trade minister of Egypt, who recently asked, “Why all of a sudden, when third world labor has proved to be competitive, do the advanced nations start feeling concern for our workers?”²¹

The opposition of developing countries to including social issues in trade agreements and using trade sanctions as an enforcement mechanism is more than a mere negotiating problem. Because the WTO makes decisions by consensus rather than majority vote, the determined opposition of only a few countries will block any consideration of labor and environment provisions in future negotiations. A leading cause of the failure to launch a new round of trade negotiations in Seattle in 1999 was the disagreement between the United States and developing country governments over including labor standards in WTO negotiations. That disagreement was brought to the fore by President Clinton’s statement that he favored both including such provisions in trade agreements and, as a long-term goal, their enforcement through sanctions.²² Developing country delegates voiced strong opposition to that idea. Whatever the wishes of the United

21. Youssef Boutros-Ghali, as quoted in Sanger, David. “A Grand Trade Bargain.” *Foreign Affairs*. Volume 80. Number 1. January/February 2001. pp. 66-67.

22. *Seattle Post-Intelligencer*, December 1, 1999. p. 1, as cited in Elliot, Kimberly Ann, “Getting Beyond No...! Promoting Worker Rights and Trade,” in *The WTO After Seattle*. Schott, Jeffrey, Ed. Washington, D.C.: Institute for International Economics. July 2000.

States or other developed countries with regard to the consideration of labor and environmental standards in the WTO, the opposition of the developing countries makes such an outcome highly unlikely and would effectively preclude new trade agreements incorporating trade sanctions.

PRINCIPLES

In fashioning recommendations for action, we have found it useful to be guided by a set of underlying principles. These are:

- Raising standards of living is a paramount goal. A country with a higher per capita income can solve more of its problems. We should pursue policies that help poor countries grow, not those that protect narrow domestic constituencies at the expense of low-income individuals in developing countries.
- Global trade is an important vehicle for accelerating economic development. We prefer market-opening multilateral trade agreements to bilateral agreements or unilateral actions because multilateral agreements reduce the distortions inherent in multiple preferential arrangements. In addition, the mutual lowering of barriers in a multilateral context helps cement the rights and obligations of countries within the international trading system.
- Negotiated agreements should include some form of enforcement. Like all agreements, trade agreements are essentially contracts; contracts typically require some means of enforcement.
- For the most part, sovereign nations have the right to pursue domestic policies as they see fit. Although we have strong preferences for the direction of policies in such areas as labor rights, education, health, environment, judicial effectiveness, and government corruption, we rec-

ognize the right of individual nations to make their own choices. When the effects of domestic policies spill over to other countries, negotiations should lead to agreement on specific solutions to those problems.

- Enforcement of international economic agreements among sovereign nations need not—indeed, should not—mean the imposition of WTO trade sanctions. Reducing trade hurts both the target country and the country imposing the sanction. Other means of enforcement or inducement to compliance are available.
- The ultimate responsibility for adjustment to changed economic conditions rests with the affected individuals, businesses, and communities. A society that gains from economic change, however, has a collective interest and responsibility in assisting those hurt by such change to adjust to the new conditions.

RECOMMENDATIONS

Raising the visibility and changing the tone of the national discourse on trade would be important steps toward building a domestic constituency for further trade liberalization. Support for open trade has suffered from a lack of sustained high-quality public discussion. The subject has often been reduced to sound bites and videos of street demonstrations. These issues deserve greater attention and more open and forceful debate. Supporters of free trade can improve the tone of public discourse by recognizing the validity of social concerns and becoming more engaged in efforts to improve social outcomes. Groups and individuals who have felt that trade does not benefit them or meet their concerns are more likely to discuss the issues and engage in the legitimate political process if they feel that the political-economic system is responding to their concerns.

Although there is likely to be continuing disagreement about how the political system should deal with social concerns in the context of trade, it cannot be denied that there is an economic connection between those concerns and the trading system. At the recent Summit of the Americas, President Bush took an important step by stating that, “Our commitment to open trade must be matched by a strong commitment to protecting our environment and improving labor standards.”²³ **The President and other government and private-sector leaders should visibly and vigorously communicate the vital role played by global trade in increasing standards of living at home and abroad. They should also make clear and effective their support for continual worldwide improvements in labor and environmental conditions and the reduction of poverty. In this context, Congress should grant the President authority to negotiate new trade agreements under fast-track rules.*** Such authority might be modeled on previous trade acts, which established negotiating objectives that included respect for worker rights and other issues.²⁴

Acknowledging connections among these issues does not mean that they should all be treated in the same forum or under the same agreement. If all issues were negotiated simultaneously under one agreement, progress would never be made. Experience has shown that specific issues can be negotiated and agreements reached under the auspices of specialized international agencies. At present, specialized organizations already exist with missions to advance labor and environmental concerns. **Formulation of policies for trade, labor, and environmental issues,**

23. Reported in Blustein, Paul. “Protests A Success of Sorts: Labor; Environment On Leaders’ Agenda.” *The Washington Post*. April 23, 2001. p. A11.

24. Trade Act of 1974, section 121(a)(4); P.L. 93-618, 88 Stat. 1986; and Omnibus Trade and Competitiveness Act of 1988, section 1101(b)(14); 19 U.S.C. 2901(b)(14), 102 Stat. 1125.

and enforcement of agreed actions, should lie within the purview of the relevant national and international bodies. Trade issues belong in the World Trade Organization (WTO), labor issues in the International Labor Organization (ILO), and non-trade environment issues in the United Nations Environment Program (UNEP) and similar forums. To deal effectively with such issues, those agencies should be strengthened and supported through U.S. leadership and funding. In recent years, the United States has increased its presence in the ILO and has stepped up its funding, in particular for the International Program on the Elimination of Child Labor. At a minimum, we should maintain current funding levels and policy engagement by the United States. An important step for the United States would be the ratification of all of the ILO's core labor standards.

Secrecy engenders suspicion and mistrust. The organizations with responsibilities for international economic issues, in particular, have much to gain by becoming less secretive. Much of the public distrust of the WTO can be traced to the closed nature of its proceedings. While we do not believe naively that openness by itself will lead to an acceptance of the WTO by those opposing it, it can help assuage those concerns and build support in the public at large. **International economic organizations should increase their openness and transparency to the public. In particular, the WTO dispute-resolution process should be opened to public scrutiny.**

Over many years, CED has expressed its support for the development of the world's low-income countries. We have on many occasions recommended that those countries take the necessary steps to improve their economic and political institutions. We have also emphasized the important role that education plays in raising income and the need for developing countries to rid themselves of the pernicious effects of corruption. In

general, developing countries should be adopting internationally agreed upon standards and best practices. In the economic arena, they have strong incentives to do so, since movement towards higher international standards induces increased investment and trade. Our experience has been that better performance in reaching or exceeding market-oriented standards, such as those emphasizing transparency, accountability, and anti-corruption, goes hand in hand with increasing incomes. One of the keys to reaching those standards, however, is that they are voluntary and accepted by the countries themselves as serving their own interests, rather than being imposed by foreign governments. **Developing countries should be allowed to pursue their own labor and environmental standards, which are likely to rise as their incomes rise. However, they should be encouraged to enforce those standards, to raise them to internationally recognized levels, and to adhere to relevant agreements. Trade agreements should incorporate the principle that countries will not weaken their existing labor and environmental rules or their enforcement to gain an advantage in international trade or investment.**

One way to help countries raise their standards is for international organizations to set benchmarks of performance. Benchmarks also provide vehicles for countries to voluntarily pledge their compliance, when they see an advantage in doing so. Similar mechanisms are used domestically by businesses in the United States and other countries to establish codes of conduct or voluntary standards of practice; examples are the Better Business Bureau, Internet privacy codes, or the motion picture and television rating systems. These systems work best when they include some form of discipline or enforcement once an entity has agreed to join and abide by its standards. Such systems can be used in the international arena to help raise

labor and environmental standards.

The ILO in large part does this now through the establishment of standards and conventions, formal monitoring, reporting, and technical assistance. We believe that the ILO holds great promise for helping countries to raise labor standards. Yet, we recognize that the ILO is an imperfect mechanism for positive change and that much more remains to be done to make it effective.

The example of ILO's efforts to deal with Burma is instructive.²⁵ In 1996, worker delegates of the ILO filed a complaint regarding a longstanding problem with forced labor in Burma, and the ILO began an investigation. Attempts to resolve the problems directly with the government of Burma initially failed. However, after the ILO threatened a prohibition of technical assistance and banned Burma from ILO meetings, its responsiveness improved. Burma has since opened its discussions with the ILO and has shown an interest in improving its standards. The progress made in this case is encouraging. Nevertheless, it also reveals some problems. Progress has been slow and limited, partially because countries have been unwilling to implement direct measures against Burma, but also because the threat of external force rarely compels a nation to make domestic policy changes that it would not otherwise make based on internal considerations.

Specialized international agencies (ILO and UNEP) should strengthen the promotion of internationally recognized standards to which countries can subscribe, taking account of differences in levels of development. These standards should be enforced by means that do not diminish trade and its potential to support economic development. Enforcement could proceed first through

25. For more on the Burma case, see Elliot, Kimberly Ann. "The ILO and Enforcement of Core Labor Standards." Institute for International Economics. April 2001 update of Policy Brief No. 00-6. July 2000.

public disclosure and then through a menu of economic remedies, which should include positive inducements as well as disciplinary measures such as fines.²⁶ Some attention has been directed recently to a variety of options that could substitute for trade sanctions to enforce international agreements. Fines are incorporated into the NAFTA side agreement on labor and a similar agreement between Canada and Chile. A variety of options are available to implement a fine-based enforcement system; for example, fines could remain within the country and be used for remediation.²⁷ The ILO and other agencies also have the option of providing technical assistance and other forms of positive reinforcement to induce compliance rather than coerce it.

A complementary path to raising labor and environmental standards is to engage in an incremental strategy of trial and experimentation. In addition to testing the efficacy of various approaches to the problem, such a strategy could help build good will and confidence on the part of participants. That is one of the aims of a proposal by the Trade and Policy Group of the Inter-American Dialogue (IAD) and the Economic Reform Project of the Carnegie Endowment for International Peace (CEIP).²⁸ (See box, "Breaking the Labor-Trade Deadlock" for a summary of their proposal.) The IAD/CEIP proposal is specifically aimed at breaking the policy logjam in the FTAA negotiations. If successful, the approach could be extended to other

26. Individual countries, including the United States, always retain the ability to act unilaterally when their national interests justify it. Such unilateral actions differ from measures that might be taken by international agencies to enforce multilateral agreements.

27. See Elliott, Kimberly Ann. "Fin(d)ing Our Way on Trade and Labor Standards?" *International Economics Policy Briefs*. Number 01-5. April 2001. <www.iie.com/policybriefs/news01-5.htm>.

28. Carnegie Endowment for International Peace and Inter-American Dialogue. "Breaking the Labor-Trade Deadlock." *Carnegie Endowment Working Papers*. Number 17. February 2001. <www.ceip.org/files/Publications/wp17.asp>.

BREAKING THE LABOR-TRADE DEADLOCK

Summary of a Working Paper of the Inter-American Dialogue and the Carnegie Endowment for International Peace

The current stalemate preventing the advancement of the trade agenda results from disagreements over the role that internationally recognized core labor standards should play in trade negotiations. Some groups in the developed nations want the linkage between labor issues and trade to be recognized and demand mechanisms, such as trade sanctions, to ensure that core labor standards will be enforced in all countries. Developing countries, however, oppose bringing labor issues into trade agreements and fear that trade sanctions will be improperly used as protectionism. A new approach would be to create a system capable of improving the coverage and enforcement of internationally recognized core labor standards without resorting to the use of trade sanctions.

The IAD/CEIP has proposed a model that separates the discussion of labor issues from trade negotiations. The plan, which could most easily be implemented by the FTAA countries, would center on the creation of a discussion/negotiation process among the nations' labor ministers. The group would examine the treatment of labor standards in the hemisphere and, in time, begin a series of negotiations on labor issues, which could be conducted in parallel with the FTAA process. By delinking the labor issue from regional trade negotiations, more rapid progress could be achieved on both fronts.

The IAD/CEIP proposal would expand the authority of the group of labor ministers established at the 1998 Summit of the Americas Meeting in Santiago to include analysis of the promotion and enforcement of labor standards in the hemisphere and possibly the implementation of such standards throughout the hemisphere. Initially, the group could create three study areas: private-sector remedies, technical assistance and transparency measures, and the examination of active labor market policies. They could then use their study groups' results to conduct negotiations aimed at securing adequate coverage and enforcement of internationally recognized core labor standards.

The Western Hemisphere would seem to be an ideal trial area. On one hand, because of similar constitutions, societal ideas, and open-market economies, the FTAA nations might be more capable of generating rapid results. At the same time, because the group includes countries that have been highly involved on opposite sides of the labor debate (namely the United States and Brazil), its results would not be weighted towards either the developed or developing nations' interests. If successful, the process could serve as a building block in efforts to establish worldwide consensus on the appropriate enforcement of internationally recognized core labor standards.

arenas. In brief, it calls for the establishment of a process of analysis and negotiation over internationally recognized core labor standards in the Western Hemisphere in parallel with the FTAA trade negotiations. Consistent with CED's recommendations above, the IAD/CEIP proposal would not use trade sanctions to enforce a labor standards agreement, but would allow the use of monetary fines.

Policy makers should avail themselves of

opportunities, such as those presented by the bilateral agreement with Jordan, negotiations with Chile and Singapore, and multilateral negotiations for a Free Trade Area of the Americas (FTAA), to take incremental and experimental steps to resolve policy conflicts between trade and labor and environmental issues.

Economic progress depends on the capacity of labor and capital to move to new activi-

ties that can realize the opportunities created by new technology. Society as a whole gains from such mobility, but the reallocation of labor entails costs that are largely borne by displaced workers. A portion of these costs should be borne by society, both as a matter of equity and as a pragmatic necessity for alleviating worker anxieties that could block market liberalization.

A temporary supplemental wage and health assistance program, such as the “wage insurance” program recently suggested by a bipartisan blue-ribbon panel investigating trade issues, could go a long way towards both providing an increased incentive for displaced workers to find reemployment and overcoming some of the anxiety-based resistance of workers to the causes of economic changes.²⁹ The U.S. Trade Deficit Review Commission has called for Congress to address the “broader costs of job displacement,” including reducing the earnings loss created when new jobs initially pay less than previous jobs, and noted that “wage insurance is one such option.” In the view of the Commission and others who have examined wage insurance, an advantage is that it can be structured to encourage displaced workers to accept new jobs more rapidly even if the wage is lower than in former jobs.³⁰ In addition, it provides workers of different ages benefits that are related to the stages of their

29. See U.S. Trade Deficit Review Commission. “Worker Adjustment Assistance.” *The Trade Deficit: Causes, Consequences, and Recommendations for Action*. Washington, D.C.: GPO. October 2000. pp. 161-176. The bipartisan panel was chaired by Murray Weidenbaum and included, among other members, the current U.S. Trade Representative, Robert Zoellick.

careers. Younger workers may be provided an incentive to return to work promptly, where they can receive valuable on-the-job training, whereas older workers may be provided a less difficult transition to retirement. The Commission cautioned that careful attention should be given to containing the costs of a wage insurance proposal and to possible adverse incentive effects that often arise in insurance programs. One prominent proposal for wage and health insurance is designed to maximize coverage for those most in need while containing costs and minimizing adverse incentives. (See box, “Wage and Health Insurance: Addressing Worker Anxiety.”) **To reduce worker anxiety about economic change, the United States should adopt a modest system of temporary supplemental wage and health assistance along the lines suggested by the U.S. Trade Deficit Review Commission. The program should be open to workers who are “displaced” based on Department of Labor criteria and reemployed at less than their previous wage. It should be capped at an appropriate level and percentage of lost income. It should apply to all job displacement, not just that related to trade. The system should be administered by the states and funded from general federal government revenues, rather than by payroll taxes.**

30. An experimental program of a similar type in Canada demonstrated the feasibility of the concept, although the impact of the program on mobility was small. This small effect may be related to the fact that the program was designed as an add-on to Canada’s relatively generous long-term unemployment compensation program.

WAGE AND HEALTH INSURANCE: ADDRESSING WORKER ANXIETY

Summary of a Proposal by Lori Kletzer and Robert Litan^a

Wage and health insurance has been proposed to share the costs of economic change incurred by displaced workers and to encourage them to quickly seek reemployment.^b Accounting for a modest increase in the current unemployment rate, the joint programs are estimated to cost roughly \$3.5 billion annually. Some of their costs could be offset if the program replaced specialized adjustment assistance programs for trade and other identified causes of job displacement, such as military base closings.

The Need for a New Program

In addition to the immediate loss of income, involuntary unemployment inflicts costs on workers such as the loss of health insurance and the costs of finding reemployment. Even for those who quickly secure a new job, losses often persist in the form of lower wages. With job loss and turnover increasing as a result of factors such as technological innovation, immigration, and increased foreign competition, the number of displaced workers in the United States exceeded eight million in 1999, even as the economy grew by 4.2 percent per year.^c Unforeseen job loss is particularly alarming to older and unskilled workers, who have been hardest hit. In a slowing economy, these groups will experience even greater job turnover.

Without savings, these workers have few options when unemployed. Unemployment Insurance (UI) provides 26 weeks of cash benefits to workers who are laid off through no fault of their own. Additionally, workers may be entitled to another year of income through the Trade Adjustment Assistance (TAA) program, which was created in 1962 to provide benefits to individuals who were hurt by the nation's trade policy. The program (and its newer counterpart initiated for the North American Free Trade Agreement) is essentially based on providing income support and training to individuals who lost their jobs because of foreign competition.^d Thus, it provides benefits only to individuals who can prove that their job loss resulted from increased imports or a shift of production outside the country and that they are enrolled in a training course. TAA programs are not available to most displaced workers.

In general, these programs reimburse workers for 50 percent of lost income. At the same time, however, they disregard the loss of health insurance, encourage enrollment in training courses that are less valuable than on-the-job-training, and neglect workers who accept jobs at lower salaries. As a result, these programs provide little incentive for workers to actively seek reemployment.

Wage Insurance

Unlike these current programs, wage insurance would provide incentives for workers to quickly seek reemployment, regardless of their new income level. At a modest cost, a wage

insurance proposal would: encourage workers to seek reemployment by paying a fraction of their income loss for a two-year period following the initial date of job loss; provide funds for displaced workers, regardless of the reason for their displacement; and provide a health insurance subsidy for a six-month period or until the date of reemployment (whichever comes first).

Workers accepting a new lower-paying job would receive a fraction of their income loss for a two-year period following the initial date of job loss. Such income, however, would not be paid until a new job is found, thereby encouraging individuals to seek reemployment. At their new jobs, individuals would receive crucial on-the-job-training and thus acquire skills that would make them more productive, and more valuable, in the long run. In addition to its improved system of incentives, the program's non-discriminatory nature is better suited for today's economy than the TAA programs. These single out trade as a cause for action, whereas technological change and immigration are more significant causes of job displacement.

Both the wage insurance and complementary health insurance programs would be paid for out of general revenue and administered through state unemployment offices. To contain costs, wage insurance benefits would be provided only to previously full-time workers who were at their old job for two years or more (about 20 percent of all displaced workers in 1999). Assuming a 50 percent reimbursement of wage losses and an increase in unemployment to the 1997 level, the program would cost about \$3.5 billion, roughly one-sixth the cost of UI.^c Furthermore, the program might replace the TAA programs, whose costs have steadily increased to nearly \$300 million annually, and are expected to exceed \$400 million by 2005.^f

- a. Kletzer and Litan, "A Prescription to Relieve Worker Anxiety."
- b. Displaced workers are defined by the Bureau of Labor Statistics in its Displaced Workers Surveys as those "persons 20 years of age and older who [in the last 3 years] lost or left jobs because their plant or company closed or moved, there was insufficient work for them to do, or their position or shift was abolished."
- c. U.S. Department of Labor, Displaced Worker and Employee Tenure Surveys.
- d. The NAFTA-TAA program was created as a result of the NAFTA Implementation Act of 1993. Workers are eligible for benefits provided certification of loss of job to Canada or Mexico.
- e. Kletzer and Litan, "A Prescription to Relieve Worker Anxiety."
- f. *Budget Options*. Congressional Budget Office. Washington, D.C.: GPO. February 2001. p. 324.

Conclusions



CED strongly supports international economic integration through open markets for trade and investment to improve global economic well-being. The time has come for the U.S. Congress to grant the President authority to negotiate new trade agreements under fast-track procedures. Although we recognize the economic relationship between trade and social goals, such as improving labor and environmental conditions, the World Trade Organization should not become the enforcement mechanism for social priorities that are not primarily related to trade. More progress towards our social goals ultimately

will be made if the United States works diligently through international bodies that are focused directly on achieving gains in these areas. Access to markets should not be used as a stick to impose conditions on the developing countries. Experience shows that conditions in those countries will improve and standards will be raised as their income rises. The surest route to raising per capita incomes in developing countries that follow sound economic policies is through the reciprocal opening of borders to trade and investment.

Memoranda of Comment, Reservation, or Dissent

Page 2, HARRY L. FREEMAN

I strongly support the CED position on trade. However, a few points need more emphasis. By referring questions of labor standards and environmental issues to the ILO and UNEP, and similar international organizations, we must do more than try to improve the power of those institutions. We need to correct the lagging enthusiasm for, say, the ILO and a revamping of its Articles; but we need a linkage of timetables so that a stronger ILO emerges, with U.S. support, no later than the end of a multilateral WTO round. Would those who argue for a stronger ILO accept a bland promise from the U.S. to make it stronger when the U.S. has, as a practical matter, not even supported the organization? We need time frame linkage.

This is a very well-written paper; however, we must find a way to show the public that we are more than “just another business organization arguing for free trade.” Voting to publish it should be a mid point, not the final point.

Pages ix and 13, COLETTE MAHONEY

I approve of the statement on free trade and with the recommendations with *one* exception. I do not agree, and dissent, from the sentence in the first recommendation, suggesting that Congress should grant fast-track authority to the President. I do so for several reasons, not the least of which is that such action will deter the “constructive dialogue” recommended by the statement.

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IW	Institut der Deutschen Wirtschaft Cologne, Germany
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