

2017 and Beyond  
***Canada and the American Challenge***  
*Some thoughts*

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*Herman & Associates*  
*Toronto*  
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*Web - [www.hermancorp.net](http://www.hermancorp.net)*  
*E-mail - [lherman@hermancorp.ca](mailto:lherman@hermancorp.ca)*

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**Dealing with Mr. Trump**

We know that substantial re-tooling the *North American Free Trade Agreement* is a priority item on President Trump's "America First" agenda. A draft Notice to the Congress, leaked on 30 March 2017, sets out the US government's broad NAFTA negotiating objectives.

Virtually everything in the NAFTA will be on the table.

It's expected the Trump team will aggressively seek major changes to: redress merchandise trade imbalances with Canada by:

- changing rules of origin;
- increasing US content in automotive and a host of other sectors;
- taking down or limiting Canada's supply management system, especially in the dairy sector;
- eliminating bi-national panels reviews;

- expanding Buy America policies and;
- ensuring against outward investment flows to Canadian manufacturing industries.

The Canadian daunting challenge will be to focus on those aspects of the NAFTA where Canada has negotiating leverage – which may be quite thin – and countering US demands with advantageous Canadian positions.

An over-arching Canadian strategy, and which has been so far well-executed, is to **build alliances** among key businesses and a wide array of US political leadership, using these contacts to convey the Canadian message about US benefits under the NAFTA, hoping counteract the Trump administration's demands when the parties get to the negotiating table.

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### **Who's at Home?**

When it comes to trade negotiations with the Americans, one of the challenges is to know whom to deal with. You might think it's the President but, as in all things in Washington, it's much more complicated than that.

Under US legislation, the US Trade Representative (USTR), in the Executive Branch, is supposed to have lead responsibility in trade talks. But earlier Mr. Trump named Wilbur Ross, the Commerce Secretary, to lead the NAFTA re-negotiations, unleashing a turf war between the Commerce Department and the Trade Representative's office.

Added to the mix is the National Trade Council, a new White House agency created by Mr. Trump to advise on trade policy, headed by Peter Navarro. He will also want to make sure his office's influence is maintained as the talks unfold.

Another problem is that Trump's choice for USTR, Robert Lighthizer, has yet to be confirmed by the Senate. There's a fight going on between the Republicans and Democrats in the Finance Committee as to when his confirmation hearing is to be scheduled.

Without the USTR confirmed and while this jockeying is going on, **key senior positions in USTR and Commerce remain unfilled**, leading to a vacuum on the top tiers of these agencies.

So there's a bit of a waiting game before NAFTA negotiations commence in earnest. And then there's the Congress.

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### **It's the Congress Stupid**

The American Constitution is all about checks and balances, designed to ensure no one branch of government can dominate. Thus, the Congress has been given equal authority with the President in international trade matters.

Trump can bluster and complain about NAFTA all he wants, but he can't get to first base on trade talks without the approval of Congress and its key Committees.

By the same token, as I explain, this dispersion of power plays to Canada's advantage as we head to the negotiating table.

To even get NAFTA talks started, Trump needs Congressional approval. That comes under what's called **Trade Promotion Authority or "fast-track"**, a requirement that applies to all US trade negotiating efforts.

There are several problems with fast-track. First, it was supposed to limit the power of Congress to interfere in negotiations once the authority is given or to insist on changes to a negotiated treaty. All it could do would vote for or against approval when the deal was done.

Over the years, fast-track was modified. Now it involves complex steps, all of which are designed to maintain Congressional power and oversight and ensure that key Committees have an un-diminished role in US trade negotiating activities.

The first step in the fast-track process, as we know, is for the President to get approval to negotiate. For this, he has to give 90 days' advance notice to Congress before negotiations can start, setting out the administration's objectives.

The 90-day notice sets up markers against which progress will be judged by key Congressional committees, both the Ways & Means Committee of the House and the Senate Finance Committee.

In effect, fast-track is a **set of marching orders** that requires the Executive to regularly consult with both these committees plus the Congressional Oversight Group to make sure he discharges those orders.

What this means is that Congress will be involved throughout the NAFTA talks. While the Canadian government will be negotiating with the Executive, the Canadian team will have a monster looming in the back of the room in the form of key Congressional committees.

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### Border Tax Adjustments

No question, dealing with the Congress in parallel with USTR or the Commerce Department in the NAFTA negotiations will be a difficult challenge. Even more ominous in many ways is the **Ryan-Brady tax reform plan** being worked on in the House of Representatives.

The plan would cut in US corporate taxes to 20% as a net cash-flow tax, combined with a border tax adjustment mechanism that would tax imported goods at a similar rate of 20 percent.

This would be achieved by denying tax deductions for imported goods used by US industries while exempting exports of American goods from the same domestic cash flow tax.

A border tax geared to cash-flow (a kind of income tax in another guise) would almost certainly contravene the *General Agreement on Tariffs & Trade* ("GATT", incorporated in the NAFTA) as a measure that discriminates against imported goods by treating them differently by applying a higher tax or charge to imports than on those produced locally.

If enacted, other governments will challenge any such tax at the WTO. Given the lengthy process of WTO adjudication, there is a fear of immediate countermeasures

taken outside of the WTO framework with potentially disastrous repercussions for the global trading system at large.

The border tax spectre lurks in the background, adding a complicated dimension to NAFTA re-negotiations. It is difficult to see how Canada (and Mexico for that matter) can settle NAFTA issues with the Americans with a possible border tax on the Congressional agenda.

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### The Multilateral World

Since 1945, the US has led the world in building international institutions, not only the World Trade Organization but the IMF and World Bank as well. Each of these three have issued a call to Trump to not turn the US back on multilateralism and retreat to a variation of the kind of protectionist policies that devastated global commerce in the 1930s.

The WTO and its dispute settlement mechanism has been the brunt of criticism by the Trump team and its rules have been claimed to be one of the prime reasons for US trade deficits with most of its major trading partners.

These criticisms are ironic, in the sense that the WTO and its rules are **based largely on American leadership** and reflect the US trade law system.

There is a major disconnect between Canadian trade policy, strongly supportive of multilateral rules and WTO dispute settlement proceedings, and the highly critical negativism of the Trump administration.

How this all unfolds remains unclear. A signal will be given by the person Mr. Trump names at the new US ambassador to the WTO. However, judging from comments recently made by Commerce Secretary Wilbur Ross, prospects for any kind of positive US engagement in the multilateral process are not encouraging. This impacts not only Canada but the global community at large.

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### **Softwood Lumber**

The softwood lumber dispute is all about market share. US producers know that tying Canadian producers up with an unending Commerce Department investigation will lead to a diversion from export sales activities. And US customers will back off buying Canadian imports until the case is resolved.

In fact, the potential **market share gains** of a mere 1 or 2% alone probably make it worthwhile for the US industry to have filed a new case. Even if they eventually lose at the WTO or NAFTA panels, the market gains will offset their out-of-pocket legal and other costs.

The question is whether anything is gained trying to settle this contentious and complicated trade dispute within the context of the NAFTA re-negotiations. Dealing with it in the NAFTA context adds inordinate complications that limit Canada's negotiating leverage in other areas.

The strategic issue is whether the softwood lumber file should be put on a **separate track** and dealt with outside changes to the NAFTA itself. On balance, it seems better to take softwood lumber out of the NAFTA process.

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### Trade Remedies – A US Priority

It would be nice to think that Canada and the US could find peace on the trade remedy front and agree not to apply anti-dumping or countervailing duties to each other's exports.

After all, Canadian industries (mostly) respect business standards to not dump in the other person's backyard. And, generally speaking, governments these days aren't in the subsidy game to promote exports (at least not directly).

Nice thoughts. But backing off trade remedies is not part of current American trade policy, whether the Republicans or the Democrats. Quite the contrary, even under Obama and before Mr. Trump's America-First declarations, US policy aimed at making their system even tighter and stronger.

What that means is that **Canada can't be out of step** with the Americans when it comes to dealing with dumped and subsidized imports

Canada's trade remedies regime (under the *Special Import Measures Act*) in fact has been moving in step with developments south of the border over the decades. In many respects the Canadian system is very similar to that in the United States.

However, the system hasn't been modernized in any serious way in more than 15 years. During that time major changes have taken place in international business and the way goods and services move across borders.

So while Canada does not embrace protectionism, there was clearly a need to update Canada's system to give federal agencies the tools needed to ensure that, as in the US, anti-dumping and countervailing duty orders were not being circumvented through various practices and techniques.

These legislative changes were announced in the **2017 Federal Budget**.

In a way, the SIMA changes reflect an ongoing Canadian dilemma – on the one hand, strong opposition to protectionism reduced access to markets and, on the other, the need to ensure that the Canadian trade remedy system works in close parallel with the US system.

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*Lawrence L. Herman, Herman & Associates, a former Canadian diplomatic, practices international trade law and is a Senior Fellow of the C.D. Howe Institute in Toronto.*

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