

Institutional vs. Leadership Requirements for Regional Integration: The European Union, MERCOSUR and Other Integration Schemes Compared

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Finn Laursen
Department of Political Science and European Union Centre of Excellence
Dalhousie University
Halifax, NS, Canada
E-mail: finn.laursen@dal.ca
<http://www.euce.dal.ca>

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Abstract

According to Andrew Moravcsik the EU has tried to secure "credible commitments" by pooling and delegating sovereignty to common institutions. The European Commission and the European Court of Justice (ECJ) have what some scholars call supranational powers. An increasing number of decisions in the Council of Ministers can be taken by a qualified majority vote (QMV). According to other scholars, including Walter Mattli, leadership is important to overcome "collective action problems" in international cooperation. This paper will contrast these different explanations of successful regional integration and compare the EU with integration in South America, MERCOSUR in particular. What is the current state of regional integration in South America? To what extent has MERCOSUR created autonomous common institutions? Have some member states been able to provide leadership, and if so, to what effect? The discussion will be put into a comparative perspective, referring also to other integration experiences in other parts of the world.

Introduction¹

The different integration schemes in the world vary in various ways. They vary in functional scope, institutional set-up, size of membership and impact. The different factors used to explain this variance also vary, from economic gains over geopolitics to learning processes and creation of new collective identities.

If the integration schemes in different parts of the world are so different, are they all *sui generis*? Does it make sense to compare them? Some scholars have argued that they have enough common traits to be comparable. Most often at least they try to create freer trade, if not free trade, between the participating states. Many also try to create freer movement for services and capital. Then they become FTA Plus schemes. One possible way to look at this is that they constitute international regimes, i.e. rules, regulations and decision-making procedures (Krasner, 1983). But, as we shall see, one can argue that at least the European Union (EU) has gone beyond this and become a political system which can make authoritative decisions for the entire group of participants (Easton, 1965; Lindberg and Scheingold, 1970).

Although much integration theory has been developed to explain the European case integration theory has also been used to study integration in other parts of the world, including the Americas, East Asia and the Pacific. In this paper we shall discuss the role of common institutions in economic integration comparing especially the EU, and MERCOSUR.

¹ The theoretical part of this paper relies on earlier publications by the author, especially the introduction and concluding chapter in Finn Laursen (ed.), *Comparative Regional Integration: Theoretical Approaches* (Ashgate, 2003). See also the Spanish version in Laursen 2004. The paper can be seen as a follow up to Laursen 2005a and 2005b.

Game-Theoretic Perspectives

Regional integration efforts can be seen as an effort to overcome a fundamental problem in the relations among sovereign states, namely that of defection. According to classical international law states are sovereign. They do not have to accept supranational institutions. The international system is seen as anarchic. States can of course conclude agreements with other states, bilaterally or multilaterally; but once they find that conditions have changed, they are no longer bound by such agreements. They may be tempted to cheat to gain more for themselves relative to their partners. International agreements, therefore, can be fragile and unstable as long as they are based on the classical notion of sovereignty.

Modern game theory discusses this in a formal deductive fashion. The famous Prisoners' Dilemma game illustrates the situation where individually rational actors, which could be states, arrive at sub-optimal outcomes if they act independently. Further, the theory shows that agreements, which should realise optimal outcomes, will often be unstable because actors will be tempted to cheat or defect from the cooperative agreement to realise outcomes that are better for themselves in the short run (Brams, 1975; Stein, 1990; Taylor, 1987).

Post-war efforts at international cooperation among industrialized countries in the economic area can be seen as a response to the protectionism - and beggar-thy-neighbour policies - of the 1930s. Free trade, it can be argued, will normally be in everybody's interest. Yet, it is not so easy to realize. The states tried through the General Agreement on Tariffs and Trade (GATT) – now part of the World Trade Organization (WTO) - to facilitate and increase international trade. Yet, trade conflicts have remained an important aspect of relations among the industrialized countries (Grieco, 1990; Conybeare, 1987; Gilpin, 1987).

The experience of the original European Communities (EC) is instructive in this respect. The EC first of all started as a customs union, which should lead to free trade among its members (and introduce a common tariff towards third countries). But once the customs union was in place (1968) it gradually became clear that a customs union is not sufficient to realize free trade. Member States could continue to protect their national industries through non-tariff barriers to trade (NTBs). Some of these were technical barriers to trade like different national standards for products (Pelkmans and Winters, 1988).

A number of cases followed. Many of these eventually were taken to the European Court of Justice (ECJ), which sometimes called for changes in national legislation or practices.

The EC's Internal Market project of the late 1980s can be seen as a renewed effort to overcome Prisoners' Dilemma situations. In the Single European Act (SEA) the Member States accepted the use of qualified majority voting (QMV) in the Council of Ministers to complete the Internal Market. The Commission under Jacques Delors also played a leadership role.

These elements of an independent Commission and QMV in the Council add up to what has been called supranationality (Keohane and Hoffmann, 1991). The Commission is an independent European body; it is there to represent and further the European interest. National interests are represented in the Council; but to the extent that QMV is accepted in the Council, no single member can stop the adoption of measures they do not like. One of the problems of traditional intergovernmental cooperation and the rule of unanimity is that the slowest members will normally determine the speed. Under such form of cooperation one should expect decisions to be based on the lowest common denominator. The EC on the other hand has created institutions that facilitate the "upgrading of the common interest" it was argued early on (Haas, 1961).

Another important institutional element in the EU is the ECJ which makes binding decisions. Community law is different from traditional international law. It has primacy if it conflicts with national law; and much EC legislation has direct effect (Louis, 1990).

If we compare the EU with other regional integration organizations some of these institutional differences become apparent. None of the other regional schemes have created independent supranational bodies like the EU Commission; none of them have accepted anything resembling Community law and real limits on their sovereignty in the form of binding majority decisions (see also Feld and Boyd, 1980; Jamar, 1982). In the EC there has been a pooling and delegation of sovereignty. According to Moravcsik this is done to assure 'credible commitments' (Moravcsik, 1998). Some scholars talk of 'supranational governance' when they describe the EU (Sandholtz and Stone Sweet, 1998). At least one scholar has also described the institutional setup of NAFTA as 'supranational governance' (Gruber, 2000). Yet NAFTA's institutional set-up falls very short of the EU institutions. And the institutions of the ASEAN Free Trade Area (AFTA) are even weaker. How does MERCOSUR fit in here?

Integration is not only about getting optimal outcomes, i.e. efficiency. There is also an element of redistribution in integration schemes. The game that can illustrate this is the Battle of the Sexes. Whereas the question about efficiency is the question of reaching the Pareto-frontier, the question of distribution is where you end up on the Pareto-frontier. An element of power enters the equation. Whereas liberal institutionalists scholars have looked at efficiency, realists and neo-realists have emphasized the question of power and distribution (Krasner, 1991, Little, 1997).

Among integration theories inspired by game-theoretical approaches we especially find Andrew Moravcsik's liberal intergovernmentalism and the contribution by Walter Mattli.

Liberal Intergovernmentalism and Mattli's analytical framework

Andrew Moravcsik's framework suggests three stages in integration studies, first national preference formation, then interstate bargaining and finally institutional choice (Moravcsik, 1998). The model is simple and could in principle be used to study integration in other parts of the world than Europe. Indeed, Moravcsik basically sees the EU as an international regime.

In this paper on institutions we are especially interested in stage three in Moravcsik's framework, namely institutional choice. The questions asked concern the reasons why states choose to delegate or pool decision-making in international institutions. Delegation in the EU refers to the autonomous powers given to the Commission and the European Court of Justice. Pooling of sovereignty refers to the application of majority decisions, especially in the Council of Ministers. To explain institutional choice Moravcsik contrasts three possible explanations: Federalist ideology, centralized technocratic management or more credible commitment. The answer he arrives at is that states delegate and pool sovereignty to get more credible commitments.

Walter Mattli has dealt with regional integration from a comparative perspective, comparing European experiences, including older ones, with experiences in other regions of the world. To explain regional integration both Moravcsik and Mattli emphasize demands from society as well as supply from politicians. Interstate bargaining determines supply in Moravcsik's framework. Mattli puts more emphasis on leadership, i.e. "the presence of an undisputed leader among the group of countries seeking closer ties:"

Such a state serves as a focal point in the coordination of rules, regulations, and policies; it may also help to ease distributional tensions by acting as regional "paymaster" (Mattli, 1999, p. 14).

Successful integration then depends on both demand from market actors and supply from political actors. Willingness to supply integration “depends on the payoff of integration to political leaders” (Ibid., p. 13). On the supply side both “commitment institutions” (such as the Commission and ECJ in Europe) and an institutional leader are mentioned, but the latter is considered most important. Mattli mentions ‘centralized monitoring and third-party enforcement’ as examples of commitment institutions, and says,

The provision of such institutions is one supply condition for successful integration, but it is a weak one. In its absence, cooperation may still be possible on the basis of repeat-play, issue-linkage, and reputation. Nevertheless, “commitment institutions” can catalyze the process of regional integration, particularly if they offer direct access to those actors with the greatest vested interests in seeing integration completed (Ibid., p. 14).

Concerning the regional paymaster this role was played by Prussia in the German *Zollverein* in the 19th century. It is argued that Germany has played such a role in the EU. A central question on the supply side is how to overcome collective action problems associated with both Prisoners’ Dilemma and Battle of the Sexes games. There must be mechanisms to deal with the temptation of defection as well as distributional inequities. In the case of NAFTA Mattli argues that the United States has been the regional leader. But in cases where there has been no undisputed leader, such as ASEAN and the Andean Pact, coordination problems ‘are likely to be insurmountable. Two or more potential leaders in a group can also be a problem. APEC, where the United States and Japan are seen as contending leaders, is mentioned as an example (ibid., pp. 56-57).

Mattli has illustrated the varying outcomes of integration in a figure that we reproduce in slightly shortened version (Table 1).

Leaving out some of the integration schemes studied by Mattli we notice that he has the EU, NAFTA and EFTA until 1973 with highest success rate (1973 was the year the UK and Denmark left EFTA to join the EC). The lowest success rate is given to the Central American Common Market (CACM) after 1969, ASEAN, the Economic Community of West African States (ECOWAS), LAFTA and the Andean Pact. In the middle groups we find two contemporary schemes, the Asia Pacific Economic Cooperation Forum (APEC) and MERCOSUR.

Table 1: Outcomes of integration schemes

		(Uncontested) regional leadership	
		Yes	No
(Potential) market gains from integration	Relatively significant	3 EU NAFTA EFTA (until 1973)	2 EFTA (after 1973) APEC MERCOSUR
	Relatively insignificant	2 CACM (until 1969)	1 CACM (after 1969) ASEAN ECOWAS LAFTA Andean Pact

Success rate: 3 highest
1 lowest

Source: Adapted from Mattli (1999), p. 66.

The Mattli framework for studying regional integration has the clear advantage of simplicity, singling out a small number of variables as decisive for the success of integration. It pays equal attention to demand and supply factors. The role of ‘commitment institutions,’ however, takes second place in Mattli’s theory, and it is not mentioned in the table. Still we believe that the study of ‘commitment institutions’ deserves to be advanced.

Degrees of Economic Integration

We mentioned at the outset that the EU has gone much further than other integration schemes. One way to look at this is to use the steps suggested by economists.

Most integration schemes involve some economic integration. Economists distinguish between various stages of economic integration. Bela Balassa’s classic five steps of economic integration are given in table 2.

Willem Molle has introduced some further distinctions, giving the following stages of economic integration: free trade area, incomplete customs union, customs union, incomplete common market, common market, economic union, monetary union, economic and monetary union, political union and full union. Political Union is reached when ‘integration is extended beyond the realm of economics to encompass such fields as anti-crime policy (police) and foreign policy, eventually including security policy.’ Full union involves ‘complete unification of the economies involved.’ A full union is likely to involve social security, income tax and macro-economic and stabilisation policy. The latter ‘implies a budget of sufficient size to be effective as an instrument of these policies.’ The end of the continuum thus is ‘some form of a confederation or federation’ (Molle 1994, p. 12).

Table 2: Balassa’s Categories of Economic Integration

	No Tariff or Quota	Common External Tariffs	Free Flow of Factors	Harmonization of Economic Policies	Unification of Policies, Political Institutions
Free Trade Area	X				
Customs Union	X	X			
Common Market	X	X	X		
Economic Union	X	X	X	X	
Total Economic Integration	X	X	X	X	X

Source: Nye, 1971, p. 29.

Applied to the different integration schemes in the world it is clear that the EU has moved towards the last steps, unification of policies and creation of political institutions, while most other schemes try to establish free trade. The Maastricht Treaty included the plan for Economic and Monetary Union (EMU). Among the 15 member states before the big enlargement in 2004 twelve had introduced the single currency, the euro. This has not made the EU a fully-fledged federation. The EU has not gone very far in the fiscal policy area, but the Stability Pact sets requirements for national fiscal policy. Some harmonisation of taxation policies has been tried, but with limited

success. Taxation, including spending for social welfare, remains largely a national responsibility. The EU budget can maximum take 1.27 percent of the EU GDP.

On the political side the EU deals with foreign, security and lately also defence policies as well as Justice and Home Affairs Co-operation, the latter including police co-operation. As such the EU has become a political union, but the EU remains rather weak in these political areas where the Member States have been unwilling to transfer sovereignty to common institutions. Consensus or unanimity still dominates in 'high politics' areas and the Commission and ECJ gets less involved than in economic matters.

Looking at integration in other parts of the world many integration efforts include at least efforts to create free trade. This is clearly the case of NAFTA, MERCOSUR and the ASEAN Free Trade Area (AFTA). Many of these efforts began in the late 1980s and early 1990s and could be seen as responses to the internal market programme in Europe and to some extent the difficulties of concluding the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). Facilitation of investments is often a part of these schemes, too. There may also be provisions about services. NAFTA also has so-called side-agreements on environment and labour policies. But most states hesitate a lot about free mobility of persons. The EU has realised the four freedoms as part of the internal market: free movement of goods, capital, services and persons. None of the other integration schemes have gone so far in establishing a common market, but at least the Mercosur aims in that direction (E.g. Coleman and Underhill, 1998; Fawcett and Hurrell, 1995; Gamble and Payne, 1996; Haggard, 1995 and 1997; Kahler, 1995; and Lawrence, 1996).

International Regimes and Supranational Polities

Integration schemes usually involve a certain degree of joint-decision making and the creation of some common formal institutions. As such they all involve the creation of regional international regimes.

Back in the early 1980s Stephen Krasner gave what has become known as the consensus definition of international regimes:

Regimes can be defined as sets of implicit or explicit principles, norms, rules, and decision-making procedures around which actors' expectations converge in a given area of international relations (Krasner, 1983, p. 2).

Neo-liberal institutionalists, especially Robert Keohane, have dealt with the role of institutions. When writing about international institutions in 1989 he argued that institutions affect states in three ways;

1. the flow of information and opportunities to negotiate;
2. the ability of governments to monitor others' compliance and to implement their own commitments – hence their ability to make credible commitments in the first place; and
3. prevailing expectations about the solidity of international agreements (Keohane, 1989, p. 2)

The concept of credible commitments was later used by Andrew Moravcsik in his effort to explain institutional choice in the EU (Moravcsik, 1998). The EU has gone much further in pooling and delegating sovereignty than other integration schemes or wider international regimes such as the General Agreement on Tariffs and Trade (GATT), now embedded in the World Trade Organization (WTO). Is such pooling and delegation of sovereignty necessary to get credible commitments? And where do MERCOSUR, NAFTA and AFTA fit in?

In recent years we have seen an institutionalist turn in social sciences and studies of European integration (see for instance Aspinwall and Schneider, 2000). ‘Institutions matter’ we are told. If so, different institutions presumably matter differently. Neo-functionalists, inspired by one of the EU’s founding fathers, Jean Monnet, have tended to be sceptical about the possibility of creating ‘credible commitments’ through classical intergovernmental institutions.

Keohane suggested ‘institutional variation’ over three main kinds of institutions, viz. conventions, international regimes and international organisations. ‘Variations in degrees of institutionalization exert substantial effects on state behaviour,’ he said. Secondly, for an institutionalist perspective to be relevant, ‘the actors must have some mutual interests’ (Keohane 1989, p. 2). These propositions can be tested further in regional integration studies.

To apply Keohane’s distinctions from 1989 to the EU we need to add some further distinctions. Jean Monnet mentioned the ‘negative experience of international co-operation, whose institutions were incapable of decision-making.’ He therefore proposed ‘a joint sovereign authority’ for the first European Community, the European Coal and Steel Community (ECSC) in 1950 (Monnet, 1978, p. 295). He also wanted to ‘abandon the unanimity rule in favour of a new system in which, to everybody’s advantage, the idea of the common interest would replace that of the national interest – or rather, the national interests of six separate countries’ (Ibid., p. 353).

None of the other integration schemes or international regimes in the world have gone so far in the direction of giving common institutions ‘supranational’ powers. In that sense the EU is certainly *sui generis*, and some scholars have argued that the EU is more than an international regime (or international organisation), but less than a federal state (e.g. Wallace 1983).

Writing about the EC in 1991 Keohane and Hoffmann echoed this:

1. The EC is best characterized as neither an international regime nor an emerging state but as a network involving the pooling of sovereignty.
2. The political process of the EC is well described by the term “supranationality” as used by Ernst Haas in the 1960s (although not as often used subsequently) (Keohane and Hoffmann, 1991, p. 10).

In comparisons between the EU and other regional institutions we therefore need to add supranational institutions to those mentioned by Keohane in 1989.

On Keohane’s other axis, mutual interest, we could use a rationalist game theoretic perspective, starting with conflicting interests (Deadlock) over dilemmas of common interests (Prisoners’ dilemmas) via dilemmas of common aversions, especially co-ordination games with distribution problems (Battle of the Sexes) to situations of no conflict (Harmony) (see especially Stein 1982, and Krasner 1991, but also Grieco 1988 and Snidal 1991).

In Prisoners’ Dilemma (PD) situations good institutions are required to get Pareto-efficient solutions. Under the Battle of the Sexes (B of S) institutions have to contribute to solving problems of distribution. In the case of Simple Co-ordination Games (SCG) there are neither problems of defection nor distribution. So no regimes are needed. When there are fundamental conflicts of interests (Deadlock) no co-operative institutions will emerge. Nor are they needed at the other end of the continuum in situations of harmony.

The suggestion is that the configuration of interests (or preferences) structures different kinds of situations that affect the institutional requirements if joint decision-making is to take place. The two fundamental situations requiring good institutions are, to use Stein’s terminology, the dilemmas of common interests, where the issue is one of reaching efficient solutions, and dilemmas of common aversions, where the problem is one of distribution.

We have tried to summarise the essentials of the argument in Table 3. In pure conflict situations it is limited what institutions can do. Some convergence of interests will have to take place before there can be cooperation. At the other end, harmony of interests require no institutionalisation. ‘Parallel unilateral action’ as advocated in East Asia and within APEC should be sufficient. The problem for AFTA and APEC may be that harmony of interests does not necessarily exist. Domestic pressures have made it impossible for APEC to progress towards freer trade in sensitive areas. AFTA has done somewhat better during the 1990s.

Simple co-ordination problems – like whether to drive on the left or right side of the road – requires decisions, but no elaborate regimes. They are basically self-executing once decided upon. It is suggested that the so-called Open Method of Co-ordination (OMC) invented by the EU and applied to employment policy under the Amsterdam treaty and a number of issues under the so-called Lisbon Strategy of 2000 can solve simple coordination problems. The Lisbon Strategy set the strategic goal for the EU ‘to become the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion.’ It is a good question, however, whether the problems the EU is trying to solve with the OMC are all simple co-ordination problems. So far progress seems to have been limited.

Table 3: Nature of Issues and Institutional Requirements

Nature of issue	Conflicting interests/pure conflict	Dilemmas of common interests (PD) Temptation to defect	Co-ordination problem with distributional issues	Simple co-ordination problem	Harmony of interests
Institutional requirements	Institutions to no avail Convergence of interests required	Pooling and delegation of sovereignty Sanctions against defection	Pooling and delegation of sovereignty Budgetary means	Open Method of Co-ordination (OMC) sufficient	Institutionalisation not necessary ‘Parallel unilateral action’ sufficient

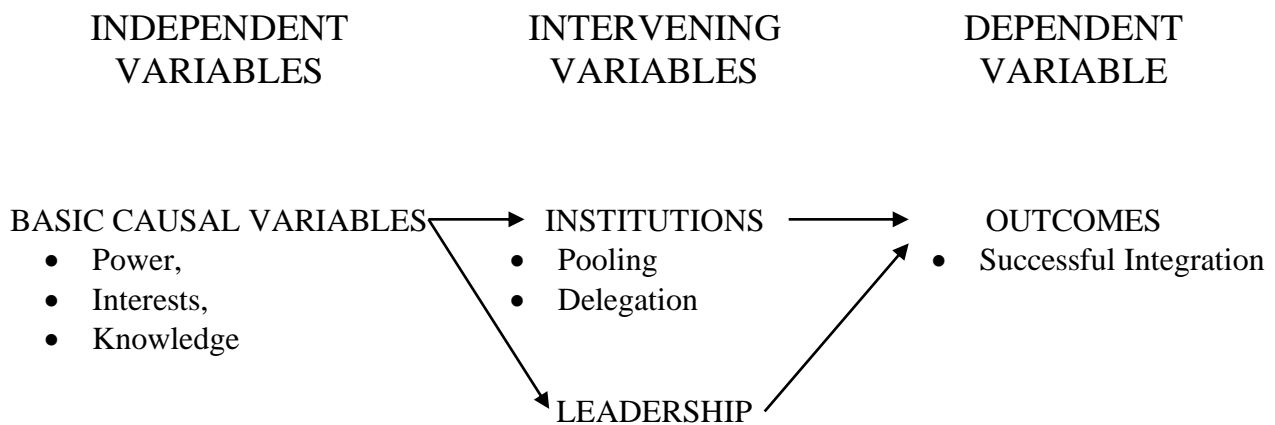
Source: Compiled by the author

Used in a comparative perspective this raises the question whether other mechanisms than pooling and delegation of sovereignty can provide for ‘credible commitments’ when there are temptations to defect from agreements or distributional inequities follow from integration. The most obvious candidate for such mechanism is leadership (or hegemony), as we saw Mattli suggesting. A number of scholars have seen leadership as an important variable in processes of integration (e.g. Lindberg and Scheingold 1970). Thomas Pedersen has studied the role of France and Germany in the European integration process. These two countries have performed a kind of ‘co-operative hegemony’ he suggests (Pedersen, 1998).

A possible way to look at the relationship between institutions and leadership is to suggest that they both are intervening variables. This would give a basic research design like the one suggested in fig. 1. But it could also be the case that leadership is important in the process of establishing institutions, which would create a longer causal chain. Without going into further discussions of the logic of comparative research the suggestion is that comparison of a number of

regional integration schemes should be able to advance our knowledge of the respective roles of institutions, including in particular supranational institutions, and leadership.

Figure 1: RESEARCH DESIGN: A Modified Structural Model



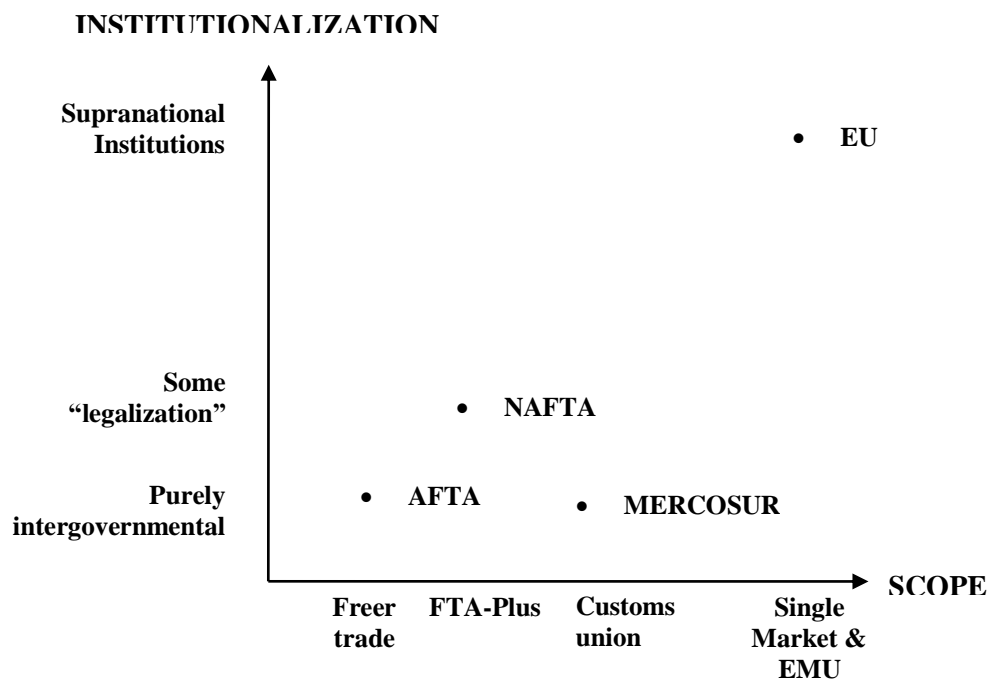
Source: Compiled by the author with inspiration from Krasner, 1983, p. 8

The dependent variable, ‘successful integration’, would in a comparative study mean ‘freer trade’. To what extent do the participants succeed in abolishing tariffs and non-tariff-barriers to trade (NTBs)? Do they succeed moving further in the stages suggested by Balassa? One can also ask, do they succeed in achieving the declared goals?

One could then also ask about the impact of ‘freer trade’. Should we for instance expect increased intra-regional trade in relation to total trade? Extra-regional trade could well increase at the same time because of parallel efforts through GATT/WTO to create freer trade in the world.

In figure 2 we try to illustrate the relationship between institutionalization and scope of integration in MERCOSUR, AFTA, NAFTA and the EU. To what extent is that relationship causal? And if it is, how can one actually prove it?

Figure 2: Institutionalization and Scope of Integration in MERCOSUR, AFTA, NAFTA and the EU



Source: Compiled by the author.

The Case of MERCOSUR

The Southern Common Market (MERCOSUR) was founded by Argentina, Brazil, Paraguay and Uruguay by the Treaty of Asunción of 21 March 1991 (MERCOSUR, 1991a). The preamble said that expansion of domestic markets, through integration, was a vital prerequisite for accelerating economic development. More specifically the purpose was to establish a common market. This would involve

The free movement of goods, services and factors of production between countries through, inter alia, the elimination of customs duties and non-tariff restrictions on the movement of goods, and any other equivalent measures;

The establishment of a common external tariff and the adoption of a common trade policy in relation to third States or groups of States, and the co-ordination of positions in regional and international economic and commercial forums,

The co-ordination of macroeconomic and sectoral policies between the States Parties in the areas of foreign trade, agriculture, industry, fiscal and monetary matters, foreign exchange and capital, services, customs, transport and communications and any other areas that may be agreed upon, in order to ensure proper competition between the States Parties;

The commitment by States Parties to harmonise their legislation in the relevant areas in order to strengthen the integration process (Article 1).

This can be summarized as first of all a customs union with a common trade policy. Beyond that the goal was also a common market which would be based on co-ordination of policies in specific areas, including money, as well as harmonization of legislation. In the Balassa scheme (see Table 2) this might take MERCOSUR towards an economic union. But were the commitments credible?

Nowadays MERCOSUR is often referred to as an incomplete customs union. So there is still a long way to the ultimate declared goal.

Institutional Setup

The Treaty of Asunción established two main institutions (Article 9):

- (a) The Council of the common market
- (b) The Common Market Group.

The Treaty specified that “The Council shall be the highest organ of the common market, with responsibility for its political leadership and for decision-making to ensure compliance with the objectives and time-limits set for the final establishment of the common market” (article 10). As to composition it was specified that “The Council shall consist of the Ministers of Foreign Affairs and the Ministers of the Economy of the States Parties.” It would meet “at least once a year with the participation of the Presidents of the States Parties” (Article 11). A rotating presidency was foreseen (Article 12).

As for the Common Market Group, it was defined as “the executive organ” and it would have “powers of initiative.” It would propose specific measures for applying the treaty, monitor compliance and “take the necessary steps to enforce decisions adopted by the Council” (Article 13). It would be composed of four members and four alternates from each member state, representing the Ministry of Foreign Affairs, Ministry of Economy or its equivalent and the Central Bank (Article 14).

The treaty also established an “administrative secretariat” in Montevideo to service the Common Market Group (Article 15).

How were decisions to be made by the two institutions, the Council and Common Market Group? By “consensus” (Article 16). So there was no pooling of sovereignty.

Was there delegation of sovereignty? No. The organizational structure established by the Treaty of Asunción did not foresee autonomous supranational institutions like the European Commission or the European Court of Justice (ECJ). The established organs were purely intergovernmental.

The Treaty of Asunción lacked a section on dispute settlement. This issue was dealt with by the Protocol of Brasilia for the Solution of Controversies, adopted on 7 December 1999 (Mercosur, 1999b). It foresaw three possible steps: direct negotiations, participation of the Common Market Group and arbitration. If the first two were not successful an ad hoc Arbitral Tribunal could be established. It would have three members and make binding decisions (Article 21). The Protocol of Brasilia also had a section on private party complaints. Private parties would have to “file their complaints with the National Section of the Common Market Group of the State Party wherein they maintain their usual residency or which is the headquarters of their business” (Article 26). So private parties did not have direct access to the dispute settlement mechanisms.

The Treaty of Asunción specified a transition period until 31 December 1994. By then “the final institutional structure of the administrative organs of the common market, as well as the specific powers of each organ and its decision-making procedures” should be determined (Article 18).

The Protocol of Ouro Preto of 17 December 1994 added more institutions and was more specific (MERCOSUR, 1994). It listed six organs (Article 1):

- I. The Council of the Common Market (CCM)
- II. The Common Market Group (CMG)
- III. The MERCOSUR Trade Commission (MTC)
- IV. The Joint Parliamentary Commission (JPC)
- V. The Economic-Social Consultative Forum (ESCF)
- VI. The MERCOSUR Administrative Secretariat (MAS).

The first three in the list were referred to as “inter-governmental organs with decision-making powers” (Article 2). The first would make binding Decisions, the second would make binding Resolutions, and the third would make binding Directives or Proposals. (Articles 9, 15 and 20).

The new MERCOSUR Trade Commission would be composed of four members and four alternates from each State Party, to be coordinated by the Ministries of Foreign Affairs (Article 17). It would monitor, propose, analyse and also take some decisions (Article 19). Further, it would “be responsible for considering complaints referred to it by the National Sections of the Mercosur Trade Commission and originated by State Parties or individuals, whether natural or legal persons” (Article 21). So it would have some functions similar to those of the European Commission without getting its independence as well as a judicial function without approaching anything resembling the ECJ.

The Joint Parliamentary Commission would represent the parliaments of the States Parties. It would have an equal number of members representing each State Party, to be appointed by the respective national parliaments. It would be able to make Recommendations (Article 22-26). So it was not given any real political, budgetary or legislative powers. So it was a weak body compared with the European Parliament, which started out as a consultative assembly, but which was gradually empowered over the years, to become a real co-legislature in the Treaty of Maastricht.

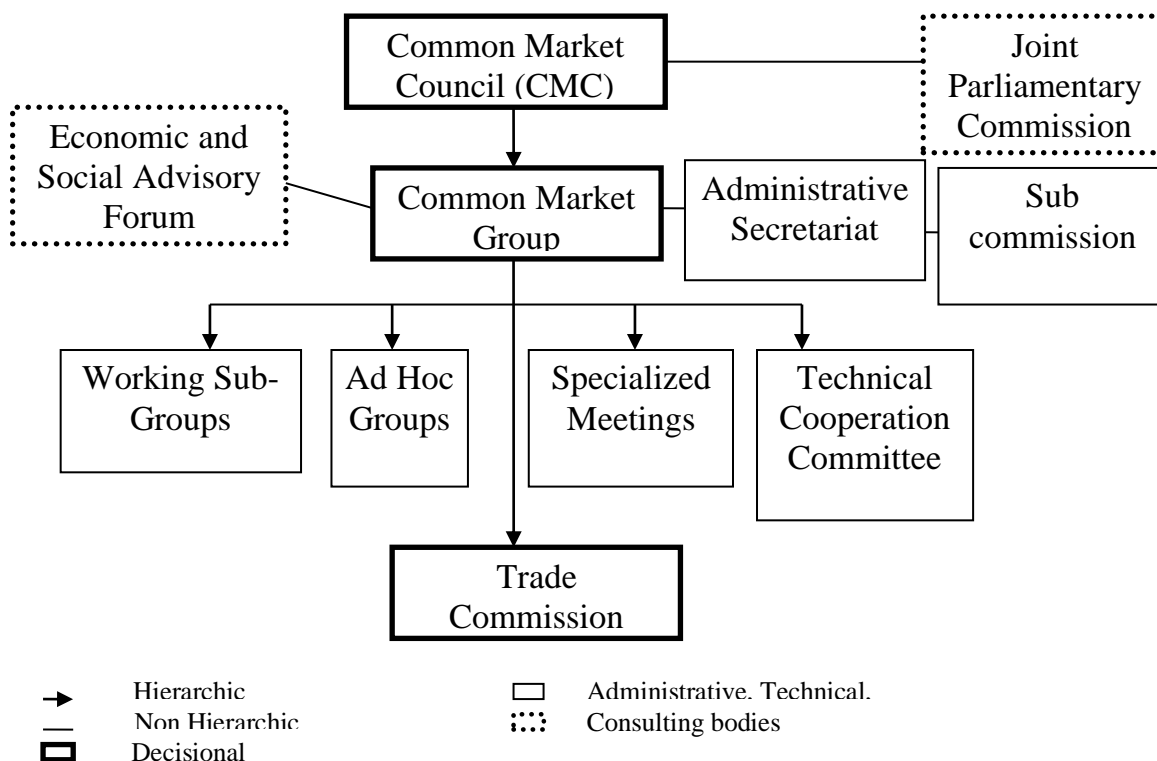
The Economic-Social Consultative Forum would represent “the economic and social sectors”. It would be able to make recommendations (Article 28 and 29).

The Mercosur Administrative Secretariat would provide operational support, “providing services to the other Mercosur organs” (Article 31). It would be headed by a director (Article 33). It would have a budget, “funded by equal contributions from the State Parties” (Article 45).

The Protocol of Ouro Preto also gave “legal personality” to MERCOSUR (Article 34).

An annex to the Protocol established a General Procedure for Complaints to the MERCOSUR Trade Commission. If consensus cannot be reached in the MERCOSUR Trade Commission the case goes to the Common Market Group. If no consensus can be reached there, the case may go to an Arbitration Tribunal, as foreseen in the Brasilia Protocol. Needless to say, mediation and arbitration are weaker mechanisms of dispute settlement than binding court decisions.

Figure 3: The Initial Institutional Structure of MERCOSUR (Simplified)



Source: Malamud, 2003, 55.

Between 1994 and the beginning of the 2000s there were various institutional changes, none of them radical. This is a list summarising these changes given by one source (Pena and Rozemberg, 2005):

- Consultation and Political Consensus-Building Forum (1998). This body is composed of high-level officials from Foreign Ministries. Its aim is to consolidate and expand the political dimension of MERCOSUR.
- Meetings of ministers. This allows sectoral meetings of ministers, such as industry, agriculture, environment, education, etc.
- Commission of Permanent Representatives of MERCOSUR. Created in October 2003 this body assists the Council and the President *Pro Tempore* in all activities required of it. It is composed of a Permanent Representative from each member state as well as one president.
- Permanent Review Court. It was created by the Olivis Protocol in February 2002 (MERCOSUR, 2002).
- Administrative Labour Court. This body deals with complaints by MERCOSUR Secretariat officials and their employees.

But institutional changes and additions have continued:

In 2003 the Administrative Secretariat was changed into a technical organ, the MERCOSUR Secretariat (Caetano et al, 2009, 39).

In 2005 a MERCOSUR Structural Convergence Fund was created (INTAL, 2009).

In 2007 a Consultative Forum of Cities and Regions was created. It had been decided to create it in 2004 (Caetano et al., 2009, p. 57)

Similarly it was decided in 2004 to create a MERCOSUR Parliament (Parlasur). In 2007 it replaced the Joint Parliamentary Committee. After a first stage, 2007-2010, where each member state will have equal representation of 18 members, a second stage with direct elections and proportional representation, 2011-2014. The Constitutive Protocol foresees a lot of functions, including declarations, recommendations and proposals to the Common Market Council. The Parliament has not been given legislative budgetary, powers or control powers (Caetano et al., 2009, 63-70).

Institutional Capacity

In an account by two Mercosur experts three things were emphasized the major institutional traits of MERCOSUR:

1. Its strong inter-governmental bias
2. The “incomplete” character of its organs’ legal acts, and
3. The absence of an independent jurisdictional body (Bouzas and Soltz, 2001)

The intergovernmental nature of MERCOSUR institutions is made very clear in the Treaty of Asunción and its protocols. Bouzas and Soltz have the following verdict on the Common Market Council:

Over time, the credibility and effectiveness of CMC meetings diminished. The growing difficulty to iron out differences in lower decision-making layers led to issue-congestion and an over-burdened agenda at the top. The credibility of Presidential summits, that also started as important “signalling” events, also suffered as failures to implement and agree on pending issues mushroomed since the mid-nineties. The regular intervention of the heads of state in trade and policy disputes (christened as “presidential diplomacy”) served at critical times to unlock blocked negotiations or de-escalate conflict. However, as implementation and follow-up were usually poor, this method over-exposed top political leaders and ultimately damaged credibility (Ibid., no pagination)

The MERCOSUR Trade Commission added in 1995 would eventually suffer from many of the same problems as the Common Market Council and its subcommittees. Overall, it is clear that intergovernmentalism has difficulties overcoming collective action problems. Bouzas and Soltz put it this way:

The intergovernmental structure of MERCOSUR made the process flexible and cost-effective at the initial stages. However, it also stimulated governmental (and executive) “encapsulation”, limiting the permeability of the decision-making process to non-governmental actors (Ibid).

The question concerning the “incomplete” legal acts referred to the fact that they had neither immediate applicability nor direct effect. MERCOSUR acts have to be transposed (“internalised”)

through domestic legislative or administrative acts the same way other international law has to be transposed. This contrasts with the direct applicability of Regulations in the EU and direct effect of most EU legislative acts. In MERCOSUR “the process of transposition has been slow, uneven and highly vulnerable to the good will” of the governments. Efforts to improve transposition in 1998 “had very limited impact upon performance.”

Finally, concerning the Brasilia Protocol’s Dispute Settlement mechanisms Bouzas and Soltz mentioned especially three problems:

One has been the possibility of delayed negotiations: if member states agree, they can extend the mandatory fifteen-days term to undertake bilateral negotiations in the CMG almost indefinitely. In practice, this means that the triggering of third-party adjudication procedure can be delayed and replaced by political and diplomatic bargaining.

(....)

A second problem has been that the *ad-hoc* character of the tribunals conspires against the development of a “body of common interpretation”.

(....)

Finally, there is the critical issue of enforcement. Although the verdict (sic) of the *ad-hoc* tribunals are formally final (they are not subject to an appeal procedure) and binding, the practical meaning of “binding” in each member state differs according to the domestic constitutional background (ibid).

It remains to be seen whether the creation of a Permanent Review Court in 2002 will be able to deal with the second problem.

A Mattli Inspired Perspective: demand and supply factors in the MERCOSUR

Bouzas and Soltz took a look at MERCOSUR applying the key concepts of Mattli’s analytical framework (Bouzas and Soltz, 2001).

Traditionally there has been a low level of interdependence between the member states of MERCOSUR. This explains a relatively low functional demand for integration – and integration institutions. But structural reforms starting in the 1980s have increased economic intercourse between the member states and the trade liberalisation implemented during the transition period in the early 1990s did have some effect. Intra-region trade increased.

As unilateral and preferential trade liberalisation, as well as “contagion” effects, raised interdependence the demand for more formal, substantive and centralised institutions began to mount, particularly on the part of smaller countries (Ibid, no pagination).

But there were disagreements on what constituted a “level playing field” and the slow pace of “internalisation” and weak dispute settlement mechanisms aggravated the grievances. “The critical year of 1999 demonstrated the limited institutional resources (rules) to deal with the shock (the sizeable devaluation of the Real).”

In sum, weak “demand pressures” for regional institutions at the start-up of MERCOSUR helps to account for the “lean” institutional design originally adopted. But this did not prevent member states from taking “hard” decisions and successfully implementing them. The ensuing rapid rise in interdependence was not strong enough to alter one basic feature of MERCOSUR, namely: structurally asymmetric interdependence produced by large differences in size (Ibid).

In other words, MERCOSUR has a fundamental problem of asymmetric interdependence. Brazil is by far the biggest country. If weighted voting, as it exists in the European Union, had been adopted in MERCOSUR Brazil would be able to dominate.

One can speculate that enlargements beyond the new membership of Venezuela agreed in 2006 could eventually reduce the problem of asymmetry. But it is beyond the objective of this paper to discuss this further.

The supply side of the question concerns the extent to which political leaders are willing and capable of responding to demands and challenges. Did the politicians and member state governments succeed in overcoming the “collective action” problems? Did they create “commitment institutions” or did they provide enough leadership to hinder defection and ease distributive tensions.

When Mattli wrote about MERCOSUR in 1999 he said:

Within MERCOSUR Brazil is the dominant economy. It accounts for approximately 75 percent of total MERCOSUR GDP and for 80 percent of its industrial manufacturers. Nevertheless, Brazil has been reluctant to use its economic and political position to assume active regional leadership. Whenever short-term national interests have been at stake, Brazil has relegated MERCOSUR to second place. (Mattli, 1999, 160).

For instance, “Brazil has staunchly opposed plans to establish an EU-styled Commission or a supranational court.” Further, “it has refused to pay heed to calls for regional redistribution schemes, which may be of little surprise in a country that is used to be one of the world’s least equitable distributions of domestic wealth” (ibid). So Mattli’s conclusion was a challenge to Brazil: “In the absence of active Brazilian leadership, MERCOSUR is unlikely to develop much beyond today’s imperfect customs union” (Ibid., 161).

Bouzas and Soltz arrived at similar conclusions: “Weak “supply” conditions help to account for lean “commitment” institutions and the practical absence of enforceable co-ordination initiatives at the regional level” (Bouzas and Soltz, 2001). “(...) incentives for the larger member state to provide the leadership required (and pay the costs for it) have been very weak”.

Tentative Conclusions

Table 4 summarises the argument and compares MERCOSUR with other integration schemes. The argument has been that ‘institutions matter’. But this has not been proven fully. A more tight research design including more detailed case studies could probably strengthen the conclusions. It could also be tested further by deeper comparative empirical analyses whether leadership, as argued by Mattli, is more important than ‘commitment institutions’.

Table 4: Institutional capacity and achievements of five integration schemes

	EU	NAFTA	MERCOSUR	AFTA	APEC
Nature of agreement	Framework treaty: Institutional framework for developing common policies	Law treaties: Specific policy rules in the treaties	Framework treaty Specific requirements to establish customs union and common trade policy Coordination and harmonisation foreseen to establish common market	Framework Agreement Main mechanism: Common Effective Preferential Tariff (CEPT) Scheme	Parallel national action: Voluntary liberalization
Institutional capacity	Pooling and delegation of sovereignty Some redistribution through structural funds and some common policies (esp. the Common Agricultural Policy)	Under the general NAFTA: No pooling, some delegation in respect to dispute-settlement Under the labour and environmental agreements: Some pooling, but not employed in practice; Some delegation of authority to panels, but used sparingly No redistribution	No pooling or delegation Limited redistribution (Structural Convergence Fund since 2005)	Under ASEAN in general: Consultation, consensus, no interference in internal affairs ('ASEAN way') AFTA includes 'commitments', some monitoring through intergovernmental bodies and Secretariat Dispute Settlement Mechanism includes some delegation, but not (yet) applied No redistribution, but ASEAN Development Fund is being established	No pooling, no delegation of sovereignty No redistribution
Leadership	National leadership, especially from Germany and France Supranational leadership from Commission	Some US leadership at the outset Helped create law-treaty	Weak Brazilian leadership	Weak Indonesian leadership	Briefly US leadership during Clinton administration.

Achievements	Internal Market: free movement of goods, services, capital and persons Economic and Monetary Union (EMU) Several common policies	FTA-Plus: Goods, services, investments, competition: important increases in intra-NAFTA trade and FDI Cooperation on labour and environmental issues: minimal effects so far	Incomplete customs union Weak implementation Major steps needed to achieve the declared goal of a common market	Accelerated liberalization though 1990s Still some excluded sectors and NTBs Some beginning liberalisation of services and investments	Limited progress towards free trade Early Voluntary Sectoral Liberalisation (EVSL) unsuccessful for sensitive sectors
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Source: Compiled by the author (see also Laursen 2005a and 2005b).

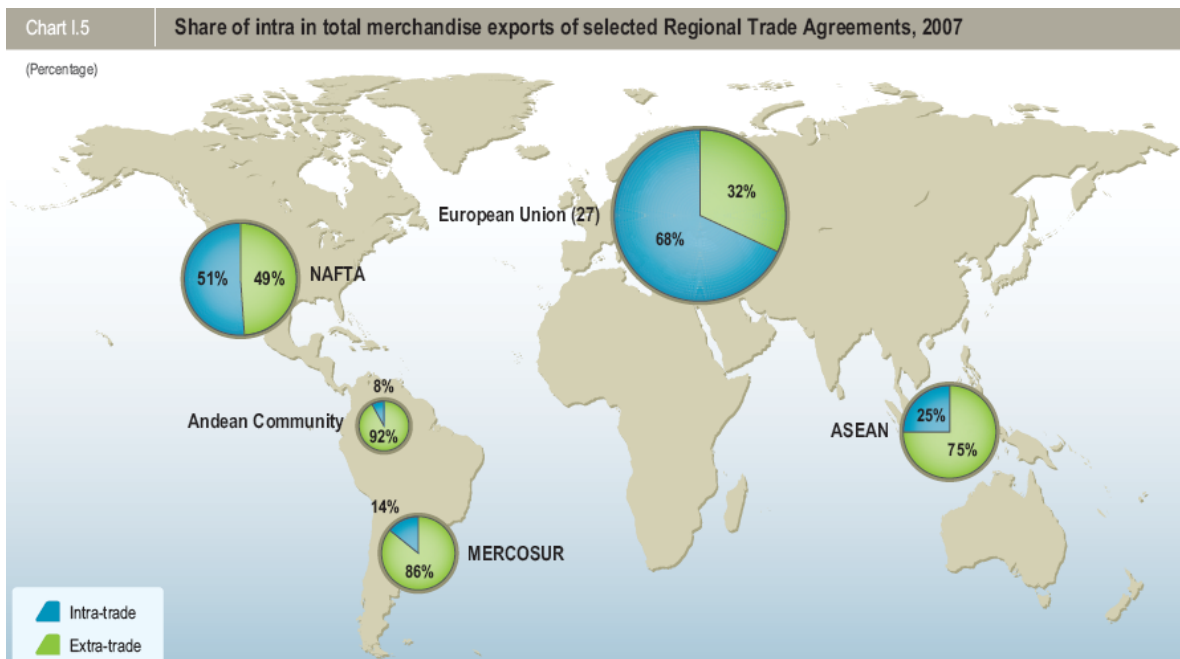
Table 7 shows what happened to intra-regional trade through the 1990s and the beginnings of the 2000s. In NAFTA and MERCOSUR intra-trade increased relatively much in the 1990s, but in ASEAN barely. Actually intra-regional trade did not really increase over the last 30 years within ASEAN. Intra-regional trade fell sharply in MERCOSUR in 2001 and 2002, presumably because of the Argentine crisis. After having reached 24.8 percent in 1998 it fell to 11.6 in 2002. No comparable decline was recorded in the other regions.

Table 7: Intraregional Export Shares, 1970-2000

	1970	1980	1990	1992	1994	1996	1998	2000	2002	2004
NAFTA	36.0	33.6	41.4	43.7	48.0	47.6	51.0	55.7	56.7	55.9
EU	59.5	60.8	59.0	59.5	56.8	62.8	62.5	61.6	60.6	60.7
MERCOSUR	9.4	11.6	8.9	14.0	19.2	22.7	24.8	20.8	11.6	12.6
ASEAN	22.9	18.7	19.9	19.1	22.7	22.9	20.6	23.9	23.7	22.2

Source: International Monetary Fund, *World Economic Outlook*, October 1999, Table 5.1, p. 129; The World Bank, *World Development Indicators*, 2004, and 2005, Table 6.5, 2006, Table 6.6 (From 2007 these statistics are not available on line)

Figure 4: Intra-regional Export Shares in 2007.



Source: World Trade Organization, *International Trade Statistics 2008*. Geneva, 2008, p. 3.

Figure 4 gives the shares for 2007. MERCOSURE falls far behind ASEAN, NAFTA and the EU (WTO, 2008).

Scholarship on regional integration faces the challenge of developing stronger comparative research designs for additional empirical research. Back in the early years of integration studies Nye presented a comparative study (Nye, 1971). The analytical model was rather complex and does not seem to have been much used. More recently Mattli has developed a comparative framework (Mattli, 1999). But most existing studies of regional integration are single case studies. More comprehensive studies are needed.

In a study published a few years ago Joseph Grieco looked at three systemic explanations when comparing the different degrees of institutionalization in Europe, North America and East Asia. A functionalist theory looking at the different level of intra-regional trade could not explain the differences. Interestingly enough, if we look at East Asia, intra-regional trade is greater than for ASEAN. Similarly, if we look at APEC it is higher than for NAFTA. Next he looked at hegemonic leadership. He operationalised it by looking at the share of GDP of exports of the largest state in the region (Germany for the EU, United States for NAFTA, Indonesia for ASEAN, Brazil for MERCOSUR, etc.) to the whole region. This theory did not explain differences in institutionalization either. His third effort to explain the differences in institutionalization was to look at shifts in relative disparities within a region over time. The hypothesis was the following: “when the relative disparities in capabilities within a region are shifting over time, disadvantaged states will become less attracted to institutionalization and the latter will become less likely to occur” (Grieco, 1997, p. 176). This theory, he concluded had some explanatory power. But in the end he admitted that “even if the concept of relative disparity shifts allows neorealism to account in some measure for the variation in regional institutionalization ... it must be said that it is unlikely

that any purely systemic-level argument will be able to account fully for that variation. A focus on systemic-level forces must be complemented with attention to domestic factors” (ibid., p.185).

Questions for further research include the role of power, interests, knowledge and values, negotiations and institutions. More detailed comparative studies of the role of commitment institutions and leadership would especially be useful. Have second generation integration schemes turned out to be as resilient as predicted by some in the early 1990s? If so, why? Or will we see ‘roll-back’ as happened to many integration efforts in the 1970s?

In this paper we have focused on MERCOSUR and compared with the EU. Some references to NAFTA and AFTA based on earlier studies have also been included. NAFTA has successfully created more trade and FDI between the three member countries. The elaborate dispute settlement system of NAFTA has mainly been used in anti-dumping cases. Consultations between national institutions have largely resolved other disputes. AFTA has created freer trade, but the impact has been limited and there are doubts about the possibilities of creating a real FTA-Plus without further institutionalization.

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