Incomplete Contracting in International Relations:

Patterns of Regional Integration in Europe and North America

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I. Introduction

This paper offers a theory of incomplete contracting and the transfer of state sovereignty. Complete contracts are agreements that aim to specify and proscribe behaviors for the contracting parties in such a way that covers every contingency. Incomplete contracts leave terms to be specified due to procedural and strategic uncertainty. I argue that incomplete contracts generate endogenous momentum for the expansion of organizational boundaries, and shift bargaining power to the holder of residual rights.

This theory of sovereign transfers draws upon theoretical developments in the field of institutional economics. As economists and, increasingly, political scientists have noted, institutions arise when actors cannot independently reach cooperative arrangements.[1] It does not assume that institutions determine preferences. Indeed, the initial choice for particular institutional arrangements will greatly hinge on the preferences of the agents involved. These preferences are exogenous to the model. However, institutions, once created, provide opportunities and constraints. Rules induce roles.

I intend to illuminate how initial choices for particular institutions in the formative phases of European and North American integration influenced the subsequent political processes in both regions. The paper begins with a review and critique of the Williamsonian theory of vertical integration, and then presents an alternative theory of integration that focuses on the importance of incomplete contracts and property rights arrangements for creating hybrid sovereign

configurations. While the theory arguably has relevance for explaining post-colonial arrangements, overseas basing arrangements, accords on natural resource exploitation, and distinct modes of federalist arrangement, I limit myself here to comparing the process of European integration with that in North America.

II. Oliver Williamson, Specific Assets and Vertical Integration

Williamson's well-known analysis posits that the frequency of transactions and the nature of the assets involved determine the level and mode of governance.[2] Specifically, when transactions are frequent and assets are idiosyncratic or "specific," vertical governance or hierarchy will result.[3] Williamson reasons that hierarchical organizational forms alleviate the hold-up problems generated by relationally-specific exchanges in a manner that cannot be guaranteed by comparable independent actors involved in market-based exchanges.

Applications of the Williamsonian model to various aspects of international relations have yielded significant conceptual breakthroughs. Vertical integration parallels the merging of sovereignties under a new and unified authority structure, i.e., hierarchy. Jeffry Frieden applies the transaction costs model to argue that colonial powers with many site-specific investments, such as mines or plantations, were more likely to opt for direct control and empire, rather than other powers with investors who held more mobile assets such as monetary debt.[4] It has influenced many other political scientists as well.[5]

Although the Williamsonian theory is powerful, it has also been criticized from a variety of perspectives.[6] First, the stark dichotomy between hierarchy and the market insufficiently describes the variety of organizational arrangements and relational contracting forms that fall somewhere in between these poles. In reality, several intermediary forms of relational contracting can provide alternatives to the market/hierarchy dichotomy, as Williamson himself concedes.[7] Some alternate hybrid governance arrangements include reciprocity arrangements, franchising, joint ventures, binding arbitration and quasi-vertical integration.[8] Second, some scholars have argued that Williamson ignores issues of relative power and vulnerability, and that transaction-specificity and frequency of interaction, by themselves, may not determine whether and how governance structures emerge.[9] Third, the ability to engage in iterative games will also diminish the need to fully integrate, as the "shadow of the future" may bring about a stable institutional arrangement based on reciprocity.

Fourth, the Williamsonian model assumes that actors know what their desired relation is going to be and what types of assets will be involved in the future. Although Williamson often highlights frequency and asset-specificity, a third determinative factor, uncertainty, remains poorly specified. In reality, most contracting environments are characterized by a strong degree of uncertainty and potential exogenous shocks that might prevent contracting parties from undertaking costly long-term integration. If this is problematic for the understanding of economic interactions, it is doubly so for states in the

international realm.

Finally, the extrapolation of Williamsonian contracting to international relations and political integration also runs into several obstacles. Unlike firms, political elites do not merely seek to maximize their economic benefits for their states. Governments have many reasons to desire to retain their sovereignty. Even if regional integration might yield significant economic gains,[10] governments will fear usurpation by other more powerful states. National culture and self-identification also form important ingredients of politicians' legitimacy of rule.[11] Moreover, strategic politicians will fear a loss of office or diminishing autonomy.[12] Efficiency gains are thus only one aspect of a politician's considerations or utility.

Consequently, two theoretical issues frame the modification of the model. First, I identify a number of hybrid governance arrangements and organizational forms in corporate governance and in the international system that lie somewhere between the anarchy/hierarchy continuum emphasized by Williamson. Second, I seek to explain how power relations partially determine the institutional choices of negotiating actors and to clarify the subsequent endogenous bargaining processes.

III. An Incomplete Contracting Theory of Hybrid Sovereignty Agreements

Institutional economists, inspired by Oliver Hart, have developed an alternate way of thinking about the organizational boundaries of the firm and the

processes through which governance arrangements emerge.[13] The Hart model builds upon several insights provided by neoclassical theories of the firm, agency theory, and Williamsonian transaction costs economics, and adds the concepts of incomplete contracting and property rights.

The distinction between complete contracts and incomplete contracts reflects the standard distinctions drawn between neoclassical rationality and bounded rationality. Under neoclassical assumptions of rationality, agents choose the best complete contract that is available. Both parties carefully craft an optimal contract that explicitly specifies the rights and obligations that each party would assume in the relationship. The contract would detail what is to be produced, how much is to be produced, by what time, and at what price.

In addition, a truly "complete" contract would also specify certain provisions in anticipation of the circumstances or contingencies that might arise to alter the terms specified above. Up to a certain point, parties could presumably anticipate the routine events or circumstances that might affect the terms of their initial agreement. These contingencies and potential remedies (i.e. price adjustments, arbitration, etc.) would also be included in the initial contract.

By contrast, the incomplete contracting approach assumes that in long-term relationships, the imperfections of the market place will force the parties to renegotiate many aspects of the initial contract. The process of long-term contracting is itself costly and fraught with different types of transaction costs that actors cannot foresee or specify in advance.[14] First, contracting

environments are characterized by a great deal of uncertainty. In a changing and unpredictable world, it is difficult for parties to think of the types of unforeseen contingencies that might arise in the future. Second, it is difficult and costly for parties to negotiate, given the asymmetries of information that might characterize the negotiating environment. Third, even if the parties can successfully negotiate a contract, they must do so in a manner that is readily verifiable to an outside observer or a third-party enforcer such as a court or external arbitrator. These three transaction costs—uncertainty, negotiating costs, and enforcement costs—might prevent the parties from writing an optimal complete contract. In addition, an unpredictable exogenous event might make the fulfillment of the contract impossible on its initial terms. Thus, the resulting "incomplete contract" will provide the starting point but not necessarily the long-term specifics for the relationship between two firms. The omissions, uncertainty, and ambiguities inherent in an incomplete contract might exacerbate the potential Williamsonian hold-up problem.

Incomplete Contracts and Property Rights

A second key concept—the notion of property rights and ownership—can further illuminate the bargaining processes and the full range of institutional solutions to the hold-up problem. Although we are accustomed to thinking about property as embodying exclusive ownership arrangements, the Hart model unbundles the various property rights that govern the ownership of assets. A key

insight of the property rights approach is distinguishing formal ownership from de facto control or "use" value. In general, the property rights inherent to any asset can be disaggregated into two sets of rights: control rights and use rights.[15] Control rights allocate the power to make decisions on how to use an asset, such as the ability to sell, lease, transfer, or even destroy an asset. Control rights also grant the right to transfer any of these formal rights to another party. Use rights, on the other hand, specify the rights to receive the benefits and to incur the costs from the deployment of an asset. In economic settings, such rights are usually monetary and are known as "cash-flow" rights.[16]

In an incomplete contract, the control rights of an asset are particularly important as they govern the residual rights of control to the asset: that is the right to use the asset in any manner beyond what is specified in the initial contract. Thus, control rights within an incomplete contract delineate the potential relational power over an asset.

Residual rights of control are critical in so far as they alter the bargaining power renegotiating parties over the appropriation of ex post surpluses. When contracts are incomplete, the organizational boundaries of the two parties will dramatically affect both the bargaining power and divisions of the ex post surplus in the relationship.[17] In many real world situations, parties that cannot foresee or specify contingencies must write an incomplete contract that they agree to renegotiate at a later point. In a relationally-specific investment, the dynamics of such renegotiations will be determined by which party holds the

residual rights of control as opposed to the use rights or cash-flow rights of the asset. Ownership of these control rights will depend on whether the two parties are independent or integrated within a single organizational entity. Realizations about such variations in ex post bargaining power and surplus divisions will affect each party's incentives when entering long-term relationally-specific investments. These dynamics and incentives help determine the organizational boundaries of the firm.

Explaining the Boundaries of State Sovereignty

The described model has important applications for the study of international relations. But in order to precisely identify the model's theoretical "value-added" and specify concrete hypotheses, we need to be conscientious of both the similarities and differences between economic and political analysis. As David Epstein and Sharyn O'Halloran point out, politics "has no equivalent of the free-market or price-system in economics" and the "correct baseline" for our analysis must be "political efficiencies," not economic ones.[18] In addition, the types of transaction costs involved in certain types of contracts in international relations might be distinctly political, with no obvious economic analogy. For instance, political elites' decisions on integration and decolonization are inevitably influenced by public opinion and the strength of nationalism,[19] geostrategic calculations, susceptibility to electoral pressures and rival political elites,[20] institutional divisions within government and asymmetrically distributed

information,[21] and sensitivities to systemic externalities and concerns about relative gains.[22]

Nevertheless, while there are differences between the dynamics of firms and political actors, both share three common features that justify the application of the incomplete contracting/property rights approach. First, despite the possible variations in their baseline preferences, both firms and political actors share an important structural similarity—they are types of organizations. Both political and economic organizations must organize and perform certain functions and routines that are structurally necessary for the overall operations of their governance structures. Like firms, political actors such as states or international organizations are characterized by both vertical and horizontal boundaries on their activities and functions.[23] Horizontal boundaries delimit the types of activities that organizations engage in, as well as the differentiation between these functions. Vertical boundaries denote the overall scope of authority for any given function, and the point at which institutional authority is limited in any given issue.

Second, bounded rationality characterizes the actions of both economic and political organizations. Like their economic counterparts, political actors must make decisions and pursue goals within the constraints of environmental uncertainty, imperfect flows of information, cognitive limitations and transaction costs. These features are particularly characteristic of the anarchic international system in which no overall governing authority can guarantee orderly exchange.

Indeed, information and uncertainty problems will be virulent given that states, in comparison with firms, are more likely to pursue relative gains rather than absolute gains.[24]

Finally, institutional choice is a feature common to both economic and political organizations. That is, just as firms in the private sector choose from a number of possible governance arrangements, international actors also tend to choose institutional arrangements—in this case various modes of integration and governance—because they represent the best political option from a restricted set of institutional alternatives.[25]

Residual Rights, Third Parties and General Propositions

An incomplete contracting perspective can generate several deductive propositions regarding where the bargaining leverage resides in sovereignty exchange agreements and how such arrangements might develop over the long run.

--Table 1 about here--

Formal integration in the realm of international politics (empire) is often not possible given the long-term uncertainty of the international system, international norms against hierarchy or occupation, and political concerns over ceding sovereignty. Incomplete contracts allow intermediate institutional

arrangements to emerge that are politically preferable to allocating exclusive sovereignty over an asset or function to a single political actor (G1). [26]

Sovereignty can be divided into "control rights," the formal ownership and right to transfer or sell an asset, and "use rights," the right to derive the benefits and incur the costs from using the asset. Contracts allow a host country to grant residual rights of control to a foreign power or, conversely, allow the host country to maintain these residual rights for itself (allocation with national residual rights). Additionally, states can transfer decision-making or judicial authority to a third party or supranational body. International arbitration can range from a private ad hoc arbitrator to a permanent supranational body or legislative authority.[27]

While mixed governance arrangements can help states overcome high transaction costs, the presence of relationally-specific assets will especially necessitate that states adopt hybrid governance structures (G2). In addition to their strategic and possible commercial value, fixed assets such as canals (Panama, Suez) and access ways, mines and oil wells, and basing installations have a high political and/or national symbolic value. Under strict Williamsonian logic, vertical integration and hierarchy will be required to govern these assets.

In the realm of international politics, however, their exclusive ownership by one contracting country would impose significant, and in some cases unacceptable, political costs on the other contracting party or even third parties.

By splitting or sharing sovereignty, states can avoid exclusively assigning specific sovereign assets to one party and, in certain contentious cases, can even avoid conflict.

Bargaining Leverage

Incomplete contracts generate potential rents and surpluses that can be appropriated by actors who hold the residual rights of control to an asset (B1). International actors who own the residual rights of control will use the full extent of the bargaining power afforded to them. In bilateral settings, such as decolonization negotiations or military basing agreements, this bargaining leverage may even be more important than the relative power capabilities of the contracting parties. Thus, even though a country may possess significant military capabilities, it will still be at a disadvantage in negotiations if it lacks these residual rights. This was the situation in which many former colonial powers found themselves when initial decolonization agreements were revisited, and this dynamic has also characterized base negotiations between the United States and many of its considerably weaker military base hosts. Of course power asymmetries are not insignificant. However, in complete contracts power asymmetries are dealt with by careful specification of the actual terms of the agreement. With incomplete contracts, the holder of residual rights will have the bargaining advantage even if the distribution of power does not change over time. Thus, the ex post bargaining power that flows to the holder of residual

rights has an independent and significant effect on the contours of the renegotiated settlement.

It is, furthermore, important to recognize that the logic of incomplete contracting plays out differently across cases of disintegration and integration. In cases of territorial disintegration the question revolves around which state in a bilateral interaction will get the residual rights of control. In the case of regional integration the question is rather how much authority other states, or alternatively, new parties, that is, international institutions, should receive. Should these institutions gain significant residual rights they in effect might become supranational entities. Conversely, if the contracting parties retain the residual rights of control, these institutions are more accurately understood as agents acting on behalf of the principals (the contracting states).

For example, the different allocation of residual rights in the formative phases of the EEC and NAFTA has had profound consequences for their subsequent development. As we will show in chapter 5, by giving residual rights of control to a third party, the bargaining leverage and momentum in the European case shifted to EEC level institutions. In short, the transfer of residual rights to another state or states or, conversely, to a supranational authority, has important implications for how hybrid sovereignty arrangements will evolve.

With incomplete contracts, supranational bodies with residual rights subsequently will attempt to codify and institutionalize these rights. For example, Simon Hix's explanation for the adoption of the Maastricht Treaty shows that the

European Parliament exercised its "discretion through rule-interpretation" to shape the incomplete contract of the constitutional negotiations, thereby managing to delineate and increase its own power vis-à-vis member states, well beyond what these many of the states originally intended.[28] In other words, with the transfer of residual rights to a third party, that entity acquires enhanced bargaining leverage as time progresses.

The Momentum for Sovereign Transfers

When and under what circumstances do incomplete contracts remain stable and when do they tend to become complete contracts (M1 and M2)? As we have argued, because of its unspecified nature and built-in renegotiations, incompleteness also affects the momentum for continuing further sovereign transfers and the bundling and unbundling of assets and functions. All else being equal, contracts that are incomplete must eventually be renegotiated, clarified, and adjusted. This general proposition describes the result of the learning processes that contracting actors will experience between the initial contract t=0 and bargaining point t+1. Upon renegotiation, parties will have improved information about the distributional consequences of the initial agreement as well as a better understanding of previous omissions or contingencies that are critical to the continuation of the institution. Thus, over time, previously incomplete provisions will become increasingly more specified (or complete) and develop the necessary institutional apparatus in order to do so. When sovereign rights among

bilateral contracting parties are split into control rights and use rights, this learning should allow the party with the residual control rights to further constrict the scope of the use rights of an agreement (ceteris paribus).

This natural momentum towards completeness will be enhanced, and thus hybrid sovereignty arrangements will unravel, if alternative contracting parties become available. This logic holds for either of the two parties to the agreement. The foreign power will be less willing to pay for the use rights it is given by the host country, if it sees a cheaper alternative or substitute. But this logic holds a fortiori for the owner of residual rights. In this case, the leverage of the owner of the residual rights will increase even further to the detriment of the possessor of use rights. The entrance of alternative potential partners will allow the owner of residual rights to operate in a competitive market with multiple "consumers" of the good. The residual rights holder will thus ratchet up its demands, and, if possible, try to gain exclusive sovereignty over the governance of the asset or function. For example, prior to the expulsion of the United States from its military base in Uzbekistan in July 2005, Russia signaled that it was willing to enter into a security relationship that would be less intrusive in the internal affairs of Uzbekistan, thereby making its terms more preferable to the authoritarian regime in Tashkent than the mixed messages that had been sent by the United States.[29] Conversely, a lack of alternate contracting partners for the residual rights owner will make continuation of the incomplete contract more likely and the institutionalization of joint gains under such hybrid arrangements a stronger

possibility. In short, absent alternative contracting partners, incomplete contracts should endure as long as they produce joint gains for the contracting parties.

Credibility of Commitment Problems

Given that incomplete contracts are subject to future renegotiations all parties will be concerned with the subsequent distribution of rights and assets (at t+1). Consequently, contracting actors will face credibility problems given the concerns about bargaining leverage and the forward momentum of the agreement.

In bilateral negotiations, such as in decolonization and overseas basing arrangements, the credibility problems will particularly arise for the actor who holds the residual rights. This will be particularly pronounced in cases where the holder of residual rights has ownership over transaction-specific assets but grants use rights to the other actor. The foreign investor of the relationally-specific asset, or the state that is placing fixed assets in forward bases, will want institutional assurances that the holder of the residual rights (the host) will not renege and engage in hold-up (C1 and C2).

With regional integration agreements the smaller states will be concerned about their ability to influence more powerful economies in subsequent rounds of negotiations. Small states might enter into complete agreements given the ex ante clarity on the distribution of benefits and allocation of assets. However, they will be reluctant to enter into incomplete contracts unless the more powerful

states credibly commit to the agreement by tying their hands and by transferring residual rights to a third party.

However, where residual rights have been transferred to a third-party and the contract remains incomplete, this raises concerns of its own. The contracting states will be concerned that the third party, or supranational body, usurps additional authority and powers. The 2005 votes in the French and Dutch referendums against the new European Union Constitution can be at least partially explained by the inability of either national leaders or EU officials to convince these publics that the proposed expanded EU institutions would in fact be democratic and accountable.[30]

IV. Towards a Causal Model of Governance Structures

Incomplete Contracting as a Dependent Variable: The Choice of Governance structures

Admittedly, the factors that influence actor preferences are largely exogenous to the model. Whether states wish to pursue hierarchy, grant independence, or agree to some hybrid governance form such as regional integration, will depend on a myriad of contextual factors. Preferences will be influenced by changes in geostrategy; previous patterns of interaction; and even technological transformations.[31] In tracing preferences we inevitably must rely on inductive observations of the historical record, and use structured focused comparison and process tracing to substantiate our findings.[32] This does not mean we need to turn our back on deductive theorizing. To the contrary, like the

analytic narrative approach it is possible to combine theoretical tools that are commonly employed in political science and economics, with historical narration.[33]

-here figure 1--

The states in question will engage in calculation of the relative merits of different governance arrangements as suggested by our general proposition (G1). Although preferences are difficult to stipulate ex ante, we may expect that in the case of transaction specific assets, as with territorial partition issues and overseas basing, that each of the parties will prefer to hold the maximum amount of control and use rights (vertical integration).

However, the relative distribution of power will set material constraints on what is feasible. If we are dealing with a declining great power and ascending nationalist movement, the symmetry of power will make it very costly to impose a colonial solution. For example, the French attempt to hold Algeria was prohibitively more costly, than, say, Britain's desire to hold on to Diego Garcia.

Finally, the creation of a particular governance structure will be influenced by the ability of the respective parties to commit. Where reputational or institutional mechanisms exist to counteract the likely consequences of shifts in bargaining leverage and momentum, an incomplete contract will be more readily concluded. The parties to such agreements, of course, will realize where the leverage and momentum of a future contract will trend.

Incomplete Contracting as an Independent Variable: Downstream Consequences of Hybrid Sovereignty Arrangements

From the propositions above, it will also be clear in which direction hybrid sovereignty is likely to develop (ceteris paribus). Even without a significant shift in relative power, the holder of residual rights will gradually expand its authority. In decolonization and basing agreements, the holder of residual rights will seek to gain more control rights and higher rents. Leverage and momentum will be on its side. Thus the incomplete contract will become an obsolescing bargain as time progresses. The unbundled sovereign rights of the host country in the incomplete contract will evolve towards unified holding.

However, this need not occur if both parties still see joint gains from the hybrid sovereignty arrangement, and few alternate contracting parties are available. If states perceive continued joint gains from pooling their security assets, or when they continue to reap benefits from mixing their economic resources, the agreement need not unravel. Given that the temptation to undo the agreement exists particularly on the side of the party which holds the residual rights of control, its perceptions of whether there are such gains and a lack of alternative parties will be particularly crucial.

While the theoretical model has broad applicability to such issues as territorial partition (decolonization), overseas basing, federalist arrangements, and regional integration, this essay limits itself to the case of regional integration

to show how the incomplete contracting argument extends beyond transaction specific contracting.[34]

IV. The Divergent Trajectories of the EU and NAFTA

The EU's evolution, institutions and governance have been extensively analyzed by scholars. For our purposes, I concentrate on the formation of the European Coal and Steel Community (ECSC) in 1951 and particularly on the creation of the European Economic Community (EEC) in 1957. The institutional choices made at that time laid the basis for the extensive sovereign transfers found in the current EU. I then contrast regional integration in Europe with NAFTA, by focusing on the formative phases of both, and clarify why they continue to look so different today.

No institution has blurred the distinction of anarchy and hierarchy more than the EU.[35] Indeed, even when the European Economic Community still stood in its infancy, Jean Monnet proclaimed that already 80% of state policies resided at the European Community level. Perhaps Monnet had reasons of his own to claim the supremacy of community institutions, but it cannot be gainsaid that today, trade policy, labor directives, and fiscal and monetary policies have increasingly come under community discretion. Fifty years after its formation, the European Union shows considerable vertical integration and a high level of supranational decision making over an increased number of issue-areas and functions. Yet the foundational agreement that formed the EEC in the Treaty of Rome in 1957 was remarkably sparse and functioned as a classic incomplete

contract. Andrew Moravcsik thus rightly labels the treaty a "framework agreement."[36] Giandomenico Majone notes that

> A relational contract settles for a general agreement that frames the entire relationship, recognizing that it is impossible to concentrate all the relevant bargaining action at the ex ante contracting stage. The Rome Treaty, for example, may be conceived of as a relational contract.[37]

Consequently, the European integration process exemplifies a case of incomplete contracting with creation of supranational or third party institutions.

NAFTA, although arguably the most institutionalized regional organization after the EU, demonstrates a low degree of transfers of sovereignty to supranational decision making, and a much higher degree of ex ante precision in legislation. Frederick Abbott thus observes:

> NAFTA embodies a high degree of precision and obligation and a moderate degree of delegation of decision making authority. The European Union, in contrast, embodies a high degree of obligation and delegation and a moderate level of precision.[38]

Indeed, European integration from the outset looked markedly different.

The brevity of original treaties, wide in scope but short in details, contrasts with the length of the North American agreement (that originated between Canada and the US in 1987 followed by Mexican accession in 1994), which was far more limited in its aims but highly detailed. The European states embarked on their course with many of the details still to be worked out. Important elements of European integration, such as the Common Agricultural Policy (1962), the relation of European laws to national laws, and regulations on fiscal policy, only emerged years after the 1957 Treaty of Rome.

The level of supranational decision making in the European case was also higher from the outset. The ECSC institutionalized supranationality through the High Commission and was intended to regulate the key coal and steel sectors of the West European economy.[39] Similarly, supranational decision making expanded in the years after the beginning of the Community--even if the organization had to deal with periodic setbacks such as the Luxembourg compromise in 1965 that seemingly gave individual states veto rights. Similarly, the European Commission was created to forward European objectives rather than narrow state interests (the latter were to be represented by the Council of Ministers), and with multiple directorates and large bureaucracy, it lacks any equivalent in NAFTA.

Their respective judicial milieus also differ markedly. The European Court of Justice (ECJ) has taken a key role in codifying these transfers of sovereignty by asserting the supremacy of EU law over national legislation, to the extent that

some observers suggest "governments do not control legal integration in any determinative sense and therefore cannot control European integration more broadly."[40] Arbitration in NAFTA, by contrast, remains an inter-governmental, not supranational, ad-hoc settlement mechanism. Indeed, any claim to the contrary would meet an American constitutional challenge. NAFTA thus constitutes a case of inter-governmental, complete contracting.

What explains the institutional variation between NAFTA and the EU? Simply put, why does the creation of NAFTA look like a set of inter-governmental complete contracts while the creation of the European Community looks like a set of incomplete contracts with transfers to supranational entities? What consequences do these different modes of contracting have on the subsequent institutional development of these organizations?

I focus on three issues. First, I clarify the divergent motives for political elites leading to the formation of the ECSC in 1951, the EEC in 1957, the FTA in 1987, and NAFTA in 1994. As said, admittedly these factors are exogenous to contracting theory proper. For example, some of these variables, as the German reunification question, are clearly idiosyncratic to the case at hand. I do not claim to provide new insights into the European or North American states motivations to contract with each other.[41]

Subsequently, I build on the insights from various authors to show how specific motives influenced rational elites to choose particular allocations of residual rights of control. Using insights following from an incomplete contracting

perspective I show why residual rights were allocated differently in the two cases, and why we would expect the institutional designs to aim at addressing the concerns of the parties ceding such rights.

Finally, I will argue that due to the divergent allocation of such rights at their foundation, the subsequent trajectories of these organizations show marked divergence rather than convergence. NAFTA will continue to resemble clear-in and clear-out specific contracting, little vertical integration, a high degree of ex ante legislation, and only ad-hoc arbitration. The European integrative process, by contrast, will continue to exemplify incomplete contracting, ex-post legislation, and supranational adjudication over sovereign issues and functions.

A Priori Expectations and Varieties of Regional Integration

The nature of the contract and the degree of delegation to a new institutional site will first of all depend on the relative power of the contracting parties. Governments of weak states will be concerned with the exercise of asymmetric power by the more powerful members. But all states will also be concerned that regional institutions might acquire more residual rights as the integration process proceeds. Thus, member states such as Britain are now also concerned with the supranational institutions within the EU decision making process that have residual rights of control and retain the potential for a subsequent unsanctioned expansion in jurisdictional authority.

Power asymmetries, and concerns about expansionist international

institutions, thus influence actors' calculations in deciding whether regional arrangements should take on a supranational or inter-governmental character and whether the agreement should take the form of a complete or an incomplete contract. In bilateral settings, this is relatively clear. The holder of residual rights of control, usually the host country, will have bargaining leverage over the home (or investing) country. With regional agreements, sovereign states initially are the holders of residual rights. They have to decide whether to relinquish residual rights of control over various functions or issue areas (i.e., create a supranational entity) or whether to retain their residual rights (as in an inter-governmental agreement). They also have to decide whether they wish to leave the contract relatively open-ended, and thus subject to ex-post contracting, or write—as close as possible—a complete contract ex ante, that is, a fully-specified contract at the time of signing.

--Here figure 2--

There are thus have four sets of possible outcomes for states that pursue regional economic integration. With inter-governmental complete contracts, states retain residual rights, and the contract is fully specified ex ante. This process describes regional agreements such as NAFTA. An inter-governmental incomplete contract in bilateral cases confers leverage to the holder of residual rights. In cases of regional integration with incomplete contracting, bargaining leverage might flow to the more powerful economies. Post-colonial economic blocs that are established and dominated by the former metropole power would

fit this cell. For instance, this would describe France's role in the CFA Franc Zone in West Africa or Russia's economic dominance of the Commonwealth of Independent States (CIS) and its successor European Economic Community (EUROSEC) customs union.[42] In supranational complete contracting, the states confer residual rights to a new institutional site or international organization, but fully specify the terms of the contract ex ante, with little further development beyond the original terms. The WTO, with its bounded authority over trade issues and regularly used dispute-settlement mechanism does not amount to a full transfer to a third party but goes further than the ad-hoc arbitration that typifies the NAFTA agreement.[43] Although the WTO dispute settlement mechanism is partially based on the earlier NAFTA procedures, it differs in that the WTO has a standing permanent organ--the Appellate Body--whereas NAFTA arbitration panels remain ad-hoc.[44]

Extending even beyond that point, parties may relinquish their independent status and agree to form a new unit with a distinct authority structure, as occurs, for example, when previously independent units merge to form a new state or strong federal union. They may sign a complete contract, fully allocating authority to the new entity, especially if they seek to lock in commitments of other states.[45]

Finally, with incomplete contracting and the creation of supranational institutions, the contract develops dynamically over time with institutional reconfiguration at the supranational level. Which of these is likely to develop in

practice?

Explaining Institutional Choice: Relative Power and Contracting Preferences

If states were to pursue regional integration through incomplete contracts that leave considerable residual rights with the individual members, then the more powerful states will likely seek to reinterpret and redraft the initial terms of the agreement. Less powerful actors that agree to the incomplete contract at time t must fear subsequent defection and the bargaining leverage of the more powerful state at time t+1. Weak states will thus prefer a complete contract making subsequent negotiations less important. We expect them only to consent to an incomplete contract if the larger and more powerful economic actors credibly bind themselves through supranational institutions.

By contrast, a powerful state will be less inclined to favor an incomplete contract with considerable powers vested in supranational institutions. Such an arrangement would diminish the position of the stronger state and subject it to external, third-party legislation and adjudication. That is, if residual rights flowed to a supranational entity, the bargaining leverage of the stronger power would diminish. Ceteris paribus such a state would prefer incomplete contracts without supranational authority, as Russia has pursued in the Commonwealth of Independent States (CIS).

Concerns with bargaining leverage and power asymmetries thus inevitably raise the issue of credible commitment. If the more powerful states want smaller

states to contract with them they must credibly bind their authority. Even though the weaker powers might gain from an incomplete contract they will be reluctant to surrender some sovereign rights without mechanisms to constrain the more powerful actors. Supranational delegation is one way of signaling future compliance by stronger states, but if power asymmetries are stark, as in a hegemonic environment, the stronger power will not consent to such constraints of its autonomy.

The powerful economic actor must thus weigh the benefits it gains from regional integration against the costs of surrendering some sovereign rights. If the demand for regional integration largely originates from the weaker economies, then the stronger state(s) will not consent to the creation of new institutional sites, but will retain residual rights of control. The stronger state will thus be willing to sign an inter-governmental agreement given the gains from trade liberalization but will not surrender sovereign prerogatives. Weaker states without such supranational binding mechanisms will in such situations push for complete contracts, with inter-governmental complete contracting as the result.[46] In lieu of an agreement on supranational institutions, stark power asymmetries will thus yield complete contracting without supranationality. We expect ex ante legislation (full specification and high formalization), little third-party arbitration and adjudication, and weak institutionalization beyond the inter-governmental level.

Conversely, regional organizations with modest power asymmetries will

more likely yield ex-post legislation (low specificity and formalization in the founding document), more third party arbitration and adjudication, and a higher degree of supranational decision making. The stronger states will be more inclined to acquiesce to binding, supranational institutions through which they can credibly commit, partially because balancing coalitions are possible. Modest power asymmetries will make such commitments more credible and thus small states will be more willing to leave negotiation to future, ex-post decision making.

The institutional choices of the relevant agents will also depend on demand symmetry. If the smaller states have more to gain from integration, given that they stand to gain the most from access to larger economies, then the latter will be in a stronger bargaining position and reluctant to surrender residual rights of decision making. Conversely, if both small and large economies stand to gain in roughly equivalent fashion, the stronger economies will be more pliable. They will be more willing to surrender rights as the costs of contracting with lesser states that fear defection.[47]

V. Bargaining over Sovereignty in European Integration

Writing in 1958 one observer even doubted whether the Treaty of Rome would stand the test of new challenges and that "a general crisis, arising for example from a major recession, might cause the Treaty almost to become a dead letter."[48] But, to the contrary, the EEC of the late 50s transformed itself into

a much larger organization, covering much more than just trade liberalization and acquiring many more members. The move to free trade in all factors of production has propelled the EU to tackle numerous other issues such as pension payments, gender equality, mutual recognition of standards, monetary union, and the movement of peoples and refugees. While expressing their interest in "ever closer union" the contracting parties of 1957 could hardly foresee the many dimensions that European integration would take.[49]

Given the uncertainties of final objectives and ultimate ends of the nascent regional organization, member states opted for little ex ante legislation. Indeed, the open-endedness of the Treaty conveniently allowed member states to sidestep difficult decisions that would likely precipitate opposition by domestic constituents. This low level of ex ante legislation, however, required members to rely on ex-post arbitration and supranational decision-making, particularly through the Commission. At first, the European Court of Justice (ECJ) was expected to only play a relatively minor part in the process.[50] Nevertheless, the Court has taken on roles heretofore unforeseen. Key principles and Community legislative supremacy emerged without clear stipulation by the national governments that Community law would be supranational and have direct effect. In other words, not dissimilar in impact to American landmark cases as Marbury v. Madison, or Martin v. Hunter's Lessee, the ECJ appropriated an entirely new realm of authority for itself, with the ECJ at the judicial pinnacle.[51]

European integration thus started from the outset as an incomplete

contract that delegated some residual rights to supranational authorities. Why did the European states agree to do so? What were the procedural elements of this constitutive agreement that gave the states confidence in assigning certain residual rights to supranational institutions? And what have been the consequences of these institutional designs in the long run?

To answer such questions we must start with the foundation of the ECSC and subsequently the EEC in the 1950s. The choices made at that juncture influenced the subsequent European trajectory over the next 5 decades.

The Motives of the Contracting Parties

European political elites, commercial interests, and the general public had been profoundly affected by the experiences of the Second World War. To prevent another conflict Federalists favored a lofty goal of full integration. Others, by contrast, were reluctant to surrender national prerogatives. Yet others were motivated more by concerns about European economic decline and American ambitions than security issues. In the midst of such discussions the French-German axis emerged as a critical force in propelling European integration. What enticed these states to surrender some of their sovereign rights to these nascent European institutions?

The relative symmetry of power and relative symmetry in demand influenced the institutional choices of the states in question. Symmetry of power made credible commitments possible and unilateral hegemony impossible.

Mutual interdependence, the relative symmetry in demand, as all stood to gain considerably from integration, made such integration desirable.

Realists are also correct that security concerns greatly influenced the choices of Paris and Bonn. Initially France pursued policies aimed at diminishing German power and any chance at revival. But with deteriorating relations with the Soviet Union, the United Kingdom and the U.S. opposed such a strategy. Instead France together with the U.K., the Benelux, Germany and the U.S. formed the International Ruhr Authority (1949) which aimed to control coke, coal and steel in the area. With the recognition of the sovereign Federal Republic of Germany in that same year, Germany soon opposed such control over its resources and wanted alternative arrangements. Given its war time past it had to temper its desire to gain full sovereign control by consenting to institutional mechanisms that checked such a revival of German power. Britain and the Americans simultaneously pushed for a revived and more integrated Europe. They soon fixed their gaze on the coal and steel sector where economic and security interests combined.

This sector was a critical component of re-industrialization and a key component of any war effort. With the war only a few years past, there was general unease about a rebuilt and unhampered Germany. Economically the French steel industry was also dependent on German coke. French mines and steel mills also feared a lack of competitiveness in the face of rebuilt German heavy industry. All West European countries also feared that their governments

lacked adequate control given the high degree of cartelization in the private sector.[52]

A strong proponent of federalism, Jean Monnet, drafted the treaty for the ECSC. While Monnet's idea of a supranational planning body—no doubt influenced by French dirigiste ideas—ultimately failed, the treaty did establish important institutional components that would later inform the EEC. The High Authority was thus constructed as a surpranational institution over and above the Council of Ministers of the Member States (the Benelux countries, France, Germany, and Italy). It also established a European Court of Justice to arbitrate disputes between states, firms and European institutions. The common market in this sector prohibited import and export duties, quantitative restrictions and discriminatory practices.[53] Importantly also it sought to eliminate an important source of price distortions by equalizing transport rates—which represented 20-25 % of the price of steel.[54]

The common market in coal and steel was thus from the outset about much more than lowering barriers to trade. Indeed, as Haas notes "there had been no tariffs applicable to these commodities previously."[55] It involved pricing agreements, control over investments, cartel policy, the elimination of subsidies, transparency in labor practices, etc.[56] The broad scope of this form of integration would make any attempt at complete contracting very difficult. Commenting in 1958 on what the experience of the ECSC forebode for the EEC Raymond Mikesell concluded:

> The experience of the High Authority in this field—which has been confined to the problems of regulating competition in only a few related industries is not reassuring. The task for formulating policies and regulations…of perhaps hundred of industries…seems almost overwhelming. Experience in dealing with discrimination and competitive practices indicates a need for an administrative and quasi-judicial authority with supranational powers over a rather broad area.[57]

These experiences entered into the discussions for a more comprehensive community beyond coal and steel. By the mid 1950s, the Cold War had reached its zenith with tensions surrounding Berlin, the Hungarian uprising, and suspected communist meddling in the European colonies. As NATO allies, all six contracting parties shared the threat posed by the USSR.

Despite this common threat, France and increasingly Germany saw a revived, unified Europe as a potential Third Force. French disagreements with the United States were of long-standing, going back to France's position in the wartime alliance, and disagreements about French handling of Indochina and the Algerian War. German chancellor Adenauer too was increasingly distrustful about American motives. The Suez crisis of 1956 had not only exposed European weakness. It had also showed Washington's willingness to exercise heavy-

handed leadership.[58]

Furthermore, it had become increasingly clear that Germany would regain its preeminent position on the continent. By 1954 it had joined NATO as a critical ally in the effort to deter the Warsaw Pact, thus becoming once again a "normal" state, rather than the post-war pariah. German economic growth was obvious as well. Consequently, France sought an institutional means to bind Germany to international agreements which would constrain German options.[59] French foreign minister Pineau thus assured the Soviet Union that European integration was not directed against it, but "to insert Germany into a European community."[60]

Recognizing the importance of such concerns, Edelgard Mahant suggests that geopolitical considerations provided a necessary but not a sufficient condition for integration. Common economic interests emerged as well. German industrialists realized that they would bear the costs of protectionist measures, as in agriculture, but they were willing to bear these given the expected benefits of integration.[61]

Regardless of the relative primacy of geopolitical factors versus commercial interests, we follow the logic that political elites pursued their national objectives by strategic calculation. French and German elites in particular negotiated the institutional contours through which to pursue their aims.[62] For both supranational institutions loomed large in French and German minds. Germany sought a means to re-integrate itself within Western Europe,

while France sought institutional means to curtail a rising Germany. Both pursued their respective security and economic interests.[63] Germany thus stood to gain considerably from access to the other European states. The smaller states similarly would benefit greatly given that Belgium and the Netherlands were heavily dependent on international trade.

Interdependence in other words was symmetric. Capital movements and increasing intra-regional trade gave German industry an incentive to support a supranational bargain as it stood to gain considerably from further integration. And indeed between 1952-55 intra-community trade in steel and coal increased 170 per cent, trade in other goods by 42 per cent, and trade in capital goods (excluding iron and steel) grew by 59 %.[64]

Matching Preferences with Institutional Designs

The European geopolitical and economic environment thus propelled a disposition among political and social elites to tolerate a significant degree of supranational decision making with relatively low levels of precision ex ante in legislation. Nevertheless, they still required institutional safeguards before they actually yielded sovereign prerogatives.

The Benelux states worried that the more powerful states (France and Germany) would gradually usurp more power in such institutions. Given their lack of relative power and given their dependence on access to the market of their larger counterparts, those concerns were warranted. Consequently, the

larger states needed to make credible commitments, without which weaker contracting parties would refrain from any initial agreement.

All contracting parties also had to be apprehensive of a loss of control to supranational institutions. Bargaining leverage after all would gradually shift to those institutions if they gained residual rights of control. Institutions thus had to be designed to alleviate such concerns. How were the six member states able to create institutions that could at once credibly commit the larger states and assuage fears of runaway supranationalism?

First, the six negotiating parties faced modest power asymmetries—measured in terms of relative comparability in overall economic strength. The moderate power asymmetries within Europe provided the smaller states (the Netherlands, Belgium, and Luxembourg) some measure of comfort in signing on to the founding treaty. Although the German economic miracle ("Wirtschaftswunder") was making Germany the pre-eminent economic power by the late 1950s, it still had to contend with a substantial French economy (going through its own economic miracle), as well as with Italy.

Moreover, the three smallest states, which stood to gain the most from trade liberalization, operated jointly on several issues. Indeed it was the joint action of the Benelux at the ministers' conference in Messina in June 1955 that initiated the subsequent negotiations that lead to the EEC. The Benelux also entered negotiations on the common external tariff as a coherent unit, countering the French preference for a common external tariff that would be

higher than the tariff of any member state, given that the Benelux already had negotiated a low common external tariff at an earlier date.[65] The small states showed they could band together for bargaining leverage.

Although the contracting parties only foresaw a gradual shift to majoritarian decision making rather than consensus, they also realized that guarantees had to be built in to assuage the fears of the smaller actors. Thus, the weighted voting system then envisioned, guaranteed that the 3 smaller states could not be outvoted by the three larger ones.[66]

Thus, although it was evident that West Germany would soon be the pre-eminent European power, it could be checked by other relatively powerful actors as France and Italy, or the Benelux, when it acted as a coherent unit. Germany, could not have accomplished its objectives without binding itself. With moderate power asymmetries Germany could not have unilaterally dictated the terms of agreement.[67] Moreover, France clearly wanted to bind Germany, and Adenauer understood that self-binding by Germany was a sine qua non for his nation to be accepted as a "normal" state. Consequently, Bonn had both the will to commit to supranationality while the configuration of forces also allowed it to do so in a credible manner.[68]

This does not mean that the states fully envisioned the depth of contemporary European integration from the outset. Although the Commission could initiate legislative proposals, the Council of Ministers had the ability to block proposals.[69] Also, the European Parliament at this stage had feeble powers

at best, and a direct election of the parliament was not to occur until two decades had past. The ECJ too was not envisaged with broad powers.[70] While the Court soon took on vastly expanded powers in broad interpretations of its jurisdictional competency, it has also realized that in substantive matters, legislation from the member states could nullify aims of the Court. Thus the Court selectively expanded its prerogatives. However, the incomplete contract would logically impel further supranational development.

The eventual signing by the Six of the Treaty of Rome in 1957 encapsulated the breadth of the European ambition, far beyond simply lowering barriers to trade or equal treatment as demanded by the principles of the General Agreement on Tariffs and Trade. Instead the treaty enumerated eleven activities including an end to customs duties; quantitative restrictions; a common external tariff and common external policies; freedom of movement of persons, services and capital; a common agricultural policy; undistorted competition; coordination of economic policies and so on.[71]

Institutionally, the treaty established an assembly, a Council of Ministers, a European Court, and the European Commission. It copied from the ECSC the notion of a supranational court. And the Commission would take a somewhat similar position as the High Authority in its supranational orientation, but without the expansive powers that had been granted to the latter.

In sum, the EEC started from the outset with supranational institutions in its makeup—even if their subsequent powers were still unrecognized.

Furthermore, given the vast scope of the intended integration the Treaty could not hope to resolve all related issues ex ante. Indeed the agreements that truly opened up the movement of persons and capital, the Schengen agreements and the European Monetary Union, would take decades to achieve. In other words, the Treaty was an incomplete agreement with many key issues held over for future legislation and adjudication. The formative treaty of European integration constitutes an exemplar of incomplete contracting with supranational institutionalization.

The Consequences of Assigning Residual Rights to Supranational Institutions

As a consequence of incomplete contracting and the low level of specificity, the contracting states have had to allow the ECJ to develop meaningful review of national decision making and test government policies against EEC legislation. The ECJ has gradually expanded its powers to become a truly supranational force. Already in 1963 the ECJ proclaimed in the Van Gend and Loos case that European Community legislation had direct effect. The Court, not national governments, would test the applicability of EEC law in the particular case. Individuals, moreover, had standing in proceedings against their own government. As the Court stated "the Community constitutes a new legal order of international law for the benefit of which the states have limited their sovereign rights."[72] The Costa v. Enel case, decided one year later, reinforced the van Gend and Loos decision.[73] Contrary to the Italian monist view that

international law needed national transformation in order to be effective (and thus that later national law superseded earlier international agreements), the Court decided that EEC law was directly applicable and thus supreme to national law.[74] In later decisions the ECJ also passed judgment on direct effect of directives beyond regulations and decisions. Subsequent Court decisions over the past decades have expanded the prerogatives and the judicial scope of the Court. [75]

Importantly, such decisions from the ECJ came at the very time that political elites, particularly the French government, balked at any further inroads to supranationality.[76] The ability of the ECJ to proceed while political elites, particularly in France, sought to limit the powers of the Commission and curtail supranational legislation suggests that the particular status of the Court was instrumental to the entire European integration process. That is, elites were willing to go along with the expansion of juridical powers because integration required procedural solutions to the problems associated with incomplete contracting and little ex ante legislation. The Court had to be given great leeway because elites could not know where long term contracting would lead and could not engage in highly specific ex ante legislation.[77]

Germany and France have, by and large, followed ECJ decisions that have gone against them. That is, without the ability to unilaterally dictate the terms of subsequent ex-post legislation and decision making, the larger states have consciously sought to tie their own hands.[78] Even France, although the most

ardent proponent of state sovereignty, holding back the move to majority decision making in the Luxembourg compromise of 1965, has nevertheless gradually given way to more cases of majority decision making enshrined in the Single European Act, the Maastricht, and Amsterdam treaties. France has even given way on the ECJ's monist position of EU law with the Conseil d' État changing its position.

Thus the Court did not simply interpret regulations and directives but took an active stance in actually propelling integration forward. The ECJ has handled cases ranging from tariffs and non-tariff barriers, to equal pay (the Defrenne case).

These expanded powers of the Court are not simply derivative of governments' delegated power, nor should they be construed as tacit state consent before the ECJ rulings, as Geoffrey Garret's inter-governmental perspective would assert.[79] Indeed, even powerful states have consented to adverse judgments in order to establish reputation and credible commitment. If the court were merely epiphenomenal to immediate state interests, it could not perform the necessary function of impartial adjudication. And if it were closely connected to state interests, it could not serve as a mechanism for the stronger states to tie their own hands.

At the same time our argument differs from, but does not contradict, Burley and Mattli's argument. They suggest that the ECJ worked as a "technocratic" institution outside the purview of political oversight.[80] We argue

instead that the ECJ gained considerable independent powers, exactly because it provides a logical function in the incomplete contracting process of the EU. It was not because of a lack of oversight but because credible commitment in such incomplete contracts requires that such supranational institutions must be given latitude outside of immediate state oversight.

Similarly, the Commission capitalized on the residual rights granted to it by the initial Treaty to expand and institutionalize its authority. Consequently, it has often been at the forefront of devising a vast body of Directives and Regulations to implement the original treaties in practice. As Mark Pollack notes, although various oversight mechanisms are in place to curtail the power of the Commission, these oversight mechanisms are costly, thereby giving the Commission considerable latitude in certain areas.[81]

The EU members have thus largely used ex-post legislation and supranational adjudication as a strategically motivated solution to regional contracting under high degrees of uncertainty. For this solution to work effectively, the European Commission, and perhaps even more so the ECJ, have been given considerable independent latitude.[82]

This argument, that the EU process has largely been a process of incomplete contracting and continuous negotiation, squares to considerable extent with explanations that see the EU process as driven by agreements between elites, as the inter-governmentalists suggest.[83] Moreover, Nicolas Jabko recently has shown how, starting with the SEA, the Commission itself

strategically deployed the "logic of the market," with its calculated ambiguity and flexibility over what that the term actually meant, to forge cross-cutting coalitions within states that would support the completion and institutionalization of the single market's institutions at the supranational level.[84]

But we disagree with those who suggest that the EU today should simply be seen as an inter-governmental agreement from which states can extract themselves at any juncture. While the initial choices in the creation of the European Community no doubt reflected state interests, subsequently that Community has entered a realm of supranational decision making. Once institutionalized these supranational bodies have rarely transferred back actual sovereign authority or jurisdiction to member states. The logic of incomplete contracting and the need for credible commitment have rendered the original inter-governmental agreement an obsolescing bargain.

VI. Regional Integration in North America

In contrast to incomplete contracting in European integration, NAFTA, since its adoption, has manifested complete contracting. The integrative process remains also decidedly inter-governmental with more modest objectives than the supranational decision making process of the EU. In contrast to the EU, NAFTA evinces a much higher degree of ex ante contract stipulation and less ex-post judicial and legal activism.[85] NAFTA remains limited to a free trade agreement, whereas the EEC set out to form a customs union and an economic community

from the outset.

As with our analysis of regional integration in Europe I focus on three questions. First, what were the underlying motives of the contracting parties to the agreements? Second, what kinds of institutions did the actors design to deal with their specific concerns in the contracting process? More specifically, how did the states manage to mitigate the dangers of reneging and hold-up in later stages of the agreement? Third, how did the particular allocation of residual rights influence the subsequent development of regional integration?

Motives and Objectives of the Contracting Parties

Similar to the European states, the North American contracting parties were motivated by a mix of geopolitical considerations and economic concerns. To a considerable extent, movement toward regional integration in North America was driven by the developments in European integration. In all three states domestic political and economic elites also started to converge in their preferred policies for trade liberalization.

NAFTA is a direct extension of the FTA between Canada and the United States in 1987. The latter built on the Canadian-American automobile accord two decades earlier.[86] Despite the automobile accord, the United States and Canada had not pursued further integration. Canada still opted for a more interventionist government policy than the United States. It also still retained ties to the UK and the Commonwealth preference system. The United States on its side, still

pursued a global liberal agenda, even if by 1972 it had to retreat from fixed exchange rates.

By the 1980s, the situation had changed dramatically.[87] Canadian Conservative Prime Minister Mulroney was far less inclined to interventionism than his predecessor Pierre Trudeau. The UK had also clearly moved towards European integration, rather than pursue economic agreements with the remnants of the former empire. With 80% of Canadian exports going to the United States, Ottawa became increasingly interested in opening up the cross border trade with its powerful southern neighbor, particularly in view of its weak domestic market in the 1980s.

However, despite economic setbacks in the 1970s, the United States, with its multilateral rather than regional focus, still proved a reluctant partner. Only fears of relative U.S. decline, the threat of a "fortress Europe" following the SEA, and the difficulties of getting the Uruguay Round started made the United States think of a regional alternative.[88] The "NAFTA" track would serve as an incentive for Europeans and Japanese to be more amenable to American demands. The carrot of an agreement on GATT was balanced by the stick of a regional alternative.

A similar set of calculations informed U.S.-Mexico negotiations in the late 1980s. Mexico had initially pursued protectionist policies and had frowned on foreign influences on its economy. Indeed, foreign ownership of Mexican oil deposits was constitutionally prohibited. Lopez Portillo's government had walked

away from a very favorable GATT protocol in 1979, which gave Mexico 15 years to adjust.[89]

But the fall in oil prices in 1980 and the debt crisis put an end to that strategy.[90] The Mexican governments of de la Madrid and Salinas did a dramatic about face, pursuing export led growth and foreign investors. Salinas, a product of the de la Madrid "camarilla" expanded on de la Madrid's turn to trade liberalization.[91] Staffing his administration with technocrats, de la Madrid and Salinas forged a coalition between state elites favoring liberalization and the peak associations of large business enterprises.[92] In particular, the lure of American investments in Mexico proved enticing to these corporations. The way forward lay in pursuing access to the North American market, while at the same time seeking GATT membership.[93]

Once again, the United States proved reluctant. The American agenda remained focused on progress in the Uruguay Round. The continued difficulties in concluding a final agreement, however, made the United States more amenable to Mexican overtures. A GATT agreement by the late 1980s seemed more remote than ever with disagreements on agriculture, services, and the protection of property rights. Worse even, a possible trade war loomed with Europe in view of the Spanish and Portuguese accession that raised tariffs for American soy exporters.[94] A broader regional fall back option, beyond the bilateral deal with the Canadians, gained gradual momentum in Washington.[95]

Canada, too, was initially uninterested in a trilateral agreement, though it

had started bilateral discussions with Mexico. It had few economic connections with Mexico and Mulroney did not see a broad North American deal emerge in the 1980s.[96] Canada, nevertheless, also changed its position. The Canadian government feared that the United States and Mexico would sign a bilateral deal, thereby allowing Washington to create a hub and spoke pattern through its treaties with its neighbor to the north and south. Moreover, a Mexican-American bilateral deal would likely siphon American investments from Canada. Thus Ottawa thought it wiser to maintain its seat around the bargaining table.

Thus by the 1980s Canada and then Mexico sought to pursue greater liberalization in North America. Demand, however, was asymmetric. Mexico and Canada sorely needed access to the American market, whereas the United States had multiple options. Its trading relations across North America, East Asia, and Europe made a North American agreement less imperative for the United States than for the smaller economies. Not only was the U.S. economy considerably larger, but because the demand in the other states for integration was stronger than on the American side, the United States was in the driver's seat. The preponderance of the American economy in the NAFTA region allowed the United States to get what it wanted by bargaining and bilateral or trilateral deals. U.S. officials could thus clearly set the terms of the agreement. For example, from the outset, Washington stipulated to the Mexican government that any mention of free movement of labor would terminate the discussion.[97] Other issues that were likely to arouse controversy were bracketed and addressed in side deals.[98]

Yet other items required last minute concessions by Mexico, such as on sugar and citrus.

While all states opted for North American liberalization, the asymmetric demand worked wholly in favor of the United States.[99] Washington, therefore, had little incentive or need to submit to supranational organizations or to third-party binding arbitration that might hinder the pursuit of American objectives.

Even if there had been greater enthusiasm in the United States for a far reaching agreement, the asymmetry of power would have made it difficult to create binding institutional mechanisms. The asymmetry of power between the North American contracting parties was far more pronounced than between most of the European member states. Even the 1987 FTA between Canada and the United States coupled two advanced capitalist states of highly disparate power. In 1984 American GNP came to 3,947 billion dollars, dwarfing that of Canada ($346 billion).[100] The inclusion of Mexico in the accord in 1994 similarly highlighted power disparities between Mexico and its counterparts. The American GDP in 1991 was still nine times that of Canada and more than 20 times larger than the Mexican GDP.[101] The Mexican GDP per capita was 1/7 of that in Canada and the United States. In the European case, although the German economy was strong, it accounted for only 1/5 of EC output whereas the U.S. economy accounted for almost 85% of the NAFTA region.[102] With only a few contracting negotiating states, there was no hope of an offsetting coalition.

Consequently, Canada and Mexico had to distrust American hegemony.

Indeed, at one point during the negotiations, Washington—to the dismay of the Canadians—threatened to restrict binding bi-national dispute settlement procedures only to the FTA, and not extend such procedures to the NAFTA dispute settlement. Ultimately, NAFTA did incorporate the FTA procedures, but Washington signaled strict limits as to how far it would allow its sovereignty to be curtailed.[103]

Mexico, in particular, had to fear "being too far from God and too close to the United States" as dictator Porfirio Diaz once lamented. Even Salinas, while staunchly advocating multilateral liberalization, feared as late as 1988 that "there is such a different economic level between the United States and Mexico that I do not believe such a common market would provide an advantage to either country."[104]

Counterfactually, even if the U.S. had consented to greater delegation to supranational institutions, its commitment to abide by any such legislation or adjudication would be less than credible. Canadian and Mexican dependence on access to the American market, and the ability of the United States to pursue multilateral options, gave Washington the ability to renege unilaterally if it so chose. That is, the very preponderance of the United States made it difficult to design institutions that could credibly constrain the hegemon.

Consequently, without agreements that would constrain American pre-eminence, the weaker parties had little incentive to put their fate in a relatively open-ended agreement. The contracting parties preferred to negotiate complete

contracts and exchange specific quid-pro-quos up front, rather than relegate points to further negotiations. Given the high level of formalization ex ante, and the high level of complete contracting, ad-hoc arbitration, not ex-post legislation and supranational adjudication became the norm.

The Consequences of Complete Contracting and Inter-Governmentalism

Because the residual rights of control reside with the contracting parties, NAFTA has not progressed much beyond the terms of the initial agreement. Unlike European integration, which quickly expanded into various areas of economic and political cooperation, and many more members, NAFTA has expanded little. Canada, despite gaining from liberalization with the United States, remains weary of domination by its more powerful neighbor and has excluded certain areas from the regional agreements, such as sectors deemed important to its cultural heritage. Canada has also been reluctant to accept a customs union and has explicitly sought to capitalize on foreign investment in Canada (particularly by Japan), using Canada as a convenient back door entry into the U.S. market. Voluntary Export Restraints (VER) in steel and automobiles imposed by the United States on Japan and European states only accentuated the attraction of Canada in the 1980s.[105]

With the extension of the FTA to Mexico, both the United States and Canada have excluded full factor mobility, specifically of labor. Environmental concerns with a rush to the bottom have weighed in as well. The agreement has

remained limited to diminishing trade barriers between these states rather than creating a customs union, let alone full economic integration. In lieu of common external tariffs, the parties have instead devised more stringent local content laws and "transformation tests."

In NAFTA ad-hoc arbitration has sufficed because ex ante stipulations were far more extensive. Arbitration has also been rare. By one count the number of cases brought under chapter 18 and 19 FTA clauses, and chapter 19 and 20 of the NAFTA numbered no more than 81 by 1999.[106] Actors know what the terms of the agreement are and their preferences have been incorporated into the agreement's original terms.

Not only have few challenges emerged, but most cases have been relatively straightforward, with the norm being consensus decisions.[107] NAFTA dispute settlement panels allow each state to choose two individuals from a roster of specialists with the fifth to be agreed upon by both. Although one might expect that such panels would fragment along national origins, this has not happened.

In short, the NAFTA agreement has differed in two key aspects from the European agreements for integration. These differences have had profound effects on the subsequent process. First, NAFTA institutions lack the supranational equivalent of the Commission, Parliament, or Court. Instead, political leaders brokered the terms of the agreement ex ante and in great detail, whereas the inter-governmental bargain in the EU only set the broad contours of

agreement.

Second, arbitration panels in NAFTA are ad-hoc and their composition needs the approval of the contracting parties. Panels decide single complaints rather than expand the domain of regional legislation. With no standing court, there is not an institutionalized mechanism through which the arbitration procedure can establish precedent and expand the supranational aspects of integration. Consequently, fears of a loss of sovereignty and usurpation by the regional organization remain moot.

Incomplete contracting with supranational institutions builds into the agreement, and indeed virtually demands, further development along supranational principles, and creates dynamic incentives for further integrations. Inter-governmental complete contracting, by contrast, virtually precludes such developments.

VII Conclusion

The argument I proposed, differs from the view that regional organizations are simply extensions of the state interests. That argument holds for NAFTA, as it is an inter-governmental complete contract. But it is not correct that the institutions created by the EEC, and which are now still at the basis of the EU, are simply agents acting at the behest of their governments.[108] Thus one might argue that what starts out as delegation by governments (principals) to the agent (the EU institutions), ends up increasingly within the realm of agent

autonomy. We argue that EU activism is not the consequence of a loss of principal control over the agent, but that some of the EU institutions, such as the ECJ were not, and indeed given the logic of the incomplete contract, could not be, mere agents.

We thus support Giandomenico Majone's claim that principal-agency theory misunderstands the nature of European Community structures. Simple delegation on an intergovernmental basis would not greatly enhance credibility. Instead, Majone argues for an alternative understanding of the relation of national governments to European level institutions, which he calls fiduciary delegation. Discussing the role of the ECJ in this mode, he observes:

> Iin policy areas where the Community is exclusively competent, the power to exercise public authority has been irrevocably transferred...Since the treaties did not contain an explicit list of areas of exclusive Community competence, it has been up to the Court to build up such a list.[109]

As a result of the incomplete contracting nature of the EEC Treaty, and because of the need to credibly commit, European Community institutions required the states to give up meaningful authority. This is not simply a question of principal-agency "slippage", but a logical response to how state elites can solve contracting problems.

This analysis also challenges realist expectations that European regionalization would stall. Realists aver that the cooperation between the European countries, particularly in its supranational aspects, will decline with the end of the Cold War and the declining American presence. Concerns about relative gains will become more pronounced with fears of German dominance.[110]

Instead, the logic of incomplete contracting can explain why EU institutions have become catalysts, driving the integration process forward. Given the incomplete nature of the European foundational treaties, these institutions inevitably acquired broad mandates to expand on the earlier agreements. The very incompleteness of the contract thus required further action if states wanted to capture the full benefits of their earlier agreement.

In addition, the iterative nature of European contracting, the decades of progress to ever closer union, and the expanded powers of supranational adjudication have institutionalized the incomplete contracting process in the EU. Subsequent Court decisions and supranational directives from EU organizations have produced a ratchet effect due to the dedication of assets following such decisions. Reversal of policies will be more costly than moving forward. That dynamic in turn has also facilitated the credibility of commitment of even the largest powers in the Union.

Moreover, regional differences will persist, contrary to expectations that the EU and NAFTA will converge as time progresses. Their variant institutional designs impel different behaviors on the part of national elites and regional

institutions. Incomplete contracting will spur further negotiations and specifications by supranational institutions. NAFTA as a complete contract will not.

Thus, the EU and NAFTA will continue to manifest diverse institutional practices through which they pursue the benefits of regional integration. Their institutional configurations have launched the signatories on diverse trajectories. At this point the EU proceeds with a built in dynamism. NAFTA, by contrast, provides an example of complete contracting and hence has few means to expand into other areas. Accordingly, the likelihood that other regional organizations such as ASEAN and MERCOSUR will come to resemble either the EU or NAFTA will greatly depend on whether their member states choose to adopt incomplete contracting or a complete contract as a governance mechanism.

Table 1 General Propositions

Governance of Sovereign Rights and Asset Allocation

G1: When the political transaction costs of sovereign integration or disintegration are high, incomplete contracts allow states to create hybrid governance arrangements, either by splitting or sharing sovereignty, rather than to opt for formal hierarchy or anarchy.

G2: Incomplete contracting allows hybrid governance arrangements short of hierarchy to emerge over specific assets.

Bargaining Leverage among Contracting States

B1: Upon renegotiation of a bilateral incomplete contract at t+1, the holders of the residual rights of control will have leverage. They will engage in hard bargaining so as to alter the terms of the initial contract in order to appropriate the ex post surplus.

The Momentum for Sovereign Transfers

M1. In both bilateral and multilateral settings, renegotiation of an incomplete contract at t+1 will more explicitly delineate, specify and codify the governance arrangements of an asset or function. All else being equal, incomplete contracts tend to completeness.

M2: Incomplete contracts will be maintained as long as: a). joint supply gains are institutionalized (sometimes through issue linkage); and/or b). states lack alternate contracting partners.

Credibility of Commitment Problems

C1: Incomplete contracts will be easier to conclude when the parties can credibly commitment through institutional or reputational mechanisms.

C2: The burden of credible commitment falls particularly on the holder of residual rights of control

Figure 1. Causal Dynamics in the Creation of Hybrid Sovereignty and its Downstream Consequences

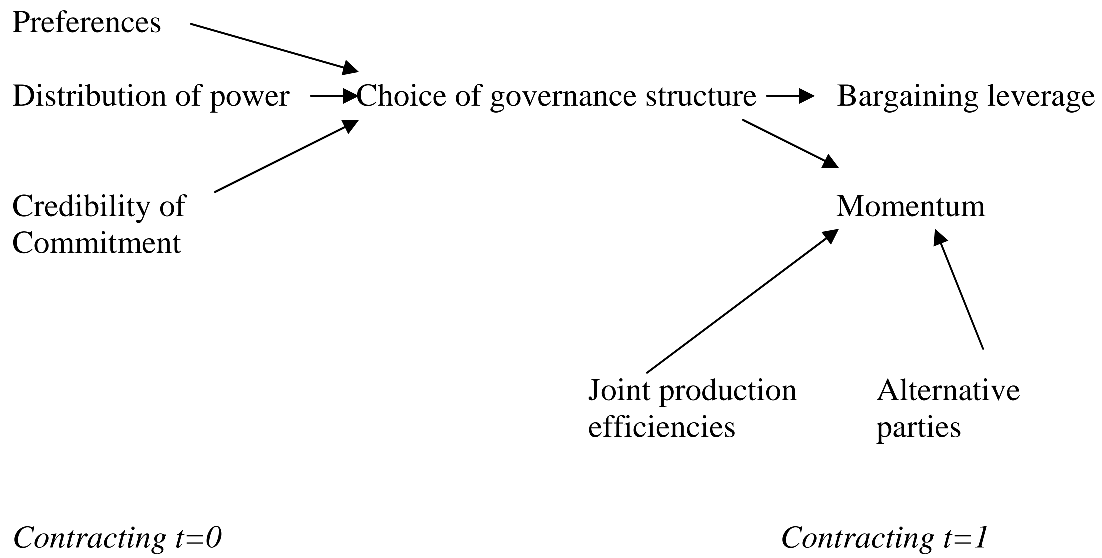
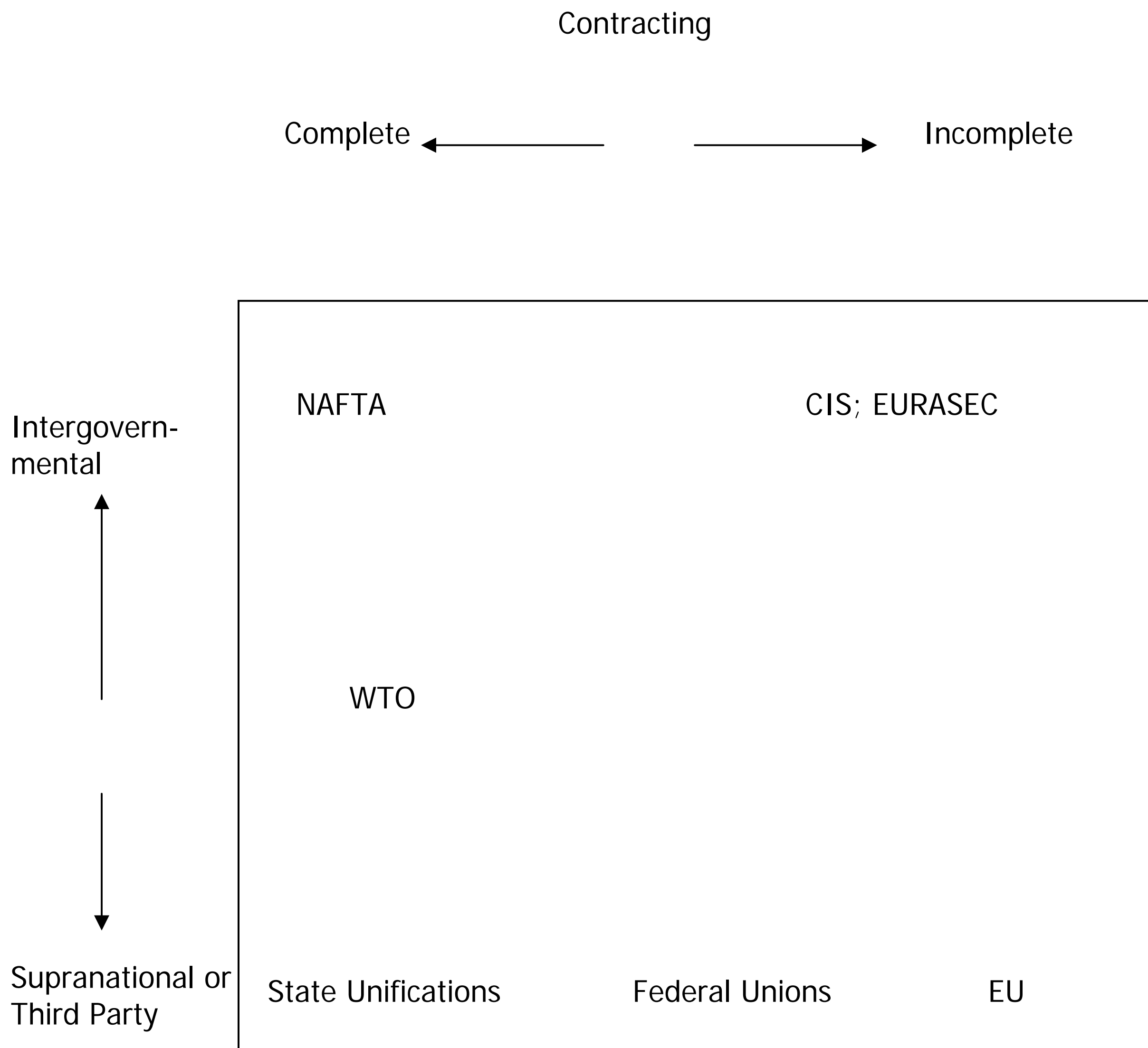


Figure 2. Modalities of Integration



Endnotes

[1] Keohane 1984; Eggertsson 1990; North 1990; and Ostrom 2005.
[2] Williamson 1975;1985.
[3] Various types of specificity include site-specific investments, physical asset-specificity, human-specificity and dedicated assets. Williamson 1985, 95-96.
[4] Frieden 1994.
[5] Keohane 1984 focuses less on transaction-specificity and more on how international institutions mitigate transaction costs. See also the work by Lipson 1985; Lake 1997, 1999, Yarborough and Yarborough 1992; Weber 2000; Weber and Hallerberg 2001, Wallander 2000.
[6] For a critical view of Williamsonian theory from a business and economic perspective, see Kay 1995.
[7] Williamson 1985, 83.
[8] For an overview, see Dow 1987. Also Mattli 2001; and Van Harten 2007
[9] Dow 1987.
[10] The Cecchini report, for example, predicted an overall 4.5-7 % GDP growth in the EC. Emerson 1988. Likewise Mexico anticipated significant economic gains from NAFTA. Cameron and Tomlin 2000.
[11] See Abdelal 2001.
[12] Krasner 1999, for example, argues that decisions about sovereignty should be modeled by the interests of political rulers rather than by the interests of states.
[13] Hart 1995; Hart and Moore 1990; and Grossman and Hart 1986.
[14] Hart 1995, 24-27.
[15] For a useful discussion, see Boycko, Shleiffer, and Vishny 1995.
[16] For a discussion see Cooley 2000/01.
[17]An often-cited historical example—that of General Motors (GM) and the automobile body manufacturer Fisher—illustrates these dynamics in practice. Hart 1995, 6-8; and Klein 1988.
[18] Epstein and O'Halloran 1999, 44.
[19] Abdelal 2001.
[20] Snyder 2000.
[21] Milner 1997.
[22] See Grieco 1990.
[23] Also see Cooley 2005a.
[24] See the discussions in Baldwin 1993.
[25] Our approach shares much in common with Barbara Koremenos, Charles Lipson, and Duncan Snidal's "Rational Design of International Institutions" project. They focus on institutions, defined as "explicit arrangements, negotiated among international actors, that prescribe, proscribe, and/or authorize behavior." Koremenos, Lipson, and Snidal 2001, 762.
[26] Intermediate arrangements among firms include split property rights arrangements (leasing) and shared property rights arrangements (joint

production and horizontal agreements). On the organizational logic of the joint venture and its advantages in mitigating transaction costs, see Kogut 1988, 319-322.

[27] Mattli 2001; and Van Harten 2007. Furthermore, states are increasingly sharing sovereignty by agreeing to binding arbitration over commercial and/or even border disputes. See Simmons 2002.

[28] Hix 2002.

[29] See Cooley 2005b; and The New York Times, July 31, 2005.

[30] See Cohen-Tanugi 2005.

[31] To give but one example of how technology affects the pursuit of empire: the shift from sail to coal required the Royal Navy to obtain re-coaling stations, and thus overseas bases across the globe.

[32] George 1979.

[33] Bates, et al 1998, 10.

[34] It is important to realize that our analysis focuses on "real" contracts. Parties sign these agreements because they expect that they will govern their relations for some time in the future. These agreements proscribe and authorize particular behavior, and are not merely "window dressing." In this sense they might be distinguished from "pseudo-contracts."We are indebted to Robert Keohane for drawing our attention to this distinction as well as for suggestions on how one might discern whether contracts do indeed constrain behavior or are merely meant to deceive domestic or international audiences.

[35] The European Union is the name for the organization since the Treaty of Maastricht (1992). Depending on the time frame to which the particular segment of our narrative refers, we will also describe the organization as the European Economic Community (EEC) or the European Community (EC).

[36] Moravcsik 1998, 152, 157.

[37] Majone 2005, 73. He observes, furthermore, that in relational contracting parties do not agree on detailed plans but on general principles, on the criteria to be used to decide unforeseen contingencies, on who has the power to act, and on dispute settlement mechanisms (72,73).

[38] See Abott 2000, 519.

[39] The locus classicus is Haas 2004 [1958]. Also see Mikesell 1958; Gordon 1962.

[40] Sweet and Brunell 1998, 73. They submit that inter-governmentalists, who argue that the EU institutions cater to and are the result of negotiations aimed to foster state interests, are wrong. See also the discussions by Burley and Mattli 1993; and Alter 1998, 2000.

[41] For further discussion of the various motives, emphasizing security and economic concerns to different degrees, see Mahant 2004; Milward 1992; Moravcsik 1998. On the importance of European elites and the ideational construction of the European project, see Parsons 2003.

[42] For a comparative discussion of post-imperial economic integration and disengagement, see Abdelal 2001.

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[43] As Daniel Drezner notes, even realists concede that the dispute settlement body of the WTO constitutes a significant case of supranational authority when enforcing decisions that go against powerful states. See Drezner 2007.
[44] Thus the WTO system establishes a permanent international judicial body, whereas NAFTA establishes a quasi-judicial body or arbitral panels. See the classification in the Project on International Courts and Tribunals. www.pict-pcti.org/publications/synoptic_chart/synoptic_chart1.htm. Also see ww.wto.org/english/tratop_e/dispu_e/dispu_e.htm#dsb
[45] Rector 2003.
[46] In addition the number of contracting actors might mitigate the relative salience of power asymmetries by facilitating countervailing alliances. This in turn will make it easier to create institutional binding mechanisms. Our conclusion would correspond with the hypothesis of Koremenos, Lipson and Snidal (2001, 794) that larger numbers tend to correlate with more centralized institutional mechanisms or quasi-legislative institutions that are empowered to adjust the agreement. However, they attribute this to renegotiation costs.
[47] Moravcsik (1998) uses a different terminology, but argues similarly that asymmetric interdependence determines concessions. Those who stood to gain the most, made the most concessions.
[48] Hurtig 1958, 381.
[49] Overviews of the early stages of European integration and its various institutions are too numerous to count, but see, for example, Archer 1990; Dinan 1999; George 1985; and Harrop 1989.
[50] Moravcsik 1998, 155.
[51] One could see the U.S. constitution as an example of incomplete contracting as well. Due to the brevity and vagueness of the founding document, the Supreme Court had to step in as a supreme arbitrator and settle many issues ex-post.
[52] Gordon, 1962, Mikesell 1958.
[53] Archer 1990, 55.
[54] Mikesell 1958, 436.
[55] Haas 2004, 60.
[56] Alter and Steinberg 2007, 91.
[57] Mikesell 1958, 437.
[58] Mahant 2004, 102, 128, 131.
[59] Even as economists debated the benefits of integration, they recognized that a key objective was to embed a rearmed and economically strong Germany in a European Community. See, for example, Gehrels and Johnston 1955.
[60] As cited in Mahant 2004, 132.
[61] Mahant 2004, 45, 47, 62.
[62] Britain also had interests in a unified Europe, but due to Commonwealth and imperial considerations, as well as French reluctance, it opted for a Free Trade Area rather than the EEC. See particularly Schenk 1996; and also Butt 1966.

[63] Moravcsik 1998, 87, 94-7, 103, 111.
[64] Mikesell 1958, 438.
[65] Hurtig, 1958, 348. The end result was a common external tariff based on the arithmetical average of the duties in the four customs territories.
[66] Mahant 2004, 94; and Moravcsik 1998, 153.
[67] The German war record of course would make such a unilateralist effort even more problematic.
[68] Even Joseph Grieco who sets out to defend a realist perspective of integration, ends up pointing to the modest power asymmetries and the willingness and ability of German to credibly commit—blending neoliberal institutionalist arguments with realist views. See Grieco 1995.
[69] Mahant 2004, 95.
[70] Moravcsik 1998, 155.
[71] For a quick overview, see Archer ch.5
[72] van Gend and Loos v. Nederlandse Administratie Belastingen, ECJ 26/62 1963.
[73] Costa v. Ente Nazionale per L'Energia Elettrica (Enel), 6/64 1964. The Simmenthal decision (1978) further expanded on this. National courts were instructed to see to it that community law was implemented and "to set aside any provisions of national law which conflict with it." See Dinan 1999, 34.
[74] See Alter 1998.
[75] See the numerous examples in Alter 1998; and 2000.
[76] For the argument that the ECJ had an important independent role in moving supranational decision making forward, see Burley and Mattli 1993.
[77] Moravcsik notes that delegation occurs when joint gains are available, distribution conflicts are moderate, and the environment is highly uncertain. See Moravcsik 1998, 75.
[78] For a realist argument that large states have strategic incentives to restrict their own latitude for maneuver, see Grieco 1995.
[79] Garrett 1995; and Garrett, Keleman, Schulz 1998. For a discussion of the inter-governmental perspective and neofunctionalists, see Grieco 1995; and Mattli 1999.
[80] Burley and Mattli 1993.
[81] Pollack 1997.
[82] At the same, the powers of the ECJ are not without limits. There are various reasons, which we cannot touch on in this paper, that induce the Court to act with caution. Indeed, qualified majority voting which is often seen as a move towards greater supranationalism, at the same time might be conceived as limiting the powers of runaway ECJ activism, given that offsetting legislation to counter ECJ decisions is easier to pass.
[83] Moravcsik 1991; and 1998.
[84] Jabko 2006.
[85] Abott 2000.

[86] See the discussion in Winham 1988; and Hufbauer and Schott 1992, ch. 1, 2.
[87] Winham 1988, 44-6.
[88] As Jagdish Bhagwati interestingly points out, as early as the 1960s some voices in the United States saw regional free trade agreements as an alternative to the EEC and multilateralism. By the 1980s with the Europeans reluctant to start the Uruguay Round and with European integration picking up steam, the regional alternative reemerged in the minds of politicians. Bhagwati 1993.
[89] Cameron and Tomlin 2000, 57-8.
[90] Even explanations that focus on the impact of ideas and ideological conversion, suggest that the impetus for change came from the international economic shock of the early 1980s. See, for example, Golob 2003.
[91] Camp describes the importance of this camarilla (clique) in Mexican politics. See Camp 1990.
[92] Thacker 1999. The losers in the process were farmers, urban poor, and the middle class, who were kept out of this ruling coalition and the deliberations on NAFTA.
[93] Mexico gained GATT membership in 1986 on much less favorable terms than were offered in 1979. See Dufey and Ryan 1994.
[94] Odell and Matzinger-Tchakerian 1988.
[95] Domestic rifts in the U.S. were significant with many labor and environmental groups opposing and larger businesses favoring the deal. Erstwhile Presidential candidate Ross Perot became one of the vocal critics of NAFTA. In the end the agreements passed its biggest hurdle, the House of Representatives, with a 34 vote margin. Keith Bradsher, "After Vote, Labor is Bitter but Big Business is Elated," New York Times, Nov. 18, 1993, A21. See also David Rosenbaum, "House Back Free Trade Pact in Major Victory for Clinton after a Long Hunt for Votes," New York Times, Nov. 18, 1993, A1
[96] Hufbauer and Schott 1992, 24. The Canadian public also seemed less than enthusiastic about what the CUSFTA had yielded. See, for example, Clyde Farnsworth, "Canada's U.S. Trade Experience Fuels Opposition to the New Pact. New York Times Oct. 3, 1993, 1.
[97] Cameron and Tomlin 2000, 71.
[98] The environment thus required a side agreement to allay some opposition. See Baker-Fox 1995.
[99] To give a recent example, when the Mexican government asked for a renegotiation of the opening of its corn and beans market in 2008, Washington flatly refused. The Mexican government responded in turn that it would dutifully abide by the earlier terms, even though roughly 3 million small and less efficient Mexican farmers fear the adverse effects of U.S. competition. Bloomberg.com, June 6, 2006.
[100] Bueno 1988, 107. Figures from World Development Report 1987.
[101] Hufbauer and Schott 1992, 5.
[102] Grieco 1994.

[103] Cameron and Tomlin 2000, 48, 49. As one observer rightly noted, "it was Mr. Salinas who staked his Presidency on the trade agreement, often dragging a reluctant nation into partnership with a powerful neighbor it has always feared." Tim Golden, "Mexican Leader a Big Winner As the Trade Pact Advances," New York Times, Nov. 19, 1993, A1.
[104] Quoted in Cameron and Tomlin 2000, 59.
[105] See, for example, Dufey and Ryan 1994.
[106] Stevenson 2000.
[107] Goldstein 1996; and Stevenson 2000. For a discussion of the general settlement mechanism, see Hufbauer and Schott 1993, 102-04.
[108] For discussions of agency theory, see Eisenhardt 1989. Doleys has sketched some of these concerns for the EU. See Doleys 2000.
[109] Majone 2005, 77.
[110] Grieco 1995; and Mearsheimer 1994/95.

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