CEI's Monthly Planet

Fighting For Freedom

July 2004 Competitive Enterprise Institute Volume 17, Number 5

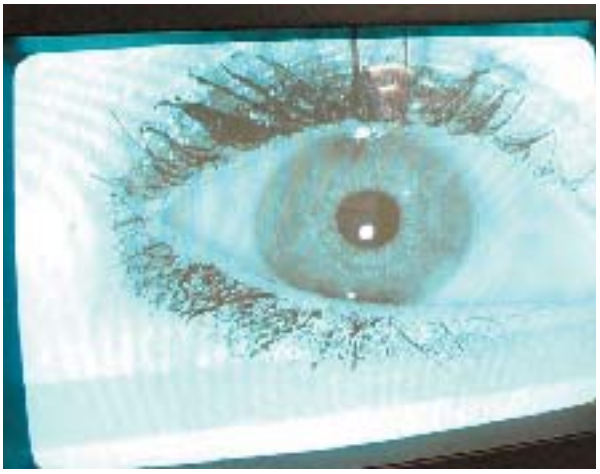
Who's Afraid of RFID?

by Jim Harper

Radio frequency identification (RFID) tags are small radio communicators that signal information about the tag and the item to which it is affixed. In the area of consumer goods, RFID holds out a variety of benefits in terms of convenience, safety, and low costs.

RFID has raised a variety of privacy-related concerns and calls for regulation. To date, RFID tags have seen limited deployments, so there is little real-world experience upon which to ground discussions about regulation. Before those discussions become timely, a variety of social forces will constrain RFID more suitably than government regulation could.

An unlikely threat to privacy, RFID technology will help producers, marketers, and retailers better understand—and therefore better serve—the entire mix of consumer interests. Legislation to restrict the technology would be premature.



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Advantages of RFID

RFID has two advantages over the bar code scanning that is common for consumer goods today. First, RFID does not require a line of sight. Items may be scanned by bringing a reader near the scanner; there is no need to unpack goods, turn them around, or clean them off. This will save time at the checkout stand, and even more at the warehouse.

Second, RFID can identify goods uniquely. The typical RFID tag may hold about two kilobytes of data, enough to contain a distinct numeric code. Correlated in a database, that code can indicate unique information about the item. Safety benefits include being able to identify where and when goods were manufactured in case of a recall or knowing when food or medicine has outlasted its "sell by" date. Item-level identification could allow receipt-free returns of goods, or tie expensive equipment to its owner so that it can be returned if it is lost or stolen.

Fears Surrounding RFID

The potential power of RFID systems has given rise to fears about the technology's effect on privacy. There are two types of privacy effects RFID could have.

First, RFID could allow people in the manufacturing or sales chain to glean more information about customers than people are comfortable with. This is part of a longstanding debate about what retailers and marketers may do with consumer information they gather through transactions.

Second, RFID could be used by a stranger to track an individual. Conceivably, someone could scan a RFID tag at one location and use a second scan elsewhere as a proxy for

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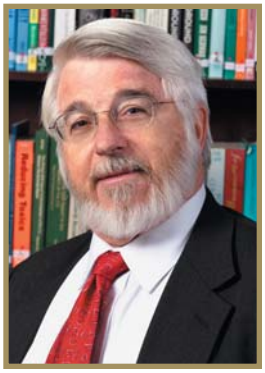
From the President



The Greening of the Balance Sheets

by Fred L. Smith, Jr.

In June, the United Nations' Global Compact Leaders Summit brought together U.N. environmental bureaucrats, international NGOs, labor leaders, and representatives of the financial world—banks, brokerage firms, social investment funds—to promote a concept known as Corporate Social Responsibility (CSR). Summit attendees endorsed adopting "voluntary" principles "to embed environmental, social and governance best practices at the heart of the world's markets."

CSR is premised on the idea that politics should determine societal goals. Private firms should then be incentivized—through regulatory quotas and taxes—to achieve them efficiently.

One CSR goal is to transform the corporate balance sheet to include not only profits, but also concerns like labor rights, human health, civil liberties, environmental quality, sexual equality, and social justice. One activist group, the California-based Rose Foundation, petitioned the Securities and Exchange Commission (SEC) to require reporting of environmental liabilities by U.S.-listed firms. At first glance, this seems prudent. Liabilities—from Superfund to asbestos—have bankrupted otherwise healthy firms. In today's litigious world, such disclosures are desirable on fiscal conservative grounds. Or are they?

Accounting, after all, is the heroic attempt to translate the dynamism of the modern firm into a set of numbers—much like characterizing an individual as a set of test scores. Never easy, accounting has nonetheless encouraged capital to flow toward firms with sound balance sheets and away from firms with weak or suspicious accounts. And this result is clearly desirable. Narrow economic accounting, of course, doesn't reflect all societal values, but was it ever supposed to?

There are an infinite number of possible futures and thus an infinite number of possible liabilities. Trial lawyers and activists attack chemicals in our water, calories in our food, automobiles on our highways, and emissions from energy production in our air. Human rights and labor activists would assign multinationals financial liabilities because they operate in nations where civil liberties or workers' rights aren't well protected. And there are always Acts of God—earthquakes, floods, and hurricanes—which prove costly.

But only some of these possible risks will ever be borne out. Accountants find it difficult enough to report upon intangible liabilities. At what point does the noise from such additional guesstimates undermine accounting's informational value? In seeking to disclose information about less likely risks, don't we obscure information about more likely risks? Should unlikley but possible windfalls be listed, too?

CSR activists already use shareholder resolutions to push corporations to adopt their agendas. Mandating the inclusion of politically charged information on balance sheets will strengthen those within the firm responsible for ancillary issues like NGO outreach, government relations, or environmental investment. Those favoring new investments to expand output to increase shareholder value—supposedly the firm's core mission—may well lose influence. Trial lawyers may use those internal conflicts over corporate policy to strengthen their case against the corporation.

This threat should be taken seriously. As the late political scientist Aaron Wildavsky noted in his criticism of earlier such efforts: Accounting may be only a social construct (as some post-modernists claim), but it has been a very valuable one. It has made markets and corporate management more efficient—producing a wealthier society.

Yet these concerns have little standing among CSR advocates. The modern corporation, they argue, has great power—power that should be harnessed to ensure social justice, sustainable development, and global stability. That's a tall order, one for which they intend to use accounting rules as a tool.

In today's world, to paraphrase Jimmy Durante, everybody wants to get into the corporate accounting act. If all restraints on what the balance sheet should list are abandoned, then everyone will expect their preferred values to gain primacy.

Should economic accounting be abandoned as no longer providing adequate guidance for a just world? Should the SEC mandate inclusion of any value championed by a politically powerful group? Or should regulators allow accountants to devise a variety of rules for different firms and different purposes? The answer, to us, is obvious.

Fred Lee Smith Jr

MONTHLY PLANET

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CEI's Monthly Planet is produced 10 times a year by the Competitive Enterprise Institute, a pro-market public interest group dedicated to free enterprise and limited government.

CEI is a non-partisan, non-profit organization incorporated in the District of Columbia and is classified by the IRS as a 501 (c)(3) charity. CEI relies upon contributions from foundations, corporations and individuals for its support. Articles may be reprinted provided they are attributed to CEI.

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ISSN# 1086-3036

Who's Afraid of RFID?

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the presence of an individual at the second place. There are lots of difficulties with attempting to use RFID this way, but it is at least a plausible threat from the technology.

Exaggerating these concerns somewhat, a number of pro-regulation "consumer" and civil liberties groups—such as the Electronic Privacy Information Center, Consumers Against Supermarket Privacy Invasion and Numbering, and the Privacy Rights Clearinghouse—have called for a wide variety of restrictions on RFID. State lawmakers around the country have introduced anti-RFID legislation, and both Congress and the Federal Trade Commission have held hearings.

RFID "Regulation" Without New Law

A variety of social forces will "regulate" RFID technology long before there is any need for government interference. These forces fall into several categories, including economic incentives, consumer preferences, and existing legal protections.

Economics is the reason why RFID is being deployed in the first place. But just as economics drives RFID forward, it will also narrowly constrain it. Because of cost considerations, the typical RFID tag in the consumer goods environment will be cheap and dumb: just good enough for communicating a small amount of information over a short distance.

The tag itself will be "passive," meaning it will have no internal power source and will work only over short distances. The system will use low frequency signals, which also do not travel great distances, because low frequency systems are cheaper and have better communications capabilities. And the chips in RFID tags will be hard-coded with a small amount of data. They will not have sensors, read-write memory, or other capabilities that are technically possible, though relatively expensive.

Given the cost of collecting, sorting, and storing information, RFID readers will not bristle from every nook of every store or the entries of every building. They will not be routinely networked to cameras for the purpose of observing shoppers (as has been done in some experiments).

Likewise, the design of RFID systems, and the data in them, will be closely guarded trade secrets. Otherwise, RFID would provide competitive information to users' rivals. Because the correlation between tags and goods will not be widely available, burglars will not be able to drive down an alley and determine which house has expensive stereo equipment, one of many "what if" scenarios that have been raised.

Consumer demand, also an economic concept, will constrain RFID in other ways. Consumers may prefer RFID tags in some circumstances, such as when RFID can help return lost or stolen property. They may reject RFID in other circumstances. For example, shoes seem a particularly inappropriate place for permanently embedded RFID because of the potential for unwanted tracking.

And consumer demand goes beyond RFID's mere presence or absence. Consumers may demand RFID tags that can be removed post-sale. Tags might be designed to be "killed" or muted at consumers' request. RFID notices may be the most appropriate response to consumers' desire for information. These are decisions to be made in myriad real-world contexts that will arise as RFID goes forward.

Self-help is another social force that will constrain RFID. If not easily removable by hand, most tags will probably be removable with scissors or razor blades. RFID tags placed in aluminized Mylar bags cannot communicate with readers. And a variety of anti-RFID technologies are already on the drawing boards, including RFID scanner-detectors and RFID jammers.

Consciously or not, people may frustrate attempts at RFID-based surveillance by passing goods among themselves and passing RFID tags to strangers. A tagged item purchased by one person may be gifted, lost, stolen, or donated to charity. People may purposefully conceal RFID tags in others' clothing, bags, and cars, undermining attempts at surveillance by adding dozens of RFID "zombies" to the streets every day.

A variety of social forces will "regulate" RFID technology long before there is any need for government interference.

Finally, existing law protects against any abuses of RFID that may occur. Property rights and laws that protect individual autonomy allow people to refuse RFID on their goods and persons. The privacy torts in most states give people a cause of action if RFID or any other technology is used to invade privacy. If RFID is somehow used to commit identity fraud, burglary, theft, stalking, murder, or conspiracy, that is just as illegal as if any other technology is used to commit these wrongs.

Conclusion

Some activists today embrace a very narrow vision of consumer interests. "Privacy," they seem to believe, entails anything that will frustrate marketing and commerce. But consumers' interests are much broader than that. Along with privacy, consumers want a complex and constantly shifting mix of low prices, convenience, customization, quality, customer service, and other characteristics in their goods and services.

Hemmed in by social forces such as economics, self-help, and existing law, RFID technology will help producers, marketers, shippers, and retailers better understand and serve the full range of consumer desires. In the interest of consumers, RFID should go forward.

Jim Harper is a Washington, D.C. lawyer who runs the privacy advocacy Web site Privacilla.org and Information Age public policy consulting firm PolicyCounsel.Com.

McCain-Lieberman: A Regulatory Pandora's Box

by Marlo Lewis, Jr.

Sen. John McCain (R-Ariz.) recently compared his push for another vote on the Climate Stewardship Act (S. 139), which the Senate rejected 55 to 43 in November 2003, to his seven-year campaign finance "reform" crusade. "It's an old strategy of mine: Force votes on the issues," he said. "Ultimately, we will win." Or, ultimately, he will lose. It is far from certain that McCain will get a rematch on S. 139 in this Congress. But in case he does, I tender the following observations.

Roadmap to Kyoto

The Climate Stewardship Act, co-sponsored with Sen. Joe Lieberman (D-Conn.), is at bottom a political roadmap back to the Kyoto Protocol, the United Nations global warming treaty that the Senate preemptively rejected by a vote of 95-0 in July 1997.

As originally introduced in January 2003, McCain's bill would have required the United States to reduce emissions of greenhouse gases, chiefly carbon dioxide (CO2) from fossil energy use, in two stages: down to 2000 levels by 2010 (Phase I) and 1990 levels by 2016 (Phase II). Though not as restrictive as the U.S. Kyoto target—7 percent below 1990 levels during 2008-2012—Phase II was close enough for government work. Too close, in fact, to have any chance of passing.

In an effort to woo the fence sitters, Sen. McCain, in October 2003, stripped Phase II from the bill. The Senate still rejected it by a vote of 55 to 43, but to McCain, that vote was only round one; and now, he is demanding a rematch.

Radical Break Disguised as "Modest Step"

Proponents will undoubtedly argue, as they did last fall, that we need not worry about the bill's economic impact because Phase I is just a "modest" first step in addressing global climate change. A recent Energy Information Administration (EIA) analysis suggests otherwise. According to EIA, Phase I would increase:

- Gasoline prices by 9 percent in 2010 and 19 percent in 2025;
- Natural gas prices in the industrial and electric power sectors by 21 percent in 2010 and 58 percent in 2025; and,
- Electricity prices by 35 percent in 2025.

Further, Phase I would reduce U.S. GDP by $760 billion during 2004-2025 (or $290 billion in present value). For comparison, consider that Congress has appropriated $135 billion to pay for the war in Iraq.

And the costs do not stop there. Does anyone believe for a moment that enacting Phase I would appease rather than embolden the Kyoto lobby—or that enacting Phase I today would not make it easier to enact Phase II tomorrow? Phase I would impose Kyoto-like emission caps on major U.S. companies. Once subject to such regulation, firms would have an incentive to lobby for the treaty's ratification in order to gain access to Kyoto's emissions credit market.

More importantly, any carbon emissions cap, however "modest," would radically change U.S. national policy. Never before has the U.S. Government regulated energy markets based on the carbon content of fuels or emissions—and for good reason. Carbon dioxide is the inescapable byproduct of the carbon-based fuels—coal, oil, and natural gas—that supply 86 percent of all the energy Americans use. Enact Phase I, and you cross a regulatory Rubicon. From that moment on, the debate in Washington would no longer be about *whether* to suppress carbon-based energy production, but about *how much* and *how fast* to suppress it. There would be no difference in kind between U.S. law and the Kyoto Protocol. Ratification of Kyoto would surely follow.

Even if Kyoto ultimately collapses because Russia declines to ratify, other countries withdraw, or the whole scheme proves unenforceable, McCain-Lieberman would still be a regulatory Pandora's Box. The bill has a built-in escalator clause designed to ensure that Phase I is only the first in a series of energy suppression mandates. Section 336 would require the Undersecretary of Commerce for Oceans and Atmosphere to determine "no less frequently than biennially" whether the bill's emission caps remain "consistent" with the "objective" of preventing "dangerous" human interference with the climate system. In effect, the bill would turn the Department of Commerce—an agency beholden to McCain in his capacity as Senate Commerce Committee Chairman—into a permanent lobbyist within the executive branch for increasingly stringent curbs on energy use.

So when McCain calls his bill "modest," he might as well say, "I just want to put the camel's nose under the tent—what possible harm could there be in that?"

When Sen. McCain calls his bill "modest," he might as well say, "I just want to put the camel's nose under the tent—what possible harm could there be in that?"

Unsustainable Regulation

The harm is that Phase I would lock America into an all-economic-pain-for-no-environmental-gain regulatory regime that can only end in failure. This assessment is confirmed by a seminal study published in the November 1, 2002 issue of the journal *Science*.

The study, co-authored by 18 energy and climate experts, examined possible technology options that might be used in coming decades to stabilize atmospheric CO2 concentrations. Such options include wind and solar energy, nuclear fission and fusion, biomass fuels, efficiency improvements, carbon sequestration, and hydrogen fuel cells. The authors found that, "All these approaches currently have severe deficiencies that limit their ability to stabilize global climate." They specifically took issue with the U.N. Intergovernmental Panel on Climate Change's claim that, "known technological options could achieve a broad range of atmospheric CO2 stabilization levels, such as 550 ppm, 450 ppm or below over the next 100 years."

As noted in the study, world energy demand could triple by 2050. Yet, "Energy sources that can produce 100 to 300 percent of present world power consumption without greenhouse emissions do not exist operationally or as pilot plants." The bottom line: "CO2 is a combustion product vital to how civilization is powered; it cannot be regulated away."

Given current and foreseeable technological capabilities, any serious attempt to stabilize CO2 levels via regulation would be economically devastating and, thus, politically unsustainable. McCain-Lieberman is a dead end. A "modest" step on a journey one cannot complete and should not take is not progress; it is misdirection and wasted effort.

Trick Photography

But, some may ask, "Shouldn't we do something about global warming?" Well, for starters, we should try to understand how much global warming is taking place, and how serious a problem it is. Unfortunately, much of what passes today for "settled" science is misinformation, conjecture, or hype.

Last October's Senate debate on S. 139 provides a memorable case in point. Sen. McCain displayed two satellite photos showing a significant contraction in Arctic ice cover between 1979 and today. To him, this was proof positive that CO2-induced warming was despoiling our beautiful world. "You can believe me or your lyin' eyes," he huffed.

However, Russian meteorological observations from 75 stations going back to 1875 show that the Arctic was warmer in the late 1930s and early 1940s than it is today. Yet most of the buildup in atmospheric CO2 concentrations occurred after 1940. For all we know (satellite photography did not exist 70 years ago), ice cover retreated as much during the 1930s and 1940s as it has in recent decades. What Sen. McCain dogmatically asserts to be a linear trend may in fact be the waning phase of a natural cycle.

Moreover, Arctic ice cover is affected not only by ambient temperatures but also by wind patterns, and whereas the dominant circulation pattern in the late 1950s and early 1960s favored ice buildup, the dominant pattern in the 1980s and 1990s favored expansion of open water. Further, although the Arctic has warmed in recent decades, the climate models underpinning the Kyoto treaty predicted it would warm two to three times as much. The recent warming is within the range of natural variability.

In short, McCain's seeing-is-believing, before-and-after photos do not provide a shred of evidence that CO2 emissions are causing—or are likely to cause—an environmental disaster.

Overall, Sens. McCain and Lieberman propose an expensive non-solution to a greatly overstated problem. The Senate was right to reject this regulatory Pandora's Box the first time it was proposed. Today, with energy prices higher, the decision should be even easier.

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Q & A with Jonathan Zuck:

An Experienced Software Developer, now Head of the Association for Competitive Technology, Comments on Antitrust Policy

Jonathan Zuck, President of the Association for Competitive Technology (ACT), recently shared his thoughts on antitrust policy with CEI. ACT, a national education and advocacy group for the technology industry, focuses on issues such as intellectual property, international trade, e-commerce, privacy, tax policy, and antitrust. It represents nearly 3,000 software developers, systems integrators, IT consulting and training firms, and e-businesses from across the country. Before getting involved in the technology policy debate, Zuck worked for 15 years as a programmer. He has written on technology issues for various publications, including PC Magazine, PC Week, *and* Windows Tech Journal, *as well as in several books. He has spoken at various conferences and appeared on major TV networks, including ABC, CNN, and CNBC. For more information on ACT, go to www.actonline.org.*

CEI: How did you first become involved in antitrust regulation?

Jonathan Zuck: As a software developer rather than a lawyer, I was generally oblivious to antitrust law until antitrust lawyers decided to get "involved" with my industry. The Microsoft antitrust case was my first introduction to the intricacies of antitrust law and the horrifying reality that a few lawyers with no tech experience were trying to tell us how to design software.

CEI: The Association for Competitive Technology (ACT), which you head, advocates for a "healthy tech environment," which it defines as "the collective system of laws, regulations, and court cases that affect the technology industry." Which do you consider to be the tech environment's most important factors and how does ACT measure these factors in its Tech Environmental Quality Index?

Zuck: We believe that the Tech Environment must be judged by its effect on entrepreneurial technology firms. A healthy Tech Environment encourages entrepreneurship and innovation and allows small companies to thrive. With the Tech Environmental Quality Index, we measure the effect on entrepreneurial technology companies based on 10 key factors:

1. Effect cost of doing business (regulations, taxes)
2. Effect on market opportunities
3. Particular effect on small tech firms
4. Whether it takes government out of a market or process
5. Whether it enables small firms to participate in regulatory process
6. Effect on investment (Venture Capital, Wall Street)
7. Effect on innovation
8. Effect on consumer spending
9. Effect on ROI and business spending
10. Effect on workforce growth and employment

CEI: Which specific cases do you consider the most detrimental applications of antitrust law in recent years?

Zuck: Given my focus on the information technology industry, I would point to the Microsoft antitrust case—both here and in Europe—and to the recent attempts to block the EchoStar-DirecTV and Oracle-PeopleSoft mergers. The Microsoft case demonstrated how easy it is for a few disgruntled competitors to hijack the machinery of antitrust enforcement to give them a competitive leg up. More importantly, however, the case highlighted the difficulty in crafting market definitions in an industry with such fluid products and low barriers to entry. The uncertainty created by this case undoubtedly affected the information technology industry as a whole and helped to drag down the entire stock market in the late 1990s.

The Department of Justice's (DOJ) decision to block the merger of EchoStar and DirecTV had devastating effects on the rollout of rural broadband. While DOJ was focused entirely on the effect of the merger on the satellite television market, they ignored the positive impact the merger would have had on broadband rollout. It would have given a joint EchoStar-DirecTV company the capital to put up next-generation satellites capable of providing two-way Internet broadband service to anywhere in the United States—even the most remote locations on the map.

Finally, the Justice Department's decision to block Oracle's proposed merger with PeopleSoft demonstrates just how out of step current antitrust

enforcement is with the realities of the technology industry. In order to create its case, DOJ had to gerrymander a market that includes just two of the enterprise applications technologies the two companies provide—financial management services and human resources—and limits the customer set to essentially the *Fortune* 100. DOJ ignores the fact that there is competition from outsourcing firms for both these technologies, and that there are many competitors focused on the slightly smaller customers that could easily fulfill the needs of the *Fortune* 100.

CEI: Shortly after its ruling against Microsoft, you noted that, "the European Commission is creating an unprecedented regulatory regime that assumes platform innovation is a bad thing," which "will make it difficult for any market-leading company to add new features to dominant products." Do you see this ruling as part of a trend? What do you believe motivates regulators to make decisions like this?

Zuck: I'm not sure that this is a trend, but it could become one if the European Commission (EC) is successful in defending its decision on appeal. In the U.S. case, the non-settling states (those who did not originally join in the Microsoft-DOJ settlement) attempted the same type of legal gymnastics to argue that any new feature added to Windows was inherently a case of illegal tying. The court flatly rejected this argument and the states' proposals to remedy to situation. Despite their rejection by the U.S. courts, these remedies were the inspiration for the EC's decision to force Microsoft to remove Media Player from Windows. As for the motivation, we need to look no further than the same companies that helped push these draconian remedies in the U.S. case. Unfortunately, these disgruntled competitors have been successful in convincing the Commission to do their bidding for them.

CEI: You also noted that the European Microsoft ruling sends the message: "forget innovating, start litigating, and if you fail in America, try Europe." Is globalization complicating the regulatory environment in which many businesses operate? Also, does the European Microsoft ruling indicate a threat to American sovereignty?

Zuck: The fact that globalization is complicating the regulatory environment, especially for antitrust, is unquestionable. Starting with the European Commission blocking the GE-Honeywell merger, the global patchwork of regulatory regimes has become a nightmare for multinational corporations. Differing legal standards and the inherently political nature of antitrust enforcement ensure this problem will only get worse.

In fact, the European Commission's ruling in the Microsoft case signals that this problem has become critical to the future of international business. The Commission's ruling has created a gaping chasm between the antitrust laws of America and the European Union. The Commissioners are arguing that the addition of new features and technologies to a market-leading product is per se illegal, despite the fact that the American courts have taken the exact opposite stance.

CEI: Is antitrust regulation obsolete?

Zuck: Recent history certainly suggests that antitrust regulations need to be revisited. The emergence of the New Economy, the erosion of barriers to entry, and the growing politicization of antitrust enforcement require that we look at ways to modernize the enforcement of these century-old laws. In the fast-moving and fluid markets of the information technology industry, market definitions are best described by Heisenberg's uncertainty principle (the more you examine something, the more you affect it for unpredictable results), thus creating an enormous problem for antitrust enforcers and defendants alike.

We are extremely supportive of the congressional effort to create an Antitrust Modernization Commission to examine these problems. This commission was recently funded and launched. A lot of its members are lawyers, which is troubling, but they have promised to seek a lot of outside contributions.

> The Microsoft case demonstrated how easy it is for a few disgruntled competitors to hijack the machinery of antitrust enforcement to give them a competitive leg up.

CEI: How do government policies affect copyright owners and content distribution companies seeking to pursue new distribution models? What effect will these policies likely have on the future of the online digital content industry?

Zuck: Copyright owners and content distribution companies are hindered by government policies as well as their own previous business practices in their pursuit of new distribution models. First, antitrust laws and threats of prosecution over collusion can make it difficult for intellectual property owners—the suppliers—to join forces to create a new distribution system for their content. Not only has this threat been raised in the music industry efforts to create Internet distribution platforms, but a politically-motivated and ill-advised antitrust investigation nearly capsized airlines' efforts to create Orbitz, the popular online reservation system. Perhaps more troublesome, though, is the intricate web of contracts between performers, songwriters, labels, and others in the music industry. Navigating the rights conveyed by these complex contracts (which often contain veto rights over distribution channels) has proven to be one of the biggest obstacles in the recording industry's move to Internet distribution models.

NAFTA at 10

The North American Free Trade Agreement has Boosted Trade, but the Transnational Bureaucracy it Created Remains in Place

by Ivan G. Osorio

This year marks the 10th anniversary of the North American Free Trade Agreement (NAFTA) among Canada, Mexico, and the United States. As a recent case shows, the issue of environmental policy—central during the treaty's ratification debate—remains relevant.

On June 7, 2004, the United States Supreme Court unanimously dismissed a suit by the Teamsters union, AFL-CIO, and several environmental groups to keep Mexican trucks from entering the U.S. without a review of their impact on air quality. Under NAFTA, the U. S. had pledged to open its border to Mexican trucks by January 2000. However, the Clinton Administration failed to do so, and, in February 2001, a NAFTA international arbitration panel upheld a complaint from Mexico over the issue. But when the Bush Administration moved to open the border to Mexican trucks, a coalition of labor and activist groups sued. (Plaintiffs also included Public Citizen, Environmental Law Center, and Natural Resources Defense Council.)

Obviously, American unionized truckers would prefer to keep out competition from Mexico. Ten years on, NAFTA has significantly increased trade within North America—and helped Mexico's economy. But it also has created a new class of transnational bureaucrats within its dispute resolution mechanisms. As the Mexican trucking case shows, environmental concerns are a powerful tool to hinder trade. And this is not the first time that protectionists have tried to use it.

During NAFTA's ratification debate, CEI and other free market advocates warned about the treaty's side agreements on issues unrelated to trade, especially those dealing with the environment. NAFTA's environmental agreements have set a bad precedent and have had a ratchet effect on regulatory provisions in subsequent trade deals. However, the NAFTA environmental bureaucracies have not been nearly as harmful as they could have been.

With the treaty now in place, U.S. officials should seek to increase the gains in trade, while minimizing the bureaucratic burden the treaty created. This would help the economies of all three North American nations—and their environment as well.

Green Precedent

The environmental bureaucracies created by NAFTA are inimical to expanding trade and likely to push for more regulation. However, because they are bureaucracies, their own slowness has been a blessing for North America.

A NAFTA side agreement—the North American Agreement on Environmental Cooperation (NAAEC)—established a Commission for Environmental Cooperation (CEC), headquartered in Montreal, to facilitate "harmonization" of environmental regulation between the three countries.

It is safe to say that CEC has a strong pro-government regulation bias, as recent statements by two individuals associated with it illustrate. In March, CEC issued a report claiming that genetically modified (GM) corn "threatens" native species of maize in Mexico (some varieties of GM corn have been planted in Mexico despite a ban). The report posits a series of dire possibilities and "unpredictable" effects, without outlining any actual problems. "*One thing* is clear," Chantal Line Carpentier, the study's coordinator, told *The New York Times*. "The huge diversity in Mexico should be protected in situ and in gene banks. *And Mexico does not have the money*." And CEC adviser José Sarukhán, a professor at the Institute of Ecology at the National Autonomous University of Mexico, said, "As long as we don't have regulation, we *need* to have monitoring that will give you an early warning of the presence of transgenic material." [Emphases added]

CEC's original work plan included the elimination of lead, cadmium, mercury, PCBs, and other organic chemicals and metals from the North American economy. As CEI fellow James Sheehan wrote in 1995, "This is the agenda of the U.N. Basel Convention, written into the NAFTA text, which forbids free trade in materials declared 'hazardous' by environmental bureaucrats." Since last year, Mexico has moved to create a tracking system for these substances, with CEC funding a mercury emission inventory.

While CEC has pushed parts of the green agenda, its own bureaucratic sluggishness has kept it from interfering with trade on a large scale. Some of CEC's biggest "accomplishments" include getting Mexico to stop using the pesticide DDT and cracking down on black market sales of Freon. By July 2003, it had received 40 petitions, about half of which it rejected. And, as *The Dallas Morning News* reported last year, CEC can take more than three years to finish a report.

Another side agreement created the North American Development Bank, jointly financed by the United States and Mexico, intended to loan money for building environmental cleanup facilities. By April 2003, the bank had handed out $494 million for 57 projects, including Ciudad Juarez's first wastewater treatment plant. Of that amount, only $59.1 million—12 percent—was in the form of loans. Most of the money disbursed was from U.S. Environmental Protection Agency grants.

At that time, more than $300 million remained in the bank's coffers. A lot of the money has gone unused because of the bank's policy to lend only at market rates, which many

low-income border communities cannot afford, because, as the Sierra Club's Dan Seligman points out, "the border communities by and large don't have a tax base." But the best way to build up a tax base is through economic growth. Further, subsidized loans increase risk of default by extending credit to higher-risk borrowers. The bank started offering low-interest loans in 2002, and has expanded its lending beyond basic infrastructure projects to expensive, feel-good projects dear to green activists like wind-power and energy-efficient buses.

Despite NAFTA's considerable environmental provisions, green activists have not been content with achieving the same in subsequent trade deals. They have pushed to make such provisions even stricter, as evidenced in the recently signed—but yet to be ratified—Central American Free Trade Agreement (CAFTA).

Despite NAFTA's considerable environmental provisions, green activists have not been content with achieving the same in subsequent trade deals.

Environmental activists argue that CAFTA's environmental provisions do not go far enough, even though U.S. and Central American officials completed an environmental cooperation agreement in December 2003—something usually done after the trade agreement is completed—which will focus on "building capacity" for the Central American nations to enact and enforce environmental regulations.

The Real Impact

NAFTA's economic impact began on a sour note, though its long-term effect on trade has been generally positive.

NAFTA contributed to the 1994 currency crisis through the creation of a $6 billion Federal Reserve bailout fund for the peso. As CEI's James Sheehan reported then, "The NAFTA safety net coaxed Americans into buying billions of dollars worth of high-risk Mexican debt, while ensuring that Mexican leaders would not be held accountable if they failed to make payments." Mexico's policies of excessive borrowing and spending caused the peso to crash. And following the crash, the International Monetary Fund put forth another bailout at a cost of $50 billion.

Since, then, however, things have looked better.

Protectionists denounce NAFTA as the facilitator for greedy U.S. corporations to "ship" jobs south of the border. But the fact that the U.S. unemployment rate has not skyrocketed—recently it has hovered around 5.6 percent—makes that claim ring hollow.

While NAFTA has forced some industries to adjust to new competitive pressures, its overall impact has helped the economy. According to Census Bureau figures, from 1993 to 2003, U.S.-Mexico trade increased from $81 billion to $235 billion. And, according to the Federal Reserve, total U.S. industrial output increased steadily from 1993 to 2000—from 3.3 percent in 1993 to a high of 7.4 percent in 1997 and 4.3 percent or higher in other years—only dipping during the 2001-2002 recession, which is now over. While not all of this may be necessarily attributed to NAFTA, it undercuts the argument that NAFTA would ravage American manufacturing.

Today, Canada and Mexico are the United States' first and second largest trading partners, respectively. "We are probably 85 percent into the accord now," says Texas A&M University economist Parr Rosson, "and if its objective was to increase trade, it has certainly done so."

And it is this increased trade that will most likely help improve environmental quality.

The United States and Mexico are now preparing to allow each other's trucks to travel freely on their highways. Opening the border will likely benefit air quality in border areas. Currently, Mexican trucks can travel no more than 20 miles north of the border, must stay within a designated commercial zone, and must transfer cargo to U.S. trucks—usually while idling. Mexican buses must transfer passengers. Opening the border will likely do away with the short-haul, or drayage fleet—trucks that specialize in the short hop over the border, and that are generally of lower quality and more polluting than long-haul trucks. But it was these soon-to-be obsolete drayage trucks that the protectionists pointed to as examples of the kinds of trucks that would operate on U.S. highways.

Further, opening competition is a two-way street. While U.S. trucking firms may face greater competition at home, they will also face new opportunities in Mexico, which currently excludes U.S. trucks in retaliation for the Mexican truck moratorium. And U.S. exporters also stand to benefit. Leon Flores Gonzales, president of Mexico's National Freight Transport Chamber, notes that some smaller Mexican trucking firms are worried about increased competition, but that larger Mexican firms may do well in the United States, especially if they are able to take goods back to Mexico.

Conclusion

Free trade should not require hundreds of pages of treaty text written by lawyers during negotiations in which government officials threaten to punish their own consumers to spite the other guy. It should also not involve creating new transnational bureaucracies. With NAFTA, these deeds are done, but there is good news, too. The treaty's regulatory provisions have been less harmful than expected, due to various factors.

In addition, lower trade barriers have led to increased trade with our neighbors. It is this aspect of NAFTA, and not the unrelated side agreements that statist green activists pushed onto the treaty, that policy makers should seek to expand. Economic growth, not more regulation, will help improve North America's environment.

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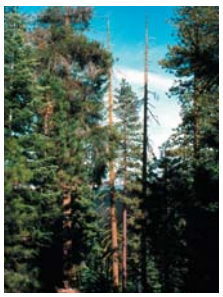
The Good, the Bad, and the Ugly

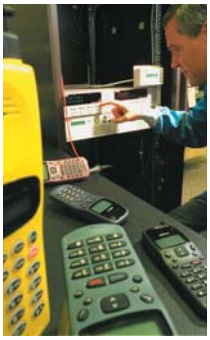
The Good: Bush Administration Takes Steps to Reverse Clinton Roadless Rule


U.S.. Fish and Wildlife Service

On July 12, the Bush Administration announced its first steps to reverse the Clinton-era roadless rule. The rule, a "midnight regulation" enacted in January of 2001, designated 58.5 million acres of the 192 million-acre National Forest System as roadless areas, thereby prohibiting road building, timber harvesting, and effectively eliminating all recreational uses, management, and fire fighting in nearly a third of our National Forests—and overriding Congress' responsibility for proposing, debating, and designating official National Wilderness Areas under the 1964 National Wilderness Act.

"While radical green critics of natural resource use argue that forest roads facilitate timber harvest, provide access to mining claims and permit exploration for oil and gas, they never point out that these roads also provide access for recreationists, campers, hunters, fishers, bird watchers, photographers, and families with children and elderly, and the handicapped to our nearly 200 million-acre National Forest System, set aside for all the people," notes CEI Adjunct Scholar Robert J. Smith. "Furthermore, forest roads are often indispensable for providing access for fire fighters to reach forest fires in time to contain them."

The Bad: Florida Officials Mull Information Technology Tax


Feature Photo Service

Florida state officials are considering taxing computer networks under a modified 1985 state law that was intended to tax the few businesses that used internal communication networks instead of a local telephone company. In 2001 the law was expanded to make any "substitute communication system" taxable by up to 16 percent, which includes a 9.17 paercent state tax plus local option taxes. But the law, as written, could empower the state to tax local telephone calls, wireless services, cable television, two-way radios, and fax machines. "The tax language is so broad that virtually any communications technologies in your home or office could be subject to this tax," argues Chris Hart, spokesman for IT Florida, a nonprofit industry organization for the state's technology professionals. "It's difficult to imagine a more anti-technology, anti-business tax. It directly attacks the efficient use of information technology."

The Florida Department or Revenue is now working to determine how the tax should be implemented. Governor Jeb Bush has said he does not favor the tax. He would be right to kill it. If implemented, the law would give Florida the most wide-reaching state tax on technology—and set a terrible example for other states. "The tax reaches too far," says CEI Technology Counsel Braden Cox. "A state tax on technology will merely stifle innovation and prevent access to the Internet."

The Ugly: Morgan Stanley Caves on U.S.-Funded Activist Suit


Feature Photo Service

On July 12, just before going trial, Morgan Stanley and the Equal Employment Opportunity Commission (EEOC) reached a $54 million settlement to end a sex discrimination suit against the brokerage by a disgruntled former employee. This is the latest in a series of lawsuits filed to change the hiring practices of private firms—and also the latest of a company cowardly caving in before a dubious activist lawsuit.

Former bond trader Allison Schieffelin accused the firm of passing her over for promotions and blatant sexual discrimination. Morgan Stanley said that Schieffelin was denied promotions because she didn't deserve them and that it has "at all times treated its women employees fairly and equitably." But by settling rather than fighting, the firm essentially legitimized Schieffelin's claims, which seem questionable, to put it mildly. The firm fired Schieffelin in 2000, citing a "an abusive confrontation" with her boss—the *woman* who got the job over which Schieffeling sued!

This seems more like a case of blatant activism. On July 28, *The New York Times* described EEOC lawyer Elizabeth Grossman, who handled the case, as someone who has a "a zealot's passion" and who "uses the kind of oratory that often gushes from lawyers who work for banner-waving advocacy groups." "The challenge is to try to make law, and to expand the system to serve employees who are protected by laws," Grossman told the *Times*. "The law is a way of achieving social change."

This is not the first time lawyers have used the courts to implement policy, circumventing lawmakers—and will definitely not be the last. Indeed, Morgan Stanley's refusal to stand its ground will only encourage disgruntled employees everywhere to sue in the hope of reaping windfall settlements from companies worried about a costly trial—of the settlement, Schieffelin gets $12 million, with $40 million going to a court-administered fund for other claims and $2 million for in-house sex harassment programs—while giving activist lawyers new opportunities to push their agendas.

Media Mentions

Vice President for Regulatory Policy Clyde Wayne Crews sheds light on federal regulatory compliance costs:

If Washington can't raise taxes to pay for its ends, it regulates. Indeed, according to Americans for Tax Reform's new Cost of Government Day report, we all worked until July 7—more than half the year—to pay the costs of taxes and regulations.

This is one day earlier than last year, and good news of sorts in that respect—but what of the future? Is it a promising trend, as ATR hopes?

Unfortunately, heavy recent government spending anticipates a regulatory boom. President Bush's education bill heralds greater entrenchment of public over private education and state mandates galore; the Medicare prescription drug benefit means new medical mandates and constraints on doctors and insurers.

- *Investor's Business Daily*, July 27

Adjunct Fellow Soso Whaley exposes the misleading premise behind the anti-corporate documentary *Super Size Me*:

In case you missed it, Morgan Spurlock brought his *Super Size Me* sideshow to Capitol Hill...

Mr. Spurlock talks about his 30-day diet of McDonald's food and the "side effects" he experienced such as weight gain, skyrocketing cholesterol, and a tattered libido. He and his cohorts...seem to believe the only way to address the so-called obesity epidemic is through lawsuits against the fast food industry, limited food choices, "fat" taxes on snack foods, and other such "nanny" measures.

Mr. Spurlock's film focuses more on blaming corporations for Americans being fat, instead of putting the onus on ourselves to take personal responsibility for what we put in our mouths. I also engaged in a 30-day McDonald's diet, with completely different results. Granted, there was a difference in our approach: Mr. Spurlock intended to gain weight and forced himself to gorge as much as possible, eating up to 5,000 calories a day, if not more. My approach included eating 1,800 to 2,000 calories a day and making wise food choices.

I ended up not only losing 10 pounds but also saw my cholesterol drop by 40 points.

- *The Washington Times*, July 24

Senior Fellow Iain Murray re-examines the hysteria over mad cow disease in the UK:

A little over eight years ago, British Secretary of State for Health Stephen Dorrell announced to the House of Commons that scientists had identified a new strain of the fatal brain malady Creuzfeldt-Jacob Disease (CJD) and that they could no longer rule out a link to "Mad Cow Disease" (Bovine Spongiform Encephalopathy or BSE). The implication was clear: Scientists said that British beef was unsafe...The panicked reaction decimated the British beef industry at a cost to the taxpayers of over £3 billion and may have helped bring down the Conservative government. Yet new evidence suggests that the whole disaster was merely a manifestation of the conflicting needs of science and politics.

- *Tech Central Station*, July 20

President Fred L. Smith, Jr. highlights the folly of the latest corporate social responsibility proposal pushed by anti-corporate activists:

In these days of corporate scandal, who can argue against full disclosure on financial statements? But now comes one cockeyed movement that pushes the concept to extremes. It would require executives to guess potential liabilities from environmental and social problems that just might affect their companies, and list them on balance sheets.

I can envision, for instance, that an oil company like Royal Dutch/Shell, as supplier of fuels that supposedly contribute to global warming, would have to report the potential environmental liabilities. How much? A ready estimate can be derived from the movie *The Day After Tomorrow*. As the film ends, half the U.S. population lies frozen beneath a gigantic ice sheet. So let's say $10 billion. Or maybe $100 trillion is a better number. See how ludicrous this gets? Remarkably, this movement is drawing support from Wall Street. In June Goldman Sachs and Morgan Stanley endorsed a report of the United Nations Global Compact that calls upon regulators to "require a minimum degree of disclosure and accountability on environmental, social and governance issues from companies, as this will support financial analysis."

- *Forbes*, July 9

Warren Brookes Journalism Fellow Neil Hrab corrects misconceptions surrounding the debate over corporate outsourcing:

Op-ed pages, political Web sites, and call-in radio shows were abuzz last spring with rants against the "outsourcing" of "U.S. jobs." Most of those critiques were based on the notion that outsourcing is a one-way street: U.S. jobs go from Boise to Bombay, and American workers get nothing in return. But that view is inaccurate. As the *Financial Times* pointed out, the world economy offers lucrative opportunities for "insourcing" by other countries into the United States.

Consider the worldwide demand for the products of America's "copyright" industries—e.g., computer software, music/sound recordings, and motion pictures—that account for a combined $90 billion in annual exports. Consumers abroad are outsourcing their demand to U.S. companies and creating work for Americans. Outsourcing, from this perspective, goes both ways.

- *Regulation*, Summer 2004

Alaska cites Greenpeace for Environmental Law Violation

On July 14, the Alaska State Department of Environmental Conservation cited Greenpeace for breaking environmental laws by failing to submit mandatory oil spill prevention plan documents before entering state waters. The Greenpeace ship Arctic Sunrise, with 27 activists on board, was ordered to anchor until the documents were filed, but the ship resumed its passage in violation of the order and was stopped again.

...END NOTES

Anti-Smoking Strategies from Across the Atlantic

Americans usually think of Europeans as more tolerant of smokers, but recent developments challenge that perception. Switzerland's Federal Health Office is declaring a proverbial war on tobacco, actively considering bans on nearly all tobacco advertising and tobacco companies' sponsorship of sporting events. Health Office head Thomas Zeltner recently urged Swiss law enforcement to crack down on cigarette smuggling—while at the same time endorsing higher cigarette taxes, which are what motivates smugglers in the first place. Meanwhile, in Sweden, in an acknowledged publicity stunt, an organization called A Non-Smoking Generation has covered Stockholm with posters claiming that smoking stunts penis growth, that cigarette filters are filled with mouse excrement, that second-hand smoke is killing birds, and that girls start smoking because they are stupid. "Our lies are so exaggerated that we hope they will make people stop and think, and then come to our website," said a spokeswoman for the group.

Some Good News!

On June 23, a federal appeals court in Florida ruled that a police dog cannot search for drugs on private property without a warrant. A new study by researchers from St. Thomas Hospital in London found that moderate alcohol consumption can help protect women against brittle bone disease. And in France, workers at a German car components factory dealt a blow to the country's 35-hour work week on July 19, when they overwhelmingly approved a plan to work an extra hour a week for the same pay. While the change is modest, it could set an important precedent: It is the first vote of its kind in France, and the vote was nearly unanimous (only 2 percent opposed the proposal).

And Some, er, Other News

In Fort Myers, Florida, the Lee County Sheriff's Office offered a free fishing trip to the deputy who made the most arrests in July. The Canadian postal service recently convinced a pet store chain to stop selling dog biscuits shaped like mail carriers. Baseline, a New York-based management center for senior corporate executives, recently published a study entitled *Canada Firearms: Armed Robbery*, in which it uses Canada's $1 billion gun registry as a case study in incompetence and financial mismanagement. And in Great Britain, the Industry Trust for Intellectual Property, a body that represents some of the world's largest film companies, launched a campaign to convince consumers that when they buy pirated DVDs they are funding terrorists.

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