MONITORING THE IMPLEMENTATION OF THE CANADA — UNITED STATES FREE TRADE AGREEMENT

Report of

THE STANDING SENATE COMMITTEE ON FOREIGN AFFAIRS

CHAIRMAN: The Honourable John B. Stewart

MARCH 1990

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ORDER OF REFERENCE

Extract from the *Minutes of the Proceedings of the Senate*, Wednesday, April 5, 1989:

"With leave of the Senate,

The Honourable Senator Frith, moved, seconded by the Honourable Senator Stewart (*Antigonish-Guysborough*):

That the Standing Senate Committee on Foreign Affairs be authorized to monitor and report on the implementation and application in both countries of the *Canada-United States Free Trade Agreement Implementation Act* as well as on any other related trade developments; and

That the papers and evidence received and taken on the aforesaid subject before the Committee during the Second Session of the Thirty-third Parliament and the First Session of the Thirty-fourth Parliament be referred to the Committee.

The question being put on the motion, it was—

Resolved in the affirmative."

Charles Lussier

Clerk of the Senate

REPORT OF THE COMMITTEE

The Standing Senate Committee on Foreign Affairs has the honour to present its

SIXTH REPORT

Your Committee, which was authorized to monitor and report on the implementation and application in both countries of the *Canada-United States Free Trade Agreement Implementation Act* as well as on any other related trade developments, has, in obedience to its Order of Reference of Wednesday, April 5, 1989, proceeded to that inquiry and now presents an Interim Report.

Respectfully submitted,

JOHN B. STEWART
Chairman

The Standing Senate Committee on Foreign Affairs has the honour to present its

SIXTH REPORT

Your Committee was authorized by the Senate on April 5, 1989, to monitor and report on the implementation and application in both countries of the *Canada-United States Free Trade Agreement Implementation Act*, as well as on any other related trade matters.

Consequently, the Committee has undertaken a series of hearings on aspects of the Agreement itself and upon related matters and has directed its staff to prepare, and update regularly, a survey of developments. These meetings and the research done by the staff have attempted to track requirements for actions to which the two governments are committed by the FTA -- such as statutory and/or regulatory changes and negotiation on various issues -- and institutional developments, particularly relating to dispute resolution. As well, evidence of the costs and benefits to Canada of the FTA has been gathered and examined to discover areas or issues which warrant increased attention by government.

The Committee now presents it first report on this matter, entitled: Monitoring the Implementation of the Canada-United States Free Trade Agreement, together with a survey of developments prepared by its research staff at the first anniversary of the coming into force of the FTA, which bears the same title. The Committee's report draws on information assembled in the staff report. Bracketed numbers in this report refer to the section in the staff report where background information can be found.

MONITORING THE IMPLEMENTATION OF THE CANADA-UNITED STATES FREE TRADE AGREEMENT

Monitoring implementation may be taken to mean the surveillance of the process of implementation over the ten years to final tariff removals as set out by the FTA, receiving and reviewing the reports of the various working groups, and examination of the dispute settlement process and subsidy negotiations. As well, it may be seen as an examination of the over-all Canada-United States trading relationship and of the Canadian economy as it adjusts to new competitive pressures arising within the new North American market and, more generally, from global competitive pressures.

Monitoring may imply also an attempt to measure the costs and benefits of the Free Trade Agreement and the provision of analyses for the public record.

Adjustment in industries and national economies is a continual process. The structure of a country's industrial base and of particular sectors, and the corporate and government policies which assist or direct them, reflect incessant change in the national and international economic environment. The complex pattern of influences which have worked to alter the structure and location of employment across the world have played a major role in Canada also, for Canada, besides being one of the world's largest economies is also more trade dependent than many other major countries and therefore more susceptible to the influence of international forces.

In the shorter term, economies respond as well to an array of macro-economic influences such as interest and exchange rates. At this early moment of its life, the FTA therefore must be viewed as just one more influence whose effects are not easy to distinguish from the myriad other forces in play.

The Committee has not sought to reach firm conclusions in this first year under the terms of the new economic and political structure of the FTA. It has not done so because it constantly has been keenly aware of two difficulties:

(i) One year is a too short a period for patterns to become clearly evident; data and information are in short supply. Economic analysis requires "in-depth" study of investment and trade flow data which is only just beginning to emerge. Measurement with some degree of reliability and relevant results should begin to appear in some sectors in about three years -- with more certainty over a wider range after five years have passed -- if sufficient evidence is gathered and made available to qualified analysts.

(ii) Even with more data and time, economic analysis of the effects of the FTA will remain difficult because the FTA is super-imposed on a rapidly internationalizing world economy which is itself experiencing deep longer-term structural changes and intense shorter-term macroeconomic adjustment problems. Isolating "pure" FTA effects from the whole array of national and

international forces external to the FTA will therefore be difficult. Analysis of the political and institutional responses to the FTA, while requiring less time to pass before sufficient information is available for analysis or judgement to be made, also is hindered by the difficulty of separating the FTA from other external forces, actions and changes.

However, to monitor implementation is more than to measure effect. Analysis of the process of implementation and of adjustment in general can be done without the need to compile a "scorecard" of winners and losers, without answering "yes" or "no" to the deceivingly simple question, "In the circumstances, is this right for Canada?" Rather than taking that approach, the Committee has chosen to track developments, to isolate trends, to comment and advise on measures the Government might take to improve or enhance the implementation process to the end that Canada's interests be protected and advanced during the period when the remaining tasks of the free trade negotiations with the United States are being completed, and when Canada's people and industries are facing increased competition from around the world.

Even though definitive conclusions about the utility of the FTA as a policy instrument, and recommendations flowing from them, will be some years in coming, enough has emerged from the work of the Committee, and from the Staff Report, after the first year under the FTA, to point to some reasonably strong conclusions on issues which demand further and continuous monitoring. These conclusions flow, not from empirical analysis or from economic assessments made with a view to evaluation, but from an examination of

government action and the application of government resources. This perspective holds that how governments behave within the framework of the new regime is key to measuring the future success or failure of the FTA. This type of monitoring is far more feasible in the short term, and probably more important than impact assessments of uncertain accuracy. That uncertainty flows partly from the absence of a well-defined base-case against which to measure, to answer the question, "What would things have been like in the absence of the FTA?". These government actions -- both the direct implementation tasks and the work involved with the various continuing negotiations and working groups -- will be decisive in ensuring that the provisions of the Free Trade Agreement are put fully to use to Canada's advantage. In this respect, the Committee hopes that its recommendations will be accepted by the Government not as criticism but as advice giving support to government action to draw advantage for Canada from the Agreement.

As well, many commentators have suggested that U.S. trade negotiators often make use of a "goading" Congress to extract concessions during talks with other countries. Many legislative mandates can be cited as evidence supporting this view, such as the Baucus-Danforth amendment to the *Omnibus Trade and Competitiveness Act of 1988* and the consultation and layover clauses of the U.S. legislation implementing the FTA. While the Committee rejects the view that Parliament could or should play a similar role in Canada, the Committee trusts that drawing attention to such actions by the U.S. Congress can, to some degree, limit their influence.

In many respects the implementation of the more "technical" aspects of the FTA -- such as legislative and regulatory changes, further studies and working groups, the design and implementation of new certificates of origin and temporary entry permits, tariff reductions -- appears to be proceeding smoothly. However, with respect to the broader economic changes which had been predicted -- investment decisions, changes in trade direction or quantity, pressure for policy harmonization -- evidence is far less clear. The primary concern that the Committee wishes to present in this report is with respect to the efforts and resources the Government has devoted to providing research and support for (a) the monitoring of those broader changes; (b) adjustment assistance; and (c) the continuing negotiations over the remaining contentious issues, including subsidies and agriculture market management.

It is not clear that the government has provided sufficient resources and sufficient inter-departmental structure to manage the FTA properly in the Canadian interest; indeed, the evidence available suggests that it has not done so. In the view of the Committee, the inadequacy of these resources will limit the capacity of Canadian governments, institutions, and industries to respond to the continuing challenges and opportunities presented by the FTA. The Committee is concerned about four specific items:

(1) information-gathering, analysis, and monitoring efforts;

(2) the capacity to initiate action in Canada, and to respond to an "aggressive" and "legalistic" U.S. approach to FTA implementation;

(3) the capacity to arm Canadian negotiators for what promises to be a difficult and prolonged negotiation over subsidies;

(4) the capacity to transpose Canadian FTA concerns and policy initiatives into the global context of Canada's larger trade policy agenda at the GATT, the Uruguay Round of Multilateral Trade Negotiations, the Europe 1992 initiative, developments in Eastern Europe and for regional economic cooperation initiatives in the Pacific basin.

1. Information Gathering and Analysis

There is as yet no evidence that the Government has launched a focused effort to monitor FTA effects and consequences. Apart from a consultant's report solicited from Informetrica Limited, there has been little indication that additional resources are being devoted to information gathering and analysis. While it is presumed that many government departments continue to collect much of the relevant data, it would appear that no attempt is being made to consolidate this work and produce analysis; nor is there evidence that on-going data collection and analysis has been changed to reflect any additional concerns or questions raised by the FTA (See Sections 2.3.5 and 2.4.1 to 2.4.3).

In October, 1989, the Department of External Affairs commissioned a feasibility study on monitoring the economic impact of the FTA from Informetrica Limited seeking advice on the type and nature of macro-economic and anecdotal research and evidence which might be gathered, how it might be treated analytically, and how soon statistically relevant conclusions could be drawn from this work. The study was presented to the Government on December 18, 1989. It was released to the public by the Honourable John Crosbie, together with the Minister's assessment on the first year's experience with the Free Trade Agreement on January 19, 1990 (See Section 2.4.3.3).

Informetrica's study confirms the commonly held view that accurate measures of the aggregate effect of the FTA cannot be made at this point. It says:

> It is not possible to provide a complete, professionally qualified assessment of the FTAs effect on economic performance in 1989 on January 1, 1990 or shortly thereafter. In fact, it will be some years before such an evaluation is possible.

However, the study suggested that there is a good deal that could and should be done to improve the quality of assessment in the future. It set up three categories:

(i) things that can be done now (that is, in December 1989);

(ii) things that should begin soon, in 1990 and 1991, to supplement the procedures already underway; and

(iii) things that can be done more accurately after five years have passed.

The Government made public its first assessment on January 19, 1990. It purported to provide the information that Informetrica had said was possible in an early report card. In fact, while the government document and Mr. Crosbie's statement did reflect the study's contention that an aggregate assessment of the economic effect of the FTA is not feasible at this time, Informetrica had suggested that much more could be done in the short term than the government provided. This included:

(i) an analysis of monthly trade flows, particularly for categories with large tariff reductions as of 1 January 1989;

(ii) an analysis of investment flows and private and public investment intentions, comparing the 1989-over-1988 increase with 1988 over 1987. As well, Informetrica suggested that lists should be compiled of companies which are expected to be positively affected by the FTA, negatively affected, or little affected and that the investment patterns of these groups should be compared against each other and against expectations; and

(iii) the compilation of partial lists of anecdotal information about plant openings and closures by industry, with an indication of whether that industry was expected to be positively, negatively, or little affected by the FTA.

The Committee recommends that this work be undertaken at once, with the results made public on an on-going, regular basis, so that it may be subjected to independent analysis.

The Government should prepare and release to the public an annual report that would draw together the data and analysis of all government departments monitoring economic changes related to the FTA.

The Informetrica study also suggested that "some information about future monitoring plans" should be included in the Government's first assessment. Such information was not provided. In their appearance before this Committee, which occurred after that assessment was released, the authors of the study indicated that little of the analysis that could or should be undertaken can be done in the absence of data that only the Government is capable of providing. If much more time passes without that data being collected, an analysis may never be possible.

The Committee recommends that the Government indicate, in detail, its monitoring plans, and that the required data collection be initiated as soon as possible.

In general, astonishingly little is known in detail about how industrial economies respond and adjust to major structural pressures (See Section 2.4.2). Only with a much more developed understanding of the micro-economic adjustment process can any government hope to make wise policy choices in an age of deep structural pressures. The monitoring of the implementation of the FTA through additional questions attached to other Statistics Canada work, or to GST reports, which could generate data on the full cohort of Canadian business, affords a unique opportunity for the collection of almost total census information -- information which could be used by both government and business to assess and develop responses to the forces of globalization. This opportunity should not be missed.

The Government should design and undertake data collection on the adjustment process as it proceeds under the FTA with a view to providing on-going data useful to government and businesses as they prepare action plans to meet a continually changing global economy.

2. Legalism and Cooperation

The Staff Report to the Committee makes frequent reference to the differing attitudes which seem to inform FTA implementation on opposite sides of the border (See Section 2.2.0). In some respects, rather than gaining Canada exemption from harassment, the FTA seems to have licensed even more "aggressive" harassment of Canadian trade practices by the United States. Whether the FTA is to blame or not, it is apparent that Canada

continues to be subjected to harassment from U.S. competitors and the various U.S. government agencies which serve them. In part, this reflects a U.S. approach which was manifest for some years before the FTA came into force. It also appears to represent a determination by various interests in the United States to extract every benefit the FTA may offer. The Committee recognizes that existing national legislation was grandfathered by the FTA and that consequently an argument can be made that most of the harassing actions are proper applications of U.S. law (See Sections 2.5.2 and 2.5.3).

While it was not expected that trade disputes between Canada and the United States would be ended by the Agreement, it was hoped that the U.S. Administration would attempt within the latitude permitted by U.S. law to limit harassing actions. This does not appear to be happening. The Committee notes that, with respect to the inspection of Canadian meat exports, only steady and public pressure applied by the Minister of Agriculture, including an explicit threat of retaliatory action, finally elicited a cessation of U.S. border harassment (See Sections 2.2.3.1, 6.0 and 6.4).

The Government should undertake formal consultations with the United States under the provisions of the FTA to limit harassing actions by U.S. individuals, corporations, and government agencies to the full extent possible. If such an agreement cannot be reached, the Canadian government should make available to Canadians subjected to harassment similar government resources as are put at the disposal of U.S. companies. In particular, the Canadian International Trade Tribunal should be given powers and resources similar to those of the United States Trade Representative with respect to undertaking

investigations of subsidy or other trade-distorting practices identified by Canadian complainants.

If no changes in U.S. practice are forthcoming, the Government should consider supporting countervailing actions against already identified U.S. subsidy practices and instituting equivalent border measures for goods entering Canada from the United States.

While the Committee recognizes the dangers that "tit-for-tat" bargaining and retaliation may pose to the smaller trading partner, it recommends that, particularly with respect to agricultural issues, the Canadian government respond to U.S. border harassment and the subsidization of exports to third-country markets with the full use of FTA dispute settlement mechanisms and consultations; and, if necessary, retaliatory measures.

3. Subsidy Negotiations

The Government has made progress in setting out the process and in providing some resources for the subsidy negotiations with the United States. However, as the *Omnibus Trade and Competitiveness Act of 1988* and recent U.S. actions make clear, the United States will be taking an aggressive position with respect to the use of subsidies to industry. Canada can expect very difficult negotiations over the next four to six years now available under the FTA. The whole issue of harmonization (See Section 5.0) and of defining what is and is not a subsidy, what government practices are and are not to be allowed, turns on

the capacity of the Canadian negotiators to reveal U.S. practices and to justify vital Canadian programmes and practices (See Section 2.3.2).

The Government should undertake extensive consultations, in public whenever possible, with the governments in the provinces with respect to regional strategies and other provincial, industrial, or social development programmes that might be the subject of negotiation with the United States.

The Committee fears that the amount and quality of information on U.S. subsidy practices available to Canadian negotiators is not adequate. In particular, little seems to be known in detail about the plethora of state and local assistance given to U.S. business, nor of the impact of defence spending and entitlement programmes.

The Government should bolster the resources available for the study of subsidy practices in the United States.

Part of the disputation surrounding the FTA negotiations was public uncertainty with respect to negotiating mandates and the issues under discussion. Since the subsidy negotiations will raise questions concerning the proper limits of government action, in particular about how far the government should enter the marketplace, a more public

consultation process should be adopted than that used prior to and during the free trade negotiations.

Public debate of possible negotiating mandates should be encouraged, in Parliament and/or through public hearings, as well as with industry advisory bodies and provincial governments prior to the start of the formal negotiations with the United States.

4. General Trade Policy

Undertaking the work enumerated above, together with the continued analysis of the structure of Canadian economy which that implies, will equip the Canadian government to deal not only with the United States and FTA issues, but with Canada's trading and industrial policy more generally. It will provide the information necessary to make judgements about what the government can do to encourage adjustment and restructuring so that Canada and Canadians will be equipped to meet the challenges that the next years will bring (See Section 7.0).

Other Concerns:

Two other issues are of concern to the Committee. These are:

(i) a continuing tendency of the government to rely on inter-governmental negotiation to resolve disputes rather than to use the new dispute settlement mechanisms; and

(ii) the resistance to expanding adjustment programmes and the provision of new resources to education and research and development.

1. Dispute Settlement

Particularly with respect to Chapter 18 disputes, the staff report notes a tendency for disputes to be taken up by the Commission, where they experience delays and do not emerge as references to panels (See Section 2.2.3 and 6.1). Since the Commission comprises only the two trade ministers, this really constitutes little improvement over the situation that prevailed previously, other than perhaps an increase in political will which may arise from having a formal process. However, there is no formal agenda for Commission meetings; items are discussed if the ministers raise them; and no timetable is applied to any dispute unless the ministers agree to refer the matter to a panel. This practice, if continued, will rob the dispute settlement mechanisms of their chief merit, that is, the capacity of experts to tackle an issue on an individual basis in isolation from the larger political agenda of bilateral relations (See Section 6.4).

The Committee recommends that the Commission send to panel resolution any matter that has been before it for twelve months without resolution, and that any new disputes be referred to panels if resolution at the Commission level is not reached within the thirty-day period set forth by the FTA.

In the alternative, the Committee recommends that the Commission make regular public reports on the status of each dispute before it, the work plan the commission has adopted to resolve the dispute, and the reason(s) that each has not been sent to panel resolution.

As well, no resources or staff exist to support the Chapter 18 panels or the Commission itself outside of regular External Affairs personnel (See Section 2.3.5).

The Committee recommends that the question of an independent agency or bilateral institution to support the Commission in general, and Chapter 18 panels in particular, be re-examined.

2. Adjustment Assistance

With respect to adjustment assistance, the Government so far has resisted committing any major new resources either to labour retraining and mobility or to R&D stimulation as recommended by the Advisory Council on Adjustment (See Sections 4.1.1 and 4.1.2). Recognizing that the Government has decided not to try to differentiate between those

companies and individuals that are dislocated by the FTA and those experiencing dislocations as a result of other economic forces, the Committee believes current programmes are inadequate and that new resources are required. Diversion of resources from one programme to another, as the Unemployment Insurance changes currently before Parliament provide, do not meet these needs (See Sections 4.1.1 and 5.3.2.2). As well, the low levels of R&D spending by government and business in Canada remains a major problem -- one to which no new answers or initiatives have been directed (See Section 4.1.3).

The Committee urges the Government to provide a detailed response to the recommendations of the Advisory Council on Adjustment, indicating how it intends to alleviate each of the difficulties identified by the Council.

Many commentators have suggested that given the ten-year phase-in of the tariff eliminations, economic adjustment and industrial restructuring will be slow and gradual, and entail only low costs. However, 15 per cent of tariff items were removed immediately (that is, on January 1, 1989), 35 per cent more are to be removed over five years, and the final 50 per cent over ten years; two of those five and ten stages, respectively, are already in place (See Section 2.2.1). This suggests that in many sectors any adjustment and restructuring that will be required to maintain or become competitive must be undertaken very soon.

As well, two other factors suggest that adjustment costs will be borne early:

(i) effective tariff protection for many tariff line items may be eliminated well before the full value of the tariff is removed; and

(ii) elimination is definite. While tariff reductions may be accelerated, they are not to be renegotiated or slowed.

This means that adjustment costs and restructuring are inevitable, and many, if not most, companies are proceeding now to restructure (See Section 3.2). At the very time that adjustment and restructuring are required, other factors have imposed handicaps. Specifically:

(i) high interest rates in Canada which make financing costly; and

(ii) exchange rate appreciation has offset any price advantage for Canadian exports into the United States that U.S. tariff reductions may have provided, while at the same time Canadian tariff reductions have opened Canadian markets to U.S. competitors (See Section 5.2.2).

While the Committee recognizes that interest and exchange rate policy must serve many objectives, it cannot help observing that the current structure of interest and exchange rates

in Canada is precisely the opposite of what would be recommended if adjustment to the FTA were the only consideration.

The Committee recommends that the Government give urgent consideration to expanding the scope of existing employment adjustment programmes for individuals, and to increasing the total of the resources available for them, at least to the extent necessary to meet the recommendations of the Advisory Council on Adjustment.

MONITORING

THE IMPLEMENTATION OF

THE CANADA-UNITED STATES

FREE TRADE AGREEMENT

February 1990

A Staff Report to the Senate Standing Committee on Foreign Affairs

MONITORING THE IMPLEMENTATION OF THE CANADA-UNITED STATES FREE TRADE AGREEMENT

A Staff Report to the Senate Standing Committee on Foreign Affairs

February 1990

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MONITORING
THE IMPLEMENTATION OF
THE CANADA-UNITED STATES
FREE TRADE AGREEMENT

A Staff Report to the Senate Standing Committee on Foreign Affairs

February 1990

1.0 INTRODUCTION

Following the passage of the legislation implementing the Free Trade Agreement between Canada and the United States, the Senate gave its Standing Committee on Foreign Affairs a reference to monitor developments under the Agreement as it was implemented by the two governments and to examine other trade-related developments. To this end the Senate Committee has undertaken a series of hearings on aspects of the Agreement itself and upon related matters and has directed its staff to prepare, and update regularly, a survey of developments.

This report on developments relating to the Free Trade Agreement and the periodic updates of the report will attempt to track requirements for actions to which the two governments are committed by the FTA, such as further examination and negotiation of various issues, legislative and/or regulatory change, and institutional developments, particularly those relating to dispute resolution. The reports will seek, as well, to monitor evidence, in its own right or adduced by others, of the costs and benefits to Canada of the FTA. On the basis of this evidence, the reports may suggest areas or issues that warrant further in-depth examination or continued monitoring.

The report seeks to be as concise as possible -- providing reasonably up-to-date information on the status of the wide array of events and avenues of enquiry that flow from or are related to the process of implementation of the Agreement. It is intended more as a guidebook to developments than as a comprehensive assessment, even where it highlights issues or draws attention to early evidence of benefits and costs.

The report is organized into seven sections including this introductory note. Chapter Two provides a review of the legal and technical implementation of the FTA. Chapter Three reviews some evidence of specific instances of industrial or institutional restructuring that may be either directly or indirectly attributable to the FTA. Chapter Four takes note of two kinds of response to the Agreement and the effects of "globalization" more generally: the response of governments to restructuring pressures, and the response of other groups of actors either in support or in opposition. Under the title of Policy Harmonization,

Chapter Five reports on an array of non-tariff issues incorporated in, or raised by, the FTA, many of which were particularly contentious in the debates leading up to the Agreement's passage. Chapter Six examines the use so far of the dispute resolution mechanisms in Chapters 18 and 19 of the Agreement. Finally, Chapter Seven provides some background information on trade-related developments in Europe, at the GATT, and in the Asia Pacific region, on which the Committee has taken some testimony.

Chapter Seven serves to remind readers that the Free Trade Agreement is but one development among many -- both in the sense of the formal reworking of trade arrangements and in the sense of the restructuring forces embraced in the term "globalization" -- which are affecting Canadian economic arrangements. As many analysts, whether supporters or critics of the Agreement, have noted, the task of discerning the FTAs particular effects in this sea of influences is not simple, especially so early in the game..

2.0 IMPLEMENTATION: TECHNICAL AND LEGAL DEVELOPMENTS

2.1 IMPLEMENTING LEGISLATION AND REGULATION

The Free Trade Agreement came into force, as scheduled, on January 1, 1989[1].

Regulations to implement the Act were published in a special issue of the *Canada Gazette Part II* on January 6 and in a regular issue on January 14, 1989.

Further regulatory changes were introduced at later dates: rules for automotive safety and used car sales were published for comment on January 28, and for cable retransmissions on March 4, 1989.

The United States also passed implementing legislation and introduced the required regulatory changes to bring the FTA into effect[2].

The implementing legislation and regulations in each country also introduced some definitions and practices that have caught the attention of the other as perhaps not fully in line with the other country's view of the intent, perhaps not even the letter, of the text of the FTA. For example:

- Canada's regulations on cable retransmission rights, as printed in the *Canada Gazette* on March 4, 1989, are still not fully acceptable to the United States since compulsory licensing is allowed.

- The United States included a clause[3] that leaves in place the old *Tariff System of the United States* (TSUS) tariff classification system in the determination of quota levels, particularly for wool products, rather than utilizing the *Customs Cooperation Council Nomenclature* (CCCN), commonly known as the *Harmonized System*, which is mentioned in the FTA, and which was adopted for trade purposes in the United States concurrent to the adoption of the FTA[4].

C-2, *An Act to Implement the Free Trade Agreement between Canada and the United States of America*, cited as the *Canada-United States Free Trade Agreement Implementation Act*, passed the House of Commons on December 23, with Royal Assent given on December 30, 1988, following passage in the Senate.

[2] H.R. 5090 *A Bill to Implement the United States-Canada Free-Trade Agreement*, cited as *United States-Canada Free-Trade Agreement Implementation Act of 1988*, passed the House of Representatives on August 9, the Senate on September 19, and signed into law by the President on September 28, 1988, to come into effect with the coming into force of the Agreement.

[3] H.R. 5090 Sec. 104 (b)

[4] These issues are discussed below in Section 2.2.3 and 6.0.

2.2 BORDER MEASURES

2.2.0 Some Introductory Comments

One of the principal goals set forth by the Canadian government during the negotiation of the FTA was to secure and improve access to the U.S. market for Canadian goods and services and to reduce protectionist harassment. Several stand-still clauses were provided in the Agreement to afford a breathing space from trade actions. Dispute settlement mechanisms were created to deal with differences or trade actions that did arise. Nonetheless, there appears to be early evidence that a "letter of the law" approach rather than a "spirit of cooperation" continues to inform the actions of U.S. competitors and U.S. agencies with a mandate to manage the new regime. For example:

- New rules opening trade in meat and meat products were intended to ensure free access. There have been reports from Canadian exporters, however, of increased inspection and spot checks of meat that are alleged to be harassment.[5]

- The presence of U.S. National Guard troops at border stations through the summer, though explained by the U.S. Administration as part of its attack on drugs, was symbolic of the increased scrutiny faced by Canadian travellers and the enforcement of rules in a manner that seemed inconsistent with the spirit of the FTA, a spirit which would give the benefit of the doubt to travellers and traders.

Further examples of this general tendency are noted throughout the report.

2.2.1 Tariffs and Tariff Classification:

2.2.1.1 Tariff Rates:

One of the most traditional objectives of trade negotiations under the GATT has been the reduction or elimination of tariffs. The first seven rounds of multilateral talks have been quite successful in this task, and prior to the coming into force of the FTA, over 75 per cent of Canada-U.S. trade crossed the border tariff free.

In order to effect the gains from tariff removal, and to bring the FTA into conformity with GATT obligations, which require that substantially all barriers to trade be removed in bilateral free trade agreements, Article 4 of the FTA provides for the removal of all remaining tariffs between Canada and the United States.

All goods of domestic origin will move tariff free between Canada and the United States following the full implementation of the tariff reductions set out by the FTA. With only a few exceptions, this removal was divided into three sections:

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[5] This matter is before the Commission for consultation.

- those goods which would immediately move tariff free on the coming into force of the FTA on January 1, 1989;
- five equal instalments of reduction over five years beginning January 1, 1989; and
- ten equal instalments over ten years.

The United States further agreed to phase out, over five years, its Customs User Fee on Canadian goods. In addition, both countries have agreed to a five-year phase out of duty drawbacks (except in the case of citrus fruits and a specified volume of fabric used for exported clothing that is not itself subject to duty free treatment) and a ten-year phase out of duty remission schemes. As well, in the case of some fresh fruits and vegetables Canada has retained the right to institute "seasonal" tariffs for a twenty-year period. The few other remaining exceptions reflect existing bilateral or unilateral reductions already scheduled or in place. Provision was also made in the FTA for the negotiation of an acceleration of tariff reduction schedules if requested by either side[6].

To the degree that Canada is largely a "price-taker" in the commodities it trades -- since it produces and consumes too small a quantity of most products to have a large effect on world prices -- the elimination of the remaining tariffs on U.S.-Canada trade should benefit both Canadian consumers and Canadian producers who export. The benefit flows from the fact that the tariff is akin to a "tax" paid by Canadian consumers on imports and by Canadian exporters on exports.

However, given the five- to ten-year schedules for reduction of the tariffs on many items, it is too early to discern measurable consumer or economic efficiency gains. Against these ultimate gains must be weighed the more immediate dislocations of the inevitable restructuring of Canadian economic activities which these tariff changes inspire.

A significant part of the current public debate over the benefits of free trade also flows from the inability to identify specific consumer savings. For example, the $450-$800 annual consumer gain per family that was projected to arise from reduced prices on imported goods once tariffs were finally removed, especially when spread over ten years and a wide array of goods, is so small as to be virtually invisible in the short-term, if indeed any part of the saving is passed on to consumers. At the same time, while adjustment and efficient production are thought to lead to a general welfare gain and an overall increase in employment over time, many individual companies and people will experience immediate dislocation as those forces work their way through the economy.[7]

Not inconsequential either is the loss of Canadian customs revenue which must somehow be replaced by the federal government.

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[6] This is discussed below in Section **2.3.3.** - Tariff Acceleration.

[7] These matters are more fully discussed in Sections **3.1** and **4.1.1** below.

2.2.1.2 Tariff Classification:
Given the complexity and the scope of the FTA, surprisingly few difficulties relating to tariff changes have arisen in the first year of implementation.

Some initial complaints about increased rather than decreased tariffs resulted largely from the U.S. move to the *Harmonized System* of tariff classification shortly after the coming into force of the FTA. This type of difficulty also occurred when other countries introduced the *Harmonized System*, and normally have been resolved through consultations at the GATT or through technical groups at the *Customs Cooperation Council* (CCC). Countries other than Canada have also expressed concern over some tariff classifications rising from the U.S. interpretation of the new system.

2.2.1.3 Rules of Origin:
In order to move tariff free between Canada and the United States, goods must be classified as being of domestic origin. A new *Certificate of Origin* acceptable to both governments was designed and is now in use. Seminars have been conducted by Customs officials to explain the proper use of these forms.

There have been some reports, most often on an anecdotal basis, of difficulties relating to inspections to verify marks of origin. These have included reports that some trainload lots of lumber products have been delayed or refused entry to the United States because it could not be determined that each individual piece bore the correct markings, enforcing what one senior External Affairs official called "an obscure regulation". Similar difficulties have been experienced by some of those shipping steel construction material[8].

The question of goods of third country origin, particularly the so-called "maquiladora" goods from Mexico, and their incorporation into domestic goods, and rules over material transformation, are discussed below in Section 3.4 Export Promotion Zones.

2.2.1.4 Public Travel:
Initial confusion by the general public about the effect of FTA tariff reduction on dutiable goods seems to have abated. At the outset, many people thought that free trade meant no more duties on imported goods. In point of fact, while tariffs are in the process of reduction, many duties remain and the federal manufacturers sales tax and excise taxes are still payable on entry[9].

Border officials have been helpful in explaining these changes to the travelling public, and in helping them organize their claims to maximize allowable duty free entry of goods.

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[8] This may be a further example of a U.S. legalistic zeal inconsistent with the spirit of the Free Trade Agreement.

[9] It is important to note that federal customs officers are not empowered to collect provincial sales taxes on goods imported by the travelling public. Purchasers of out-of-province goods are on their own recognizance to report their purchases and remit taxes, whether they have visited another province or another country.

In a number of border areas, there recently has been increased concern over the number of shopping trips taken by Canadians to the United States. This has been of particular note in Thunder Bay and Sault Ste. Marie, Ontario, as travel between those cities and their U.S. neighbours is up significantly. Overall, day trips by Canadians to the United States are up 21 per cent over 1988. Total border crossings at the Thousand Islands are reported to be up 17 per cent in the first half of 1989 and the Watertown and Buffalo regions of New York report greatly increased numbers of Canadian shoppers. There have been similar reports from both the East and West coasts. It is believed that this trend to cross-border shopping, coupled with what can only be typified as increased smuggling[10], has had a negative impact on the sale of retail consumer goods and gasoline in Canada. While there is less evidence of increased concern over this matter in Vancouver and Windsor, where cross-border shopping trips have been common practice for many years, there has been an increase in border transits and customs declarations at adjacent border crossings.

The total number of border crossings by Canadians has increased an average of 31 per cent at the 27 major crossing points between Canada and the United States. As well, customs declarations are up, often at a rate ten times or more greater than the increase in the number of crossings. For instance, at Windsor, crossings are up only 4 per cent, but customs declarations are up 126 per cent and, at the Thousand Islands Bridge, crossings are up 17 per cent and declarations are up 56 per cent. As well, the increased volume of travellers, coupled with low or non-existent tariffs on many goods, has led to more motorists being "waved through" without a full customs declaration, particularly in the case of those making grocery purchases, at Sault Ste. Marie, Windsor, and the Niagara region.

Kubas Associates of Toronto estimates that $2 billion will be spent by Canadians on consumer purchases in the United States this year, more than 1 per cent of total Canadian retail spending.

While some of this increase can be attributed to the increased value of the Canadian dollar, which has accentuated cross-border price differentials, a significant increase in border crossings also occurred in 1989, when the dollar has been more stable. There has also been a large increase in the number of Canadians stopping at Customs before leaving Canada to check on tariff levels for various goods and some U.S. stores have begun to post Canadian Customs rates. At least one study has pin-pointed the presence of the FTA as having heightened the awareness of some of the attractions of cross-border shopping, even if it can not be said to have as yet altered rules, regulations, or duties in a significant way.

2.2.2 Temporary Right-of-entry:

Border officials on both sides report the new rules to be working smoothly.

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[10] The Thousand Islands customs office reports a 47 per cent increase in the number of Canadians caught with undeclared or undervalued goods; presumably, many more escape capture. "Festive free-trading" *Kingston Whig-Standard* December 9, 1989.

Immigration officers were briefed on the new exemptions for temporary entry and initial confusion over the interpretation of regulations is under review.

Following the consultations required under Article 1503 of the FTA, at its second meeting the Commission accepted a number of proposed changes to the provisions of Chapter 15 and amendments to the list of eligible professions in Annex 1502.1. Following a sixty-day notice period for public comment and a review by officials of any response received, the approved changes will be implemented. The proposals were published in the *Canada Gazette* on December 30, 1989, but have not yet been given notice in the *Federal Register.*

The changes to the *Temporary Rights of Entry* provisions include: the clarification of a number of definitions, including minimum standards for each included professional group; easing entry requirements for regularly scheduled bus operators; and some new additions sought by professional groups on both sides. At their own request, journalists have been deleted from the list of professions eligible for temporary entry under the new FTA rule, but they can continue to work in both countries under the provisions previously in place.

- There is some evidence that companies are taking advantage of these provisions, particularly among service companies and high-technology firms recruiting sales support and research staff from both sides of the border.

- There is perhaps less cross-border activity in the construction management and architectural fields than had been anticipated. While there is little evidence that larger and fully integrated U.S. firms are as yet working in Canada, it is still very early in the process of integrating the North American market in these fields.

Cross-border movement of professional and service personnel is likely to increase as more companies become aware of what is possible. For example, in a speech given in Toronto on December 8, 1989, New York State Governor Mario Cuomo praised the temporary entry provisions as being of great benefit to the United States. He said that the United States will have a shortfall of up to 700,000 engineers and other "high tech" specialists as it moves to compete with Europe after 1992 and with Japan; Cuomo therefore welcomed the open borders for highly trained Canadian professionals. In questions following the speech, one person indicated that such a "brain drain" might be detrimental to Canada. The response was, "I leave it to the Canadians to secure their own interests"[11]. Of course, right-of-entry works both ways, and Canadian companies seeking highly-skilled personnel for research and development can also draw on a larger pool of talent.

2.2.3 Dispute Settlement:

Even though a maximum 30-day consultation period is provided for in the FTA, it is noteworthy that many of the most contentious disputes referred for consultation, some

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[11] "Free trade also killing U.S. jobs, Cuomo says" *Toronto Star* December 9, 1989.

from as early as January 2, 1989, remain under consultation at the level of the Canada - United States Trade Commission[12].

While the FTA does not require that the Commission refer matters to panels if a mutually agreed course of action for resolution or further study is arrived at by the Commission, it was expected that these political level consultations would be replaced by panel determinations under the new Dispute Settlement Mechanisms (DSM) if agreement was not to be reached within the time frame set for the Commission by the FTA.

- For instance, the earliest dispute sent to the Commission, over plywood standards in Canada and the United States[13], has been at issue for years and appears to be moving no faster towards resolution since its referral. The Commission has simply recognized the already on-going consultations and expert examination as a part of its work and awaits their completion. In fact, at its November meeting, the Commission sent a letter to the Binational Committee on Plywood Standards "urging the submission of recommendations on common standards" no later than February 28, 1989.

This early tendency for disputes to remain at the level of the Canada-United States Trade Commission raises the following issue:

- Canadian groups, such as the softwood lumber industry, have alleged in the past that when the government undertook the management of disputes on their behalf arising from United States trade actions, consultations and political manoeuvring at Cabinet level or at the officials level at External Affairs both reduced the chances of getting a fair deal through the maximal utilization of the U.S. court system, and permitted other bilateral issues external to the matter at hand to intrude to the detriment of a full prosecution of their case.

It was the hope of these groups that panel references would bring single-minded attention to the dispute at hand. It is not clear that all that much has changed when disputes remain at the level of the Commission.

Eliminating the delays and opportunities for intrusion of extraneous issues has been a goal of many reformers of international trade dispute settlement mechanisms.

However, even in the case of an early panel reference, if there is a lack of political will in accepting panel decisions issues may remain unresolved[14]. Nor does the notion of making panel decisions binding necessarily solve the dilemma, since if all panels were binding, it is thought that far fewer matters would be referred there. However, allowing access to panel procedures from non-government actors, such as the injured parties to a

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[12] See Section 2.3 below.

[13] Discussed in Section 6.1.3 below.

[14] See Section 6.1.1 -- West Coast Fish Landing Regulations.

dispute, coupled with the binding of bilateral panel findings, might lead to greater utilization and adoption of results.[15]

2.2.3.1 Current Disputes:
A number of irritants left over from the pre-FTA era remain as points of contention between the two countries. These are either now proceeding through Chapter 18 or Chapter 19 dispute resolution[16], or are the subject of ministerial and official level consultations.

- Canada got off to an early start, first requesting consultations on January 2, 1989, on disputes over the failure of the United States to implement the agreed reductions of tariffs on plywood and over U.S. wool product reclassification under the Harmonized System. These two matters remain at the Commission level, under consultation, and have not yet been sent for panel review.

- The United States, perhaps because of the transition to a new Administration at the New Year, did not initiate any proceedings until May 24, 1989, when, on his first working visit to Canada, U.S. Commerce Secretary Richard Mosbacher announced a request for a panel on Canadian fish landing regulations. This is discussed below.

A number of additional disputes subsequently submitted for consultation may be sent to panel review, should the Commission decide that it cannot resolve the issues itself. These include alcoholic beverage and beer pricing practices in Ontario[17], the long-standing difference of opinion over plywood standards, cable retransmission rights, meat inspections, and rules of origin and marking requirements for manufactured goods.

A number of other matters have been raised and sent to panel adjudication. Each side has now initiated one action under Chapter 18:

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[15] This matter is further discussed below in Section 6.4 -- Judicialization.

[16] Chapter 18 provides the general institutional and dispute settlement mechanisms. Chapter 19 sets up a special bi-national court for reviewing anti-dumping and countervailing duty matters as an interim arrangement until new substantive provisions in these areas are negotiated. Chapter 17, which deals with disputes over financial arrangements, is similar to Chapter 18, but officials and panellists will be selected by the respective Finance Departments.

[17] While the brewing industry is "exempted" from FTA rules, "new practices" introduced in the summer of 1989 by the Ontario government liquor board may have opened this matter for FTA investigation. As well, provincial wine stocking and pricing practices continue to be of concern to the United States.

- The United States brought a complaint against Canada's landing requirements for salmon and herring on the West Coast[18]. A panel investigation and report were completed on an accelerated schedule. Its findings are still under review at the Commission.

- Canada officially launched a complaint over new U.S. import restrictions on live lobsters on December 12, 1989, the same day they were signed into law by President Bush. Although an accelerated timetable has also been requested for this panel, at the time of writing, the Commission has not acted on this request. This matter was discussed at the Commission level on November 30, 1989, and had been the subject of continuing consultations at the officials level for some time.

There have been requests for twelve Chapter 19 panels to review countervail and anti-dumping actions:

- 11 have been initiated in Canada seeking review of U.S. actions over a variety of matters including red raspberries, self-propelled paving machine parts, Canadian salt cod, pork, and steel rails.

- Only one action -- against a Canadian Import Tribunal decision on induction motors -- has been brought against Canadian decisions to date[19].

The first case referred to a Chapter 19 panel, a review of the final results of the U.S. Department of Commerce International Trade Administration's (ITA) administrative review of the U.S. anti-dumping order against red raspberries from Canada, reported on December 15, 1989. This panel made two findings: it affirmed the ITA finding on the similarity of like-products and its use of constructed values; it found, however, that a simple statement by the ITA that the inadequacy of home country sales were relevant for determining home country value, without providing a definition of adequacy, was an insufficient basis for ruling. The Panel remanded the decision for thirty days to allow the ITA to provide the evidence on which it had based its decision before making a final ruling on the matter[20].

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[18] See **6.1.1** West Coast Fish Landing Regulations.

[19] The number of disputes reported here includes each dispute referred to the Binational Secretariat for examination and/or resolution. However, the number is often cited as smaller by some commentators since some of the disputes are related to the same matter. Action can and has been brought at each of a number of stages of a countervail or anti-dumping action, such as preliminary and final determinations and initial findings of injury at the U.S. Commerce Department and the ITC, so that a single action, such as that over subsidization of pork production in Canada, can be before two panels at once. This matter is discussed further in Sections **6.0** and **6.3** below.

[20] *In the Matter of Red Raspberries from Canada: Clearbrook Packers et al v. United States Department of Commerce International Trade Administration* Article 1904 Binational Panel USA-89-1904-01 December 15, 1989. This deadline was later extended and the matter remains unresolved. See **6.2.1** - Red Raspberries below.

The full list of matters before the Binational Secretariat is presented in Annex I.

Two issues, which have been the subject of recent GATT rulings -- Canadian market management methods for ice cream and yogurt and the decision on the U.S. Superfund tariff on oil imports and customs users fees -- may have a wider impact on the future use of FTA mechanisms:

- The Ice Cream and Yogurt decision demonstrates that some of the areas that the FTA left untouched can and will be subjected to continued scrutiny by the United States through multilateral channels.

- With respect to the Superfund Tariff, the United States finally has begun the process of equalizing the tariff rate, in conformity with a 1987 GATT panel finding that the U.S. tariff nullified and impaired benefits to other GATT members. Canada and other countries had reached the stage of the GATT dispute settlement process of requesting the initiation of retaliatory action, although the U.S. response probably means that the matter will not be put to a vote of the Contracting Parties[21]. Canada has separately negotiated an agreement for the phase-out of the customs users fees.

U.S. action on the Superfund Tariff may indicate that the U.S. is becoming more responsive to GATT actions, or at the very least, that the GATT may be prepared to take action against recalcitrant members, and that the bilateral mechanisms established under the FTA can provide a coincident and/or alternate avenue for the resolution of disputes with the United States.

Further evidence of this is provided by the pork subsidy dispute[22]. Canada has requested review under both the new FTA mechanisms and the existing GATT rules. While the final determination of subsidy made by the Commerce Department has been referred to one Chapter 19 panel, due to report by early July, 1990, and the U.S. ITC finding of a threat of injury referred to another, which is due to report at the end of August, 1990, Canada has, in addition, requested the formation of a GATT panel to review whether the U.S.

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[21] Canada had prepared a list of seventy items from which it intended to select items for a retaliatory tariff if the U.S. did not expedite the removal of this particular tariff. If the matter had been put to a vote and the GATT had authorized retaliation, it would only have been the second time it had done so, the only other occurrence being in 1953 (GATT *Basic Instruments and Selected Documents*, 1S 32). However, the U.S. Congress passed legislation which removed the discriminatory aspects of the oil-tax on November 22, 1989. While legislation has not yet been passed to eliminate the customs-user fee of 0.17%, also ruled improper by the GATT, Canada is not likely to continue its action on this matter since the fee is scheduled to be phased out under the terms of the FTA.

[22] See Section 6.2.2 below.

assumption that Canadian pork processors benefit automatically from assistance to swine farmers is contrary to GATT procedures.

2.2.3.2 Panel Rosters:
Rosters have been selected and the names published from which each dispute panel will draw its members when established by a referral from the Commission.

In the case of Chapter 19 disputes, for the most part the roster consists of lawyers. For Chapter 18 panels, trade experts and those more familiar with international trade negotiations and the larger Canada-U.S. trade agenda predominate. As well, Chapter 18 panels can, by mutual agreement, draw on outsiders with expertise in the matters before them[23].

The panel rosters and the methods of selection are currently under review by the Commission and the Binational Secretariat with a view to eliminating the difficulties which have arisen in selecting panellists without any appearance of a conflict of interest. The United States recently has submitted a list of twenty new names for consideration and Canada may soon be adding to its list as well. It is expected that the total number of panellists will be increased.

These changes have come partly in response to the difficulty experienced in several cases when panel selection has been delayed until a complete inventory of all work undertaken by the firm of a potential panellist has been reviewed to ensure that there would be no real, apparent, or potential conflicts resulting from other work being done within their firms. This task has been both lengthy and difficult, since expertise on some matters is spread very thinly in both countries and law firms with hundreds of lawyers are now common, particularly in the United States.

2.2.3.3 Rules of procedure
The rules and procedures as initially set out in the FTA have been expanded and amended by the publication of further regulations in both countries, as required by the FTA.

Some changes to the Article 1904 review process were agreed to by Canada and the United States in November 1989. These changes, largely procedural in nature, were published in the *Canada Gazette Part I* on December 23, 1989, beginning at page 5398.

A comprehensive review of the rules and procedures will be undertaken by the two parties in Mid-1990. The Department of External Affairs is accepting written advice on these matters until June 30, 1990.

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[23] The first such panel, examining the FTA and GATT compatibility of Canada's new fish landing regulations, included a U.S. and a Canadian fish industry expert. Both were former officials, and therefore thought less likely to have conflicts of interest.

2.3 THE CANADA-UNITED STATES TRADE COMMISSION

The Commission established to manage the FTA consists of only the trade ministers of the two countries, the Honourable John Crosbie and the Honourable Carla Hills. They have, as a matter of course, delegated much of their authority to persons working at the officials level.

The first meeting of the Commission was held March 13, 1989, in Washington, D.C. The agenda of that one-day meeting included preliminary discussion of many of the irritants discussed above and the rules of procedure for the Commission. The Commission:

- decided that meetings would take place twice a year, with officials consulting regularly between the meetings;
- set initial parameters for the working groups on agriculture;
- finalized details and procedures for two important working groups called for by the FTA -- on the automotive industry and on subsidies; and
- agreed on a timetable for accelerated tariff reduction negotiations.

These matters are all further discussed below.

The second meeting of the Commission took place in Ottawa on November 30, 1989. *Inter alia:*

- Reports and proposed work-plans were received from two working groups: the Select Panel on the Automotive Industry and the Tourism Working Group.
- The Commission examined the work of the Chapter 19 Working Group, which was established by the Binational Secretariat to review the functioning of the dispute settlement process, and agreed to some amendments to the rules of procedure for binational review to ease some technical difficulties.
- The Commission addressed a joint letter to the Binational Committee on Plywood Standards, urging it to submit recommendations for common standards by February 28, 1990.
- Two new working groups were established: a group studying technical barriers to trade in fishery products was added to eight agricultural working groups previously established in accordance with Article 708, and a Services Group was established to monitor the implementation of Chapter 14 and to consider the expansion of liberalization of trade in services pursuant to Article 1405.

- New guidelines and expanded coverage for the temporary entry of professional workers[24] were agreed to.

- The Commission also agreed to accelerate the elimination of tariffs on approximately 400 tariff line items[25].

The two Ministers continued discussion of various trade disputes that had not yet been sent to panels, as well as dealing with the panel report on Canada's fish landing requirements.

The *Subsidies and Trade Remedy Working Group* coordinators for the two countries were scheduled to attend the meeting as a follow up to their first formal working session held November 14, 1989[26] to discuss their tentative work plan and timetable with the Ministers.

2.3.1 Automotive Panel:

The *Select Panel on the Automotive Industry* consists of thirty non-government members, fifteen from each country.

The Canadian members nominated to this group include Darcy McKeough as Chairman, representatives of the "big three" North American companies, the Canadian Autoworkers Union, the Asian transplant companies, auto parts manufacturers, distributors, and the Consumers Association of Canada.

The United States appointees include people from the "big three", the auto-parts industry, and the unions, but does not include representatives from foreign-owned companies.

The panel has been given a two-year timetable to complete its work.

The task of the panel, set out under Article 1004 of the FTA, includes assessing the state of the North American automotive industry and making proposals for public policy measures and private initiatives which might lead to an improvement in its competitiveness in domestic and international markets.

As well, the two governments each provided the panel with specific instructions regarding their respective priorities.

- The Canadian request focused on global competitiveness issues.

- The U.S. position, while also considering those matters, stressed rules of origin and subsidy issues as of primary concern.

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[24] See Section 2.2.2 above.

[25] See Section 2.3.3 below.

[26] See Section 2.3.2 below.

At the first full meeting of the *Select Panel*, held in Toronto on August 8, 1989, the panel agreed to commission two studies: one on global competitiveness; and another on the impact of a proposed increase from the Autopact's 50 per cent North American content requirement to a 60 per cent level.

No agreement was reached on the matter of subsidies.

In addition to this meeting, the co-chairmen have met three times and each group has held separate national meetings.

The Canadian panellists met December 20, 1989, in preparation for the second full meeting of the panel, which was postponed from the autumn and held in New York on January 9, 1990.

The make-up of the two national groups appointed to the Panel appears to reflect a significant difference of opinion over the task of the panel, and of the general view of the automotive industry taken by the two governments. The Canadian group includes representatives of U.S. companies[27], Korean and Japanese manufacturers, as well as dealers, specialty manufacturers, and consumer groups. The U.S. group, on the other hand, contains no representatives from any foreign companies, and its membership is drawn entirely from the industry.

At its first meeting, this group could not come to agreement on its first task -- whether to work to make the industry more globally competitive, or to ensure a more stable and protected market in order to ease the adjustment period. On both sides of the border, two of the "big three" automakers favoured an increase in North American content, one opposed it. There was a split between the two union groups, with the U.A.W in favour of an increase in North American content, the C.A.W. preferring more study of the impact before taking a position. The transplants were not represented at this meeting. In the end, uncertainty over the impact of such a change led the Panel to opt for the commissioning of a study. The parameters and timetable of this study were to be discussed at the January meeting of the Panel.

2.3.2 Subsidies and Trade Remedy Working Group:

The *Subsidies and Trade Remedy Working Group* consists of government officials from Canada and the United States.

These officials will be responsible for completing the negotiations on the definition of, and guidelines for, subsidy practices as set forth in Article 1907 of the FTA. This question

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[27] There are, of course, no major "Canadian" automotive producers, although the parts industry has several major Canadian players. Concern has been expressed that the Canadian representatives of the American subsidiary companies may, in practice, represent the same view as their U.S. parent company executives who are also a part of the group.

was set aside in late 1987 when it became clear that agreement could not be reached within the deadlines set for completion of the original FTA negotiations.

- The Canadian group is chaired by A.L. Halliday, who is also Director General of the Free Trade Management Bureau of External Affairs. Tom Bernes, Director General, International Trade and Finance Branch, Department of Finance, is the Canadian vice-chairman. At External Affairs, a five-officer group works with Mr. Halliday, who can, as well, draw on expertise from various other government departments or groups within External Affairs.

- The U.S. group is led by Anne Hughes, a Deputy Assistant Secretary in the Department of Commerce.

The FTA sets out a five-year period for these negotiations, with a possible two-year extension.

The proposed schedule for the negotiations included a preliminary meeting to set out the parameters of work, held November 15, 1989; consultations with the Canada-United States Trade Commission, held November 30, 1989; and consultations with provincial officials, held in the first weeks of December, 1989.

The next phase includes developing detailed negotiating objectives in the context of the information collected from the studies currently being conducted on subsidy practices. Mr. Halliday has stated that a full catalogue of the types of U.S. practices which will be considered will have been completed by March, 1990, and should be available for parliamentary scrutiny.

The original negotiating mandate set forth by the U.S. Congress for amendments to the FTA sets June, 1991, as the deadline for submission of an agreement on subsidies, if it is to take advantage of the "fast-track" authority[28]. However, it is possible for the Executive Branch to seek an extension from Congress for on-going negotiations, and the U.S. implementing legislation, in setting out the same five-to-seven year timetable for subsidy negotiations as the FTA, may provide the Administration with the same "fast-track" authority for the full seven-year duration of the negotiations[29].

Rather than seeking to meet that earlier deadline, it was decided, in Canada at least, that the negotiations underway in Geneva should be allowed to run their course before serious efforts to negotiate bilaterally are undertaken and the United States has now agreed.

The Geneva MTN is scheduled to be completed by the end of 1990, which means that binational negotiations are not expected to get underway until at least 1991.

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[28] H.R. 5090 Sec. 102(e).

[29] H.R. 5090 Sec. 409 (4).

With a 1991 start-up, and given the complexity and potential sensitivity of the subject under negotiation, some concern has been raised that a failure to complete the talks within the U.S. congressional deadline for "fast track" approval would threaten the adoption of any agreement in the United States. However, in an appearance before a Committee of the House of Commons, Mr. Halliday said: "I would not want it [the deadline] to be seen as something that is imposed on Canada by the Congress to conclude in that time. We have to take our time to get a good agreement rather than to be stampeded into one to meet a particular fast track authority."[30]

The Chairman of the Canadian Group has indicated that a great deal of consultation with all concerned groups will be held, both on the substance of the talks and the process for undertaking them[31]. The negotiations themselves, however, will likely be closed to public scrutiny and participation, as were the FTA negotiations. While consultation will concentrate on officials level contact with other national and provincial government departments and through the ITAC and SAGITs, Mr. Halliday has said also that "if any other group wants to consult with us on this topic, and we recognize the importance they attach to it and the sensitivities with which this exercise rightly or wrongly has been beset, we would be very happy to consult with them. So in our consultation we would be totally open to the extent that the consultative mechanisms allow us. ITAC-SAGIT is not totally open, but the other consultations would be open, and in the preparatory stage I do not think there is any problem."[32]

Concern has been expressed that during the lengthy course of these negotiations, the government will not make full use of the mechanisms of the FTA or of the GATT to prosecute cases against the United States, should any arise, that might threaten the negotiations. The Minister of International Trade, John Crosbie, has said: "it is not necessarily in our interests to be complaining everyday about some other country or some trade practices of theirs. It is to get the trade practices you object to changed that is in our interests, not to engage in public slanging matches about other countries trade practices".[33]

There is, conversely, some feeling that the Government of Canada and the provincial governments may in the interim avoid actions which might be threatened with countervail by the United States. For example, the Government of Canada has cited the possible negative reaction of the United States, and the real possibility of countervailing actions, as one of the reasons it will not move to keep open, by subsidy or otherwise, east coast fish plants currently facing closure. The Government also has indicated that no new specific

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[30] *CANADA. House of Commons. Standing Committee on External Affairs and International Trade* Proceedings November 7, 1989. P. 21.

[31] TOULIN, A. 1989 "Free trade negotiator wants advice" *Financial Post* Aug. 30 p.4.

[32] *CANADA. House of Commons. Standing Committee on External Affairs and International Trade* Proceedings November 7, 1989. p. 9.

[33] *CANADA. House of Commons. Standing Committee on External Affairs and International Trade* Proceedings May 25, 1989. p. 31.

assistance programmes will be introduced, citing potential U.S. reaction as one reason for not doing so.

These concerns illustrate the worry expressed in Section 2.2 that the more legalistic attitudes of U.S. actors and agencies threatens to create an imbalance in the unfolding of national policies under the FTA regime. There appears to be no reduction in the use of U.S trade remedy laws, nor of the threat of their use, on the part of U.S. business seeking protection. This has disappointed many Canadian proponents of the FTA who had hoped for a more co-operative atmosphere -- for access more secure than under the prior regime -- rather than a continuation of or even increased harassment during the period of the subsidy negotiations.

Some commentators and U.S. trade law experts have suggested that Canadian companies and government agencies should undertake countervail cases against U.S. subsidy practices to heighten attention in the United States. Canada has not taken this path in the past, having brought only one CVD action against the United States -- over corn subsidies.

Canadian exporters have always been subject to U.S. trade remedy law, and no one expected a total absence of disputes. It was hoped, however, that any new actions against the subsidy practices that are the subject of the negotiations would be postponed or that the benefit of the doubt would be given to the other country. This has not been the case.

At the same time, there may be a greater reluctance in Canada to fashion public policies that might rock the boat.

A case in point is the withdrawal of Canadian government support for an energy infrastructure project in Quebec because it believes the United States might bring a countervail action against any products or energy exports making use of the system. In explaining the government refusal to provide funds for the 800 km Soligaz pipeline, Energy Minister Harvie Andre said: "The advice coming up from my department was that it would be subject to countervail. Our judgement was that we did not want to risk it"[34]. However, the various U.S. trade courts have not yet found government participation in such infrastructure projects, particularly if done on a market basis, to be countervailable.

For its part, the Government of Quebec has taken this distinction to heart and remained committed to the pipeline from Sarnia to Montreal, making their contribution in the form of an investment from which they expect a return, which they therefore hope will not lead to a successful countervail action. However, natural gas producers in the United States, already unhappy with the FTA for increasing competitive pressure for them in eastern states, may nevertheless try to take action should the pipeline be built.

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[34] "U.S. penalty threat stopped federal subsidy to pipeline" *The Citizen* October 5, 1989. P. C17.

As yet further cases in point, the USTR has begun the process of examining Canadian subsidy practices in parts of the mining industry and of durum wheat production under the Baucus-Danforth review procedures[35] and is likely to receive additional requests.

2.3.3 Accelerated Tariff Reduction:

The FTA included a provision for interested parties to request accelerated reductions to, or elimination of remaining tariffs. The first acceleration agreement was initialled at the second meeting of the Canada-United States Trade Commission, held November 30, 1989, in Ottawa.

This agreement, when implemented, will remove or speed the reduction of tariffs on about 400 items which previously have represented about $6 billion in cross-border trade.

The agreement needs to be approved in Canada by the Cabinet and in the United States by Congress and is expected to come into force on April 1, 1990.

It was also agreed that the two countries would continue to examine the possibility of further tariff reduction acceleration on other items.

The agreement is the culmination of a process begun just prior to the first meeting of the Canada-United States Trade Commission in March of 1989, when a notice was placed in the *Canada Gazette* and in the *Federal Register* inviting requests for an acceleration of the tariff reduction schedule set out in the Free Trade Agreement. The two governments agreed to accept requests until March 31, 1989, and a preliminary list of items was exchanged on April 19. The final list of items that had been requested for accelerated tariff reduction was published in a 940-page supplement to the *Canada Gazette* on July 15 with comment welcomed until September 1, 1989.

Negotiations began shortly thereafter. Over 5000 tariff line items were submitted to the two governments for negotiation: 2800 items in 300 requests in Canada and 2200 items in 200 requests in the United States. Each country undertook a review of the items submitted, to determine which would go to negotiation. Approximately 1000 items were ultimately subject to negotiation. Agreement was reached on 400.

Even though parties on both sides of the border had made similar requests, agreement was not reached on the major portion of the 5000 items because "broad industry support", required by the two countries for acceleration, was said to be lacking.

Though there appears to have been little quarrel with the list of 400 items finally agreed upon, the entire process of accelerating rate reductions seems to have provoked some unease principally among the opposed firms or industries.

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[35] H.R. 5090 Sec. 409(b). See Section 2.5.3 below for an outline of this process.

Critics of the process have pointed out that the time available for consultations was extremely short; comments were accepted for only six weeks over the summer. While public hearings were held by the ITC in the United States, and all representations made there are on the public record, consultations and representations in Canada were closed to public scrutiny. While over a thousand representations were made to the negotiating group by concerned Canadian groups and companies, only a few, made public by the people who had submitted them, are available for scrutiny.

It has been suggested by some that early tariff elimination, and especially the acceleration of agreed to schedules, favours multinationals keen on immediate restructuring, or larger or already competitive companies, that are ready to take on international competition immediately, over smaller domestic manufacturers. In fact, the phasing of tariff reductions rather than immediate elimination was supposed to allow for gradual adjustment -- so as to protect those who are not yet able to compete or who will have high adjustment costs.

During the course of the FTA negotiations many companies, unions and analysts agreed that if tariffs were to be eliminated they would need some time to adjust and would go along only if they had temporary protection. As noted above, tariffs were organized into three groups, generally based on how quickly it was thought an industry could adjust to free competition with American producers. It is therefore not surprising that there has been some negative reaction to the idea of acceleration from among those who either still benefit from protection or who need more time to adjust.

While much of the concern over the acceleration process appears to be in the nature of grumbles, it would appear that there is a need for a mechanism, should future proposals for acceleration be advanced, which would provide more public assurance that a clearly defined "substantial portion" of an industry, on both sides of the border, has agreed. Where objections exist it would also be useful to provide more public evidence that they have been heeded. This would allow all companies a higher degree of certainty in planning adjustment.

Both countries are now in the process of hearing initial proposals for a second set of tariff reduction accelerations.

2.3.4 Agricultural Working Groups:

Eight working groups were established early in 1989 by the Commission under the terms of Article Seven of the FTA to deal with the various sub-sectors and issues in the agriculture sector.

An additional group was agreed to at the November, 1989, meeting of the Commission and the work of several other related groups, already underway prior to the coming into force of the FTA, had their work hastened or enhanced at the request of the Commission.

Each of the working groups is now active and work plans have been set out for initial meetings with their U.S. counterparts. Provincial agriculture officials have been consulted, and the Ministers have met. While each group has its own schedule and timetable, all are

following what some commentators have called "a leisurely pace", undoubtedly because both Canada and the United States are expending primary energy towards completing the Uruguay Round, hoping to clear the way for a multilateral agreement that would set the parameters for a more extensive bilateral accord. The likelihood of success at the Uruguay Round is discussed below.

Canadian Agriculture Minister Don Mazankowski and U.S. Secretary of Agriculture Clayton Yeutter met in June, 1989, for the first semi-annual consultation on agriculture issues called for by the FTA, but by autumn the unqualified support for the agreement of at least Mr. Mazankowski had been tempered by "concern and annoyance". Mr. Mazankowski, in referring to the United States countervail action against Canadian pork, said: "This represents a certain amount of bad faith on the part of the U.S., not to mention an inconsistency with the GATT". With reference to the condition of the Canada-U.S. relationship in general, he said, "Regrettably, by their [U.S.] recent actions on the agricultural front, rather than harmony, we have harassment".[36]

At their second meeting, held December 19, 1989, the two Ministers addressed these and other problems such as:

- Spot checks on Canadian meat at the U.S. border;
- the reclassification of sugar blends; and
- the U.S. position on dairy quotas.

Secretary Yeutter also gave assurance to Mr. Mazankowski that the U.S. ITC investigation of Canadian durum wheat under Sec. 409(b) did not have Administration support and would likely go no further than the ITC investigation.

In the FTA, both countries agreed to end the use of export subsidies with respect to trade with each other, the first such international agreement in the agriculture sector. Canada's FTA implementation legislation contained an amendment to the *Western Grain Transportation Act* bringing into force the commitment to exclude from subsidy grains destined for U.S. consumption. The United States has never applied its *Export Enhancement Program* (EEP) to shipments to Canada, although under this programme it subsidizes its agricultural shipments to some of Canada's traditional export markets. Canada has complained that in doing this the United States has not taken sufficient notice of Canada's export interests, as is required by the FTA in Article 701(4).

While some commentators suggest that agriculture subsidy practices are not a part of the Article 19 subsidy and trade remedy negotiations, they are nevertheless likely to be affected by those negotiations. Agriculture subsidies are pervasive and contentious and the source of many of the current disputes and trade remedy actions taken by the two countries against each other. Whatever regime is developed to regulate, control or measure government

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[36] Don Mazankowski, from an address to the Calgary Chamber of Commerce, October 27, 1989. See also Section 6.2.2 Pork Production Subsidies below.

subsidies will either apply to, or set an example for, discipline in agriculture subsides as well. It also seems likely that a number of disputes over the agricultural assistance programmes of both countries will be referred to Chapter 18 and 19 panels for resolution during the subsidy negotiations phase[37].

No legislation was required on either side to put into effect the prohibition in the FTA against government entities, such as marketing boards, selling to the other country goods at a price below the sum of acquisition and related costs, since both countries already ostensibly do not do this. However, increased scrutiny by U.S. industry of activities by various market management boards in Canada, particularly the Canadian Wheat Board, is likely. The absence of defined criteria for acquisition costs, which will be resolved either through negotiation at the working group level, or through the Chapter 18 and 19 dispute settlement precedents, is also likely to lead to conflict between Canada and the United States.

2.3.5 Commission Secretariat:

A Secretariat has been established to support dispute panels under Chapter 19. The Binational Secretariat has two independent offices, one located in Washington and one on Ottawa. The Ottawa office operates as a separate department of government and has eight staff members who are described by the Director as "neutral international civil servants". The U.S. office is smaller and, at the time of writing, did not have a permanent Director, although the appointment of one was expected soon.

The Binational Secretariat acts as the court of record for all Chapter 19 disputes, maintains the rosters of panellists and verifies their eligibility for individual panels. It has also done some support work for the Chapter 18 panel which reviewed Canada's salmon and herring landing requirements, even though this may not explicitly provided for by the FTA.

This Secretariat has no independent means of conducting research or background work on the cases before it, relying instead in each case for work produced by the respective parties and the panellists. This may lead to difficulties in the future if not remedied. As well, no specific mechanism for ruling on the standing of parties seeking to bring matters to a panel or for panel adjudication is in place, leading to a two-to-three month delay in initiating proceedings. Institution of a permanent or standing "motions court" judge for the Secretariats' work would address this easily. Some changes designed to address these problems were printed in the *Canada Gazette* on December 23, 1989, and further changes

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[37] In general, the implementation of the agriculture provisions of the FTA also demonstrates the differing approaches of the two countries to utilizing the FTA, as noted above in Section 2.2.0. The use of the Chapter 18 panel against new U.S. lobster restrictions, and of Chapter 19 and GATT DSMs on the pork question, may, however, indicate a stiffening of resolve by Canada to prosecute its rights under the FTA.

to the rules and operating procedures of Chapter 19 panels administered by the Secretariat are scheduled for summer 1990[38].

Institutional provisions of the FTA have been identified by many as one of its weakest points. Little provision is made for independent, permanent or specific staff or research support either for the Commission or the Binational Secretariat. As noted earlier, the Commission consists only of the two trade ministers, with day-to-day operations delegated to officials at various levels. Support work, record keeping, and research are left to existing national staff.

[38]See Section 2.2.3.3. above.

2.4 MONITORING IMPLEMENTATION

Monitoring implementation may be taken to mean, on the one hand, the management of the process of implementation over the ten years to final tariff removals, the reports of the various working groups (particularly the subsidies group), the oversight of the dispute resolution processes, and the management of the Canada-U.S. trade relationship more generally.

On the other hand, it also implies the attempt to measure the costs and benefits of the Free Trade Agreement, the processes of adjustment to it, and the provision of analyses for the public record.

This section of the report canvasses the various organizations involved in "monitoring" and reports on their organization and activities to date. This report is itself an attempt to respond to the mandate of the Senate Committee on Foreign Affairs to maintain a monitoring role.

2.4.1 Organization of the Department of External Affairs:

Management and administration of the Free Trade Agreement in Canada rests with the Department of External Affairs[39] (DEA) through the Minister of International Trade.

Particular responsibility lies with the Deputy Minister for International Trade and Associate Under-Secretary of State for External Affairs (DMT), Donald Campbell. Primary oversight of FTA matters is exercised by a Senior Assistant Deputy Minister (United States) and Coordinator Free Trade Agreement. At the time of writing, this latter position was vacant, with responsibility being exercised by the previous incumbent, Donald Campbell, now DMT.

A request by External Affairs to Treasury Board in 1989 for an additional Assistant Deputy Minister position to administer the FTA was not approved. Consequently, FTA management duties were assigned to the Senior ADM-US Branch who was also designated Co-ordinator Free Trade. Konrad von Finkenstein was appointed Deputy Co-ordinator Free Trade and ADM FT Policy and Operations.

This area of the department was re-organized in the fall of 1989. External Affairs has established the Free Trade Policy and Operations Group, which consists of about 60

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[39] External Affairs has had "*and International Trade Canada*" added to the Department's letterhead to reflect the full responsibilities of the department and its two senior ministers, however the legal name remains the Department of External Affairs. A third minister, the Minister for External Relations and International Development, has some responsibilities for the delivery of consular and immigration services overseas and for the management of Canadian International Development Agency (CIDA) which is operationally attached to External Affairs, however official Development Assistance (ODA) decisions remain the responsibility of the Secretary of State for External Affairs.

individuals with various duties related to the implementation of the FTA, inside the U.S. Branch. About one third of this number appear to be almost exclusively working on FTA matters, the balance undertaking other duties relating to Canada's United States trade policy.

The Free Trade Policy and Operations Group reports to Konrad von Finkenstein, the Assistant Deputy Minister Free Trade Policy and Operations Branch and Deputy Coordinator Free Trade Agreement, through two Directors-General: A.L. Halliday who directs the Free Trade Management Bureau and D.G. Waddell, head of the United States Trade Policy Bureau. There is also a Free Trade Agreement Legal Services division under the direction of Morris Rosenberg.

An organization chart for the Free Trade Policy and Operations Group is attached as Annex II.

In August, 1989, Mr. Halliday was assigned additional responsibility as Canadian chairperson of the *Subsidies and Trade Remedies Working Group* which is to conduct negotiations with its United States counterpart. A six-officer group in Ottawa provides support to Halliday, who can, as well, draw on resources from other groups or departments as required. It is expected that a number of outside consultants will also be retained to do initial research work on U.S. subsidies prior to the beginning of formal talks with the United States.

A "Committee on the Free Trade Agreement" has been established, consisting of senior federal and provincial officials, to smooth access and provide for consultations between officials.

The Senior Assistant Deputy Minister for the Multilateral Trade Negotiations, Germain Denis, also reports to the Deputy Minister-Trade. The Office of the Multilateral Trade Negotiator (OMTN) group under his direction operates separately from the FTA management group. It is responsible for the progress of the Uruguay Round talks and for coordinating Canadian proposals in Geneva as well as for consultation with industry and their provincial government counterparts on MTN matters. The OMTN and the FT Policy and Operations Branch consult regularly and provide background material and support to each other in areas where negotiation and consultations overlap.

2.4.2 Other Government Departments:

Part of the regular work of the Department of Industry, Science and Technology (DIST) includes monitoring employment shifts, and plant closures and openings.

International Trade Minister, John Crosbie, told the House of Commons Standing Committee on External Affairs that DIST also was undertaking this type of monitoring work with respect to any of those employment or industrial changes which could be linked to the Free Trade Agreement, but that the Department had not yet made any results known to him. He promised to pass this information on to Parliament as soon as he received it.

DIST has not provided any public information so far, nor has it described the methodology it will be using to make such determinations[40]. It is known to be collecting data on an on-going basis respecting the expansion and contraction of investment in Canada, as well as monitoring Canadian exports and activities in the United States.

DIST has released a large number of research reports on the competitiveness of specific Canadian manufacturing and service industries[41].

The new Canadian International Trade Tribunal (CITT)[42], in addition to investigating Canadian anti-dumping and countervailing complaints[43], has been given a mandate to undertake general inquiries into trade and tariff and economic matters, such as alleged subsidization in other countries[44].

The Government has indicated that it will forward all reasonable concerns raised by Canadian producers to the CITT. However, it is still unclear what actions, if any, the CITT can take on its own. New draft rules governing proceedings, practices, and procedures of the CITT are to be released in early 1990. It is expected that the regulatory process to which such rules are subject -- including public comment and government review -- will be completed in the first half of 1990. The rules will then come into effect following publication in the *Canada Gazette*. These new rules are generally expected to conform to the practices of the CITTs three predecessor agencies.

Several other government departments also undertake work related to the FTA -- such as Agriculture, Fisheries and Oceans, and Finance -- but their work most often is related to technical implementation matters or to further negotiations. Little analytical or statistical

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[40] These duties have apparently not been separated from the regular tasks of this department, so no specific measure of the effects of the FTA may be forthcoming.

[41] These reports, known as *Industry Profiles*, as well as reporting on the competitiveness of each industry, also assess the likely effects of FTA on it. Generally speaking, they find that the FTA will be of net benefit to most, although in a number of specific cases, the need for significant adjustment and/or rationalization is identified.

[42] The CITT replaces three institutions: the Canadian Import Tribunal (CIT), the Tariff Board and the Textile and Clothing Board. It is responsible for countervail and anti-dumping injury inquiries and for appeals from Revenue Canada -- Customs and Excise decisions. See COLEMAN, J. 1989 New Rules, New Institutions: The CITT Ottawa: Centre for Trade Policy and Law. Mimeo.

[43] Actions such as these can now be brought to the CITT directly by individuals and companies who consider themselves injured by foreign trade practices.

[44] This change to the CITT has been made partly in response to the Baucus-Danforth amendment to the U.S. implementing legislation which provides that this type of inquiry can be undertaken by the USTR at the request of any interested parties. H.R. 5090 Sec. 409(b). See section 2.5.3 below.

work on the impact or effect of the FTA as a whole, or of specific FTA provisions, seems to be being produced within government, nor has any research, other than that enumerated above, been released to the public since the coming into force of the FTA.

It has been suggested that this failure is related not to an unwillingness on the government's part to undertake the work, but rather to the difficulties of doing it, and of reaching valid conclusions so soon following the Agreement's enactment[45].

2.4.3 Consultation and Advice:

While a good deal of consultation and negotiation is called for in the FTA, the FTA seems to provide little in the way of institutional support to facilitate undertaking that work. With only one exception, provisions were not made for independent institutions or support organizations for the work of the FTA.

Even in the case of the only institution specifically provided for in the FTA -- the Binational Secretariat established to support the Chapter 19 dispute settlement process[46] -- no provision was made for research capabilities or a permanent facility to receive requests for standing or review of possible actions. Nor was this institution intended to be long-lived; the Binational Secretariat is scheduled to close down following the completion of the work of the Subsidies and Trade Remedies Working Group in five to seven years.

2.4.3.1 The Possible Formation of an Independent International Panel:

International trade experts, economists, and political scientists often recommend that impartial binational or multinational panels be established -- to act as an impartial third party -- to monitor the trade policy and related activity of all parties to an agreement. This was also suggested as an aid to making the FTA work, but was not included in the FTA.

A binational, independent monitoring agency or research group could provide information and data to the Commission for discussion and possible action without the potential for a too intense political reaction that might flow from only one side raising concerns about the Agreement and its implementation. As well, matters extraneous to a complaint brought for adjudication could not so easily intrude if contentious issues -- such as subsidy levels, constructed and home country price levels, or the likeness of goods -- received consideration outside of national systems and/or the Commission.

Chapter 19 dispute panels are designed to operate in this way; consequently, it would seem a logical extension to undertake monitoring and research in the same way. However, governments, particularly the United States government, generally have resisted creating sovereign, trans-national or international courts for fear of constraining independent national actions.

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[45] This matter is discussed further in section 2.4.3.3 - Informetrica Feasibility Study.

[46] See Section 2.3.5 above.

It is important to note that it is still possible that even the relatively benign review procedures set forth in Chapter 18 and 19 may be subject to a Supreme Court challenge in the United States from those who believe the binational review limits their constitutional right of access to the courts or that it subordinates the U.S. courts to foreign review.

While no such bilateral independent trade monitoring body has yet been established, the GATT recently has begun to undertake a series of such reviews of individual country's trade policies.

Each GATT member country will, through a rotational list, be subject to regular reviews of the full array of both domestic and international trade practices, for consistency with their GATT obligations. The reviews are to be presented to the full GATT Council.

It was hoped that pressure brought to be bear by public scrutiny and documentation of inconsistencies at the GATT, with a requirement that countries indicate their plans of action to bring those inconsistencies into conformity, would ensure a higher degree of conformity with GATT rules.

The first three such reports are currently before the GATT. While all three reports enumerate a number of inconsistencies, GATT members failed to demand unequivocal responses from the countries involved, including the United States. Perhaps this indicates that an independent international panel under the FTA would also have difficulties in forcing the pace.

For the moment, Canada and the United States both continue to rely on existing staff and their respective industry advisory groups, which had been established earlier or for other purposes, to provide monitoring and advice on FTA matters.

2.4.3.2 ITAC and SAGITs:

The *International Trade Advisory Council* (the ITAC) and the *Sectoral Advisory Groups on International Trade* (the SAGITs) have remained active throughout the first year following the coming in to force of the FTA. While their primary activity at present is to advise the OMTN on Uruguay Round issues, a task force on Canada-U.S. issues meets regularly and the SAGITs were consulted during the lead-up to tariff acceleration negotiations.

ITAC and SAGIT meetings are not open to the public, nor is there any evidence of the establishment of formal reporting channels which would ensure that industry advice coming in or information flowing out actually reaches all those concerned.

Following the coming into force of the FTA, the Canadian Labour Congress (CLC) withdrew its objections to serving on SAGITs and other trade advisory bodies and recommended names for consideration by the Government. CLC representatives joined the ITAC in early fall of 1989; however, government consideration of the nominations to the SAGITs took longer, with final agreement on membership reached only in December, 1989. It is expected that additional labour representatives will join the SAGITs sometime soon[47].

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[47] The Canadian Federation of Labour previously had agreed to participate.

It should perhaps be noted that while membership on the ITAC and SAGITs is limited to Canadian citizens, several members of these committees are representatives of foreign-owned or controlled corporations.

2.4.3.3 Informetrica Feasibility Study:

In October, 1989, External Affairs commissioned a feasibility study on monitoring the FTA, seeking advice on the type and nature of macro-economic and anecdotal research and evidence which might be gathered, how it might be treated analytically, and how soon statistically relevant conclusions might be able to be drawn from this work.

The study was undertaken by Ottawa-based Informetrica, Ltd., which provided its findings in final form to the government on December 18, 1989. The report was subsequently released on January 19, 1990, together with comment from John Crosbie.

Informetrica's report confirms the commonly held view that accurate measures of the aggregate effect of the FTA cannot be made at this point. It says:

> It is not possible to provide a complete, professionally qualified assessment of the FTAs effect on economic performance in 1989 on January 1, 1990 or shortly thereafter. In fact, it will be some years before such an evaluation is possible[48].

However, there was a good deal that Informetrica thought should be done to improve the quality of assessment in the future. The report divided these things into three categories:

1) things that can be done now (that is, in December 1989);
2) things that should begin soon, in 1990 and 1991, to add to the procedures already underway; and
3) things that can be done more accurately after five years have passed.

The first category includes compiling evidence of compliance with the legal requirements of the FTA, and assessing trade flows in areas with tariff reductions, particularly in areas where the base tariff was high or where the reductions in barriers is immediate. As well, analysis of trade data to measure changes between the United States and the rest of the world as sources and markets for goods, with increased disaggregation as more data becomes available over time.

Informetrica also suggested that an analysis of investment intentions based on Statistics Canada's regular survey of business could be done to determine if the FTA has had any initial effect and that lists of anecdotal evidence be compiled concerning possible plant closures and openings which might be fully or partially attributable to the FTA.

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[48] McCRACKEN, M. *et al* 1989 Assessing the FTA: Design of a Framework December 18. Mimeo.

In the second and third year Informetrica recommends more in-depth analysis of the data collected to determine if there have been changes in the direction or amount of trade, or of intra-industry trade[49]. It also suggests that Canada alter the collection of statistics where required in order to distinguish between the United States and the rest of the world (ROW), rather than grouping all foreign countries together.

Finally, Informetrica raises the possibility that analysis of the rate at which disputes occur and the functioning of dispute settlement mechanisms will be possible in the near term and will be a useful measure of market access[50].

The study proposes that formal econometric studies could be started after about five years, once the major changes of the FTA are in place, new capital investments are in production, and micro-data begins to become available.

The government issued its first formal report on the progress of the FTA on January 19, 1990[51]. It purported to provide the information that Informetrica had said should be available and included in the first "annual review". In fact, while the government document and Minister Crosbie's statement accompanying the release did reflect the report's contention that an aggregate assessment of the economic effect of the FTA cannot be made at this time, Informetrica suggested that much more could be done in the short term than the government provided. These things included:

- an analysis of monthly trade flows, particularly for categories with large or immediate tariff reductions;
- an analysis of investment flows and private and public investment intentions;
- the compilation of a list of companies expected to be positively affected by the FTA, negatively affected, or little affected with a comparison of investment intentions across groups; and
- the presentation of lists of anecdotal information about plant openings and closures by industry.

The Informetrica report also suggested that it would be useful to include information about the Government's future monitoring plans in its first report. This was not done. In fact, the Minister was unwilling to comment at the news conference he hosted on any specific activity that will be undertaken, either by External Affairs or other government departments, with respect to the items identified by Informetrica as necessary for an adequate measure over time.

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[49] An increase in intra-industry trade would indicate increased specialization and rationalization.

[50] McCRACKEN, M. *et al* Assessing the FTA p. vii.

[51] *CANADA. External Affairs and International Trade* 1990 Canada - United States Free Trade Agreement: Implementation January 16. Mimeo.

2.4.4 Provincial Governments:

Provincial governments continue to be involved in providing advice to the federal government on the FTA and trade matters in general.

Implementing the FTA was scheduled to be an agenda item at the First Ministers' Conference in November, 1989; however it, like most other items, was pushed into the background by the continuing difficulties surrounding the Meech Lake Constitutional Accord.

Various aspects of the FTA have been discussed at the federal/provincial trade ministers' meetings. On-going consultative processes have been established at the officials level.

While Alberta, Ontario, and Quebec asked early in 1989 to be officially included in the subsidy negotiations, the request was coolly received by the national government[52], which prefers to maintain the consultative mechanisms used in the original FTA negotiations.

A new draft proposal from all ten provinces for participation in the negotiations was given to the Prime Minister following the Premiers' Conference in August, 1989. It too was rejected by Minister Crosbie at a federal-provincial trade ministers consultation meeting on November 27, 1989. Mr. Crosbie chose instead to have his officials draft a plan for provincial consultation which will not include a direct provincial role in solving disputes or agreeing on definitions. This draft was scheduled to be completed by February, 1990.

2.4.4.1 Provincial Barriers to Trade:

Provincial government policies also continue to be a source of international trade irritants.

One of the concerns regularly raised with Canada by the United States is the continuation of an assortment of inter-provincial barriers to trade -- as well as several specific provincial practices, especially liquor pricing -- which have an impact on the access for and competitiveness of U.S. products in Canada.

The Canadian Government also has brought these matters up for discussion with the provincial government, but progress in achieving the implementation of FTA-mandated changes has been slow.

Moves towards trade liberalization and the removal of barriers between and among the provinces also has been slow, although some progress has been made with the adoption of an inter-provincial agreement on a number of agricultural practices and on easing restrictive provincial government procurement practices.

However, the new inter-provincial agreement on procurement practices had not been ratified by any province nearly a year after it had been negotiated by their trade

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[52] "Crosbie cool to provinces joining free trade talks" *Toronto Star* April 18, 1989 page 8.

ministers[53], and only threats from New Brunswick to walk out of the September, 1989, meeting if no progress was made seemed to force the first step towards freer trade within Canada.

Following the agreement on procurement, with a commitment to develop dispute settlement procedures by April 1, 1990, federal Industry Minister Harvie Andre was prompted to say that after "a few more meetings of the kind we had today and we'll be able to announce free trade exists in Canada."[54]

Regular meetings of provincial trade ministers will continue to be held and the Minister of International Trade has consulted with each provincial minister before meetings of the Canada-United States Trade Commission.

2.4.5 Non-governmental Organizations:

As noted in the Introduction and in Section 3.2 below, the peculiar concentration of world-wide forces affecting economic and trade developments, and the fact that the implementation of the Free Trade Agreement is in its early stages, makes the attempt to isolate FTA effects very tentative. Nonetheless, given the political attention that the Agreement has drawn, and given the existence of groups dedicated to support and opposition, it is not difficult to find strong views on developments to date, supported by personal expressions of opinion as to the influence of Free Trade on job gains or losses, depending on the orientation of the authors or commentators.[55]

Opponents of the Agreement seem to be the most active in monitoring the progress of the FTA in Canada and in bringing their findings and opinions to the attention of the public.

- The **Council of Canadians** has produced a series of report cards on the effects of economic change under the FTA and says that its membership doubled in the first year after the FTA came into force.

- The **Canadian Labour Congress** (CLC) continues to do extensive research into the job-losses and economic restructuring it sees resulting from the FTA and has a very widely distributed newsletter to disseminate its findings. The CLC remains opposed to the FTA but has nominated members to sit on the ITAC, SAGITs and other government and industry groups active in the management of FTA issues.

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[53] DROHAN, M. 1989 "Provincial trade talks too slow" *Globe and Mail* Sept. 12, page B1.

[54] DROHAN, M. 1989 "Provincial Minsters tackle trade issues" *Globe and Mail* September 13, page B1.

[55] See, for example, The Pro-Canada Dossier #23, January 1, 1990, which provides several such case histories.

- The **Pro-Canada Network** continues to publish the *Pro-Canada Dossier*, but while still active, has been much less visible than during the election. It intends to become more active in 1990, with the publication in February of a study it has undertaken on the first year under free trade.

Outside the government, free trade supporters have been far less visible since the coming into force of the FTA. This may be partly the result of an inability to draw definitive positive conclusions or to demonstrate results this early, as opposed to the specific examples of job loss and restructuring that opponents are able to cite. Nevertheless, a number of "good news" lists have been compiled and made available to the government to counteract opposition claims.

- **Prudential-Bache** recently has released a study which it commissioned on the FTA.

- The **Royal Bank** was cautiously optimistic about the impact of the FTA in a special double issue of *Econoscope* which was entirely devoted to a report on the FTA[56].

- It is expected that the **C.D. Howe Institute** will release its findings on the first year sometime in February, 1990.

An earlier controversy over the tax-deductibility of contributions made to pro-FTA groups was ended when the government agreed to accept contributions made to either side as deductible if the company making the contribution indicated that this expense was made to further its legitimate business issues[57].

A number of academic institutions and independent research groups have begun to do work on the effects and impact of the FTA, but the results of their work will likely be some time coming.

Several law firms and specialized news reporting services continue to provide regular newsletters on FTA related developments.

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[56] ROYAL BANK OF CANADA. 1990 "Free Trade Agreement: One-year retrospective" *Econoscope* 13 (11-12) January 18. 24 pp.

[57] There is still some controversy remaining, as many of the companies that made contributions to the *Alliance for Job Opportunities* have refused to reveal the amount of their contributions.

2.5 THE UNITED STATES

2.5.1 Legislation and Regulation:

In the United States implementing legislation was passed by Congress well in advance of the scheduled coming into force of the FTA.

An initial draft of the implementing bill was passed unanimously in the Senate on May 18, 1988. It included two amendments introduced in the Senate, regarding plywood standards and the permissible size of lobster imports. Canada made official objections to both of them.

The final version of the bill, H.R. 5090, passed the House of Representatives by a vote of 366-40 on August 9, 1988, and received the approval of the Senate on September 19, 1988, by a vote of 83-9. It retained the provision on plywood standards to which Canada had taken exception but the amendment on lobster size had been dropped from the bill. It was signed into law by President Reagan on September 28, 1988[58].

Much of the follow-up activity called for in the legislation in relation to the monitoring and management of the deal was delayed a few months owing to the change of Administration in the United States, but is now well underway and on schedule.

Since that time the United States has appointed its new Trade Representative and has in place all the negotiators, panel rosters, and staff to fulfil its obligations under the FTA.

The agricultural working groups, select panels, and the *Subsidies and Trade Remedies Group* have been established. The *Binational Secretariat* has also been established and provided with a budget. It is expected that a permanent director soon will be named.

The U.S. legislation also provides that any additional regulatory or legislative changes needed to make the FTA operational may be introduced within the first twelve months following the coming into force of the Agreement, or within twelve months of approved changes to it.

Any such changes require public scrutiny in the United States and, unless introduced under a "fast-track" negotiating authority, can be subject to Congressional amendment. In this regard, the ITC held public hearings to consider tariff items proposed for accelerated reduction.

The U.S. legislation also requires that the United States Trade Representative (USTR), the Cabinet level official responsible for FTA management in the United States, consult with and report to the relevant Congressional Committees over a number of matters

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[58] *The United States-Canada Free-Trade Agreement Implementation Act of 1988* 102 Stat. 1851 (U.S. Code Annotated) U.S. Pub. L. No. 100-449 [H.R. 5090] Sept. 28, 1988. This is cited as H.R. 5090 in this report.

including the progress of the U.S. trade remedies working group; the selection of potential panellists; and investigations on Canadian subsidy practices taken under the provisions of an amendment introduced by Senators Baucus and Danforth[59].

In the case of the *Subsidies and Trade Remedies Working Group* called for by Article 1907 of the FTA, the USTR is required to report on the issues being considered and the strategy being utilized by U.S. negotiators[60] and to submit an annual report to Congress on its progress towards meeting its objectives[61].

2.5.2 The Omnibus Trade Bill:

The most important development in U.S. law relating to the management of international trade has been the passage of *The Omnibus Trade and Competitiveness Act of 1988*[62], which incorporates or amends 300 pieces of earlier U.S. trade law. It passed into law on August 23, 1988, four months prior to the coming into force of the FTA and its provisions apply to Canada-U.S. trade.[63]

This legislation, which was the product of four years of work by Congress, defines both how the United States will act to defend its interests and how it views the practices of other countries.

The *Omnibus Act* proposes to achieve reciprocity by using access to United States markets as leverage to extract concessions from "unfair" trading partners. It also attempts to reduce United States export controls and, through section 301, tries to force other countries to remove barriers to imports from the United States.

2.5.2.1 Section 301:

Through the *Omnibus Act*, Congress strengthened the provisions of the *Trade Act (1974)* Section 301. These changes transfer much of the authority and discretion that earlier had been granted to the President to the Office of the United States Trade Representative (U.S.T.R.).

Congress also moved to constrain the discretion exercised by the U.S.T.R. when determining who, when, and how to proceed with trade actions against those countries with trade surpluses with the United States or that maintain "unfair" barriers to trade.

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[59] See Section **2.5.3.** below

[60] H.R. 5090 Sec. 409(A)(3)(A).

[61] H.R. 5090 Sec. 409(A)(3)(B).

[62] U.S. Pub. L. No. 100-418, 102 Stat. 1107 (1988)

[63] See Section **6.2.2** - Pork Production Subsidies and **6.4** - Judicialization below.

Section 301 of the *Trade Act (1974)* had provided presidential authority to take action and enforce United States rights under the various international trade agreements and to respond to discriminatory and/or unreasonable practices by foreign governments.

This section had been used very infrequently, in part because of its discretionary nature. However, beginning in 1985, the Reagan Administration made increasing use of this authority, initiating proceedings and retaliatory actions against several U.S. trading partners, including Canada.

Notwithstanding this increased recourse to action under Section 301, Congress remained dissatisfied; it was convinced that the Administration was disposed to consider grounds unrelated to trade policy, such as diplomatic or national defense considerations, before deciding whether or not to grant relief. As well, many U.S. plaintiffs who sought relief faced international dispute settlement mechanisms with ineffectual or non-existent time limits.

2.5.2.2 Super 301:

The perceived shortcomings of previous U.S. trade laws were addressed by the changes made by the *Omnibus Trade and Competitiveness Act*. These changes include:

- the transfer of authority to the USTR noted above;
- the requirement for mandatory action in cases where another country's trade policy or practice is "unjustifiable" or burdens or restricts U.S. trade;
- the setting of deadlines for making determinations and taking actions; and
- the establishment of very wide definitions for terms such as "unfair", "unreasonable" and "discriminatory", terms which play a major role in determining the legality of actions against foreign practices [64].

The new provisions, which are known as "Super 301"[65], required the USTR to submit a report to Congress in 1989 and again in 1990, "naming" countries and identifying foreign practices that limit U.S. exports. The lists are divided into two groups:

- "priority practices" -- those which have the most significant impact on U.S. exports; and

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[64] For example, the *Omnibus Act* includes a proviso that a foreign practice which though "not necessarily in violation of or inconsistent with the international legal rights of the United States, is otherwise deemed to be unfair and inequitable" can be actionable (Sec. 301(3)(3)(A)). Also included, under Sec. 301(d)(3), are any practices which deny "fair and equitable" access to markets, corporate establishment, intellectual property rights, cartels, restrictive distribution systems, and export targeting.

[65] Sec. 310(a)(1) and Sec. 310(a)(2).

- "priority foreign countries" -- those with the most restrictive trade practices.

The USTR is required to initiate Section 301 investigations of the priority practices it identifies in each of the priority countries. Section 302 directs the USTR to undertake negotiations with the offending countries, and, if these do not lead to redress, to seek formal dispute settlement under the appropriate international agreement[66]. Failing a resolution within the strict time frame set by Super 301, the USTR is required to take retaliatory action, which can be set at a level above the determined injury. The deadline for this action is thirty days after the conclusion of any dispute settlement procedure or eighteen months after the action was initiated.

It has been suggested that these provisions reflect a diminished interest on the part of the United States in making multilateral institutions and mechanisms function successfully. For example, nothing in the GATT suggests or permits an individual country to initiate actions or undertake retaliation if its GATT privileges have been nullified or impaired, unless and except if the GATT has made the determination and authorized the penalty. While GATT has only once authorized retaliation, more and more frequently it has been able to speed determination of complaints brought before it, to the point where its average turnaround time is now shorter than the deadlines imposed by Super 301.

Several GATT determinations recently have found fault with a number of U.S. rules and practices, including Section 337 at the *Tariff Act of 1930* (intellectual property) and the U.S Oil Import Tax. It is likely that many 301 actions, particularly those under "Super 301", could be appealed successfully to the GATT. Nevertheless, the penalty imposed by these actions, and even the threat of their use, is seen by many to be sufficiently costly that "offenders" (as unilaterally defined by the United States) will take heed instead of taking GATT action, particularly since the United States has in the past been slow to accept GATT decisions finding fault with U.S. practices or legislation.

2.5.2.3 Canada and Super 301:

The first *National Trade Estimate Report on Foreign Trade Barriers*[67], released in April, 1989, identified the most significant foreign barriers to U.S. trade, including a number of Canadian practices. These included Canadian border broadcast measures, plywood standards, cable retransmission, postal rates, and patent protection.

In May, 1989, the USTR released its list of priority countries: Brazil, India, and Japan. Canada was not named; consequently, no formal action under "Super 301" is being taken against Canada. However, should Canada be named as a "priority country" in a future *National Trade Estimate Report* the Canadian practices or programmes which had been identified in the 1989 Report would become subject to immediate 301 investigation.

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[66] That is, through the GATT, or if Canada is involved, the FTA as well.

[67] UNITED STATES. USTR *National Trade Estimate Report on Foreign Trade Barriers* April 28, 1989. The report on Canadian practices takes up nine pages of this report.

While these provisions of the *Omnibus Trade and Competitiveness Act* are not aimed primarily at Canada, and the United States government has not named Canada to its first list of "Super 301" priority countries, the provisions of the *Act* can be used by individuals and companies in the United States seeking relief from competitive pressures that they attribute to Canadian practices.

This means that Canadian practices that might be construed as aid to exports or as limiting imports could be brought under increased harassment as a result of the *Omnibus Act*. On the other hand, the dispute settlement procedures of the FTA, and the continuing negotiations on subsidies, may offer Canada more protection than other U.S. trade partners, and provide for more timely resolution of disputes than does the GATT.

U.S. actions against Canada under "Super 301" are likely to be referred automatically to the dispute settlement mechanisms of the FTA. These provide for bilateral consultations and set out timetables and panel procedures that may in time prove superior to those available under the GATT. In particular, they also include Canadian representation.

2.5.3 Sec. 409(b):

As noted above, the USTR has been provided with new investigatory powers through what is known as the Baucus-Danforth amendment to H.R. 5090. Section 409(b) *Identification of Industries Facing Subsidized Imports* instructs the USTR to consider requests from "any entity, including a trade association, firm, certified or recognized union, or group of workers that is representative of a U.S. industry" that has reason to believe it will suffer from subsidized competition before bilateral rules and disciplines are developed.

A clause that extends potential investigations under this provision to any country that concludes a trade agreement with the United States was added after Canada objected to the amendment. However, the amendment clearly is aimed at Canadian subsidy practices and goes far beyond a general relief clause for American firms or industries experiencing difficulty resulting from changes brought by agreements like the FTA.

The USTR can initiate an investigation under Section 409(b), following consultations with an inter-agency advisory committee, the Congress and the President. If it proceeds, the USTR will collect data on the industry and subsidy practices in question, provide this to the complainant, and then consider taking action under Section 301.

It is important to note that whether the USTR undertakes an investigation or not, and regardless of whether the findings are positive or negative, this "shall not in any way prejudice the right of any industry to file a petition under any trade law"[68]. A number of requests for such investigations already have been made, relating to durum wheat exports from Canada, hydro-electric pricing policies in Ontario, and some mining assistance programmes. The U.S. Secretary of Agriculture has indicated that the Administration does not support the durum wheat complaint, but nevertheless, an investigation is underway.

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[68] H.R. 5090 Sec. 309(b)(5)(A).

3.0 RESTRUCTURING THE ECONOMY: GOING GLOBAL

In this section of the Report, evidence of the restructuring of parts of the Canadian economy is examined.

Adjustment in industries and national economies is a continual process. The structure of a country's industrial base and of particular industrial sectors -- and the corporate and government policies which assist or direct them -- reflect incessant change in the national and the international economic environment.

The term "globalization" -- implying the increasing integration of the world economy -- describes a particularly intense set of forces that has been responsible for reshaping industrial economies through the 1980s. Based upon a major revolution in communications and computer technology which has, in turn, led to a rapid pace of world financial integration and the shift of substantial portions of world industrial production to newly industrializing countries, this new international division of labour has prompted both the movement off-shore of all or part of the activities of many corporations and the formation of new arrangements between corporations to share the development and production of goods.

Globalizing pressures and responses have taken many forms. These include movement towards industrial co-operation, joint ventures, international consortia, technology transfer and licensing, as well as foreign direct investment (FDI), and increased trade in goods and services. As well, there has been an explosion of financial capital moving about the world in debt forms, swamping in magnitude the volume of world trade. There also has been a large increase in national and international corporate restructuring through mergers and acquisitions and the buy-back of subsidiary corporations.

Superimposed on these forces, at any point in time, are the economic responses to broad shifts in demand for goods and services and the state of macroeconomic health. All industrial economies have witnessed a steady rise in the proportion of their work forces employed in service occupations, and all have recovered slowly through the 1980s from the recession which began the decade.

Not surprisingly, this complex sea of influences has involved complex patterns of job creation and destruction. The Free Trade Agreement has to be seen, for the moment, as simply one more influence, perhaps the one of most consequence, but one that is early in its life and one whose effects are not easy, yet, to distinguish.

The section that follows wrestles with the economic and industrial evidence of these activities and tries to distinguish among global and free trade forces. Hopefully, this section will improve as time passes and the data and information on which it relies is expanded as interested groups are able to bring their analytical guns to bear.

3.1 MEASURING JOB LOSSES AND GAINS

Much of the debate leading up to the signing of the FTA focused on the probability of job creation or losses as a result, rather than on productivity or efficiency gains from competition. The Department of Finance, in the most official of forecasts, suggested there would be real income gains of 2.5 per cent and 120,000 new jobs in the first four years (1989-1992). Still another study suggested that "neither U.S. subsidiaries in Canada nor Canadian multinationals operating in the United States will experience plant closures or worker layoffs"[69]. There were both more robust predictions of gains and more dire forecasts of losses.

A good deal of the public debate over the success or failure of the FTA continues to revolve around the question of whether there are or are not any job losses that can be directly linked to the FTA. While defenders tend to appeal to over-all employment gains, and detractors to specific job losses, many would concede that it is too early to draw accurate and relevant conclusions, and that it will continue to be difficult to separate FTA effects from other economic forces.

Nonetheless there is an emerging consensus among economists that adjustment is occurring, that employment is shifting between companies, industries and countries. The critical need is to collect data to measure and evaluate those changes, whether caused by the FTA alone or by the whole gamut of forces at work in the world economy.

Until and unless a greater effort than is so far apparent is spent in data gathering and analysis, the claims and counter-claims by proponents and opponents of the FTA, as noted below, are likely only to excite cynicism in the public-at-large.

3.1.1 Losses:

From the first day following the passage of the FTA opponents have been compiling and publishing lists of job losses, corporate restructuring and plant relocations which they tie to the FTA[70].

Estimates of specific job losses made by these groups are often wide-ranging. In the summer of 1989, for instance, the estimates ranged from 23,000 cited by Mel Hurtig, to 33,000 from the Council of Canadians (CoC), to 40,000 by the Canadian Labour Congress.

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[69] RUGMAN, A. 1988 Trade Liberalization and International Investment Discussion Paper 347. Ottawa: Economic Council of Canada. p. v.

[70] The Council of Canadians published its first *Report Card* on FTA job losses two weeks before the Act came into force, the second, three weeks after.

These estimates have not generally included measures of new employment, although recent reports from the Pro-Canada Network (PCN) recognize that some new jobs have been created, but at a rate slower than previous average monthly increases.

The CLC is expected to release its findings for the FTA's first year in February, 1990, estimating a 50 per cent fall-off in new job creation in 1989 as well as approximately 70,000 specific job losses.

3.1.2 Gains:

With rare exception, FTA proponents have shied away from publicly citing specific details of job gains, relying instead on over-all job creation figures to make their case. However, during the summer of 1989, claims were made that were as wide-ranging as their opponents, going from the 100,000 new jobs cited by the Prime Minister in the House of Commons, to 156,000 cited by Statistics Canada, to the 809,000 at one time reported by the *Winnipeg Free Press*.

More recently, Canada's embassy in Washington has provided some specific examples of what it called free trade winners, identifying companies which had made new investments or increased some activities, although in at least one case cited on their list, over-all employment at the company had declined.

As well, the investment company, Prudential-Bache, has released a study which cites several examples of companies which have prospered since the FTA was signed.

A number of studies, such as those by the Economic Council of Canada and the Finance Department, which had been completed prior to the final negotiation of the FTA have been re-worked to reflect the reduced scope of the FTA in its final form, with estimates of employment gain often reduced by as much or more than 50 per cent against earlier work.

While the Government has not yet made available results of any monitoring or surveys undertaken by the Department of Industry, Science and Technology or other departments[71], at least one internal government study indicates that about 93,000 seasonally adjusted new jobs had been created in the first six months after the coming into force of the FTA. Some 25,000 FTA related job "dislocations" per year were predicted by the same government study.

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[71] See 2.4.2. Other Government Departments above. While a good deal of statistical material is collected on an on-going basis, no evidence has come to the attention of the authors of this report that government departments or agencies normally concerned with keeping track of employment, investment and corporate activity are undertaking analysis of specific free trade effects. As noted above, the government contracted a feasibility study on doing this work. See section 2.4.3.3 - Informetrica Feasibility Study.

The Government's report on the implementation of the Free Trade Agreement also steered clear of providing a number for jobs lost or created. Although Trade Minister John Crosbie cited 193,000 new jobs created in 1989, he said "these facts and figures are not directly attributable to the Free Trade Agreement -- obviously there are many other factors at work when business people make decisions"[72].

1989 employment and job-creation figures from Statistics Canada should be available in February. They are expected to show approximately 200,000 new jobs created in 1989, down from 247,000 in 1988, and 492,000 in 1987, and roughly equal to the 202,000 reported in 1986. Although job creation has clearly slowed from the previous year, because so many other factors and economic activities are also at work equating annual job creation figures or drawing a direct line to the FTA is, as noted above, a difficult task to do with any degree of accuracy.

However, the United States has also experienced a slowdown in net new job creation in 1989 and this may reflect a general trend in OECD countries to reduced employment growth as a part of the business cycle. It is therefore very difficult to assess the role of the FTA on overall employment growth, and to use those figures to assess the impact of the FTA at this time.

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[72] Minister for International Trade John Crosbie. Ottawa news conference held January 19, 1990.

3.2 CHANGES IN THE STRUCTURE OF EMPLOYMENT AND PRODUCTION

Restructuring, both nationally and internationally, may be divided into several trends and types of activity, discussed below with possibly relevant Canadian examples.

Almost all the classes and examples of restructuring make clear that forces other than the FTA are at work. This seems all the more reason for the government and others to engage in intensive data gathering and analysis if FTA effects are ever to be sharply discerned.

3.2.1 Globalization of Production:

To state that companies and economies are becoming more inter-dependent is probably only to state the obvious. However, it really is the key to understanding the pressures for and directions of the restructuring of countries and economies.

The GATT recently has reported, for instance, that global trade is growing at a rate twice that of the growth of world production. This is a resumption of a pace not known since the 1960s, and is mirrored by a proliferation of inter-corporate relationships.

3.2.1.1 The world automobile industry:

Organization charts of the automotive industry show cross-ownerships, alliances, technology-sharing arrangements and co-production agreements so complex as to be virtually indecipherable. Such arrangements are becoming more common over a wide range of industries.

In North America -- where trade in automotive products represents the major portion of all manufactured goods that cross the border -- the companies are usually differentiated between the original "big three" North American companies -- the domestic industry -- and imports.

However, the North American content of some "Japanese" cars often exceeds that of many "domestic" vehicles. Over half the 362,000 Honda Accords sold in the United States in 1989, making it the best selling car in North America, were built in Ohio with a large portion of locally sourced parts. Nissan, has announced plans to produce on the continent two out of every three vehicles it sells in North America within the next ten years. It already produces over 240,000 vehicles per year at its plant in Smyrna, Tennessee, a plant which is slated to almost double its production when the expansion already underway is completed in 1992.

Many "big three" cars, on the other hand, incorporate engines from Japan, parts from Korea and Mexico, and designs from Europe.

The North American auto parts industry is also internationalized, often through subsidiaries or independent "twin" companies which have located in Mexico's maquiladora area.

Part of the discussion at the *Select Panel on the Automotive Industry* set up under the FTA concerns raising the North American content requirements for automobiles, under the

Auto Pact, to 60 per cent. This arises from a "big three" concern that the Japanese and Korean transplants might soon be able to claim "domestic" status as local sourcing and assembly push up the North American content of their vehicles.

3.2.1.2 The pharmaceutical industry:
In the pharmaceutical industry, research and development may be done in one country; design, marketing, and packaging work in another; production in a third; with all combined for sale in an assembly plant in the destination country.

3.2.1.3 Textiles:
In the textile and apparel industry production is similarly internationalized. Cloth is often woven in one country, cut to pattern in the next, then shipped to another to be turned into apparel before being sent for sale in a fourth country.

3.2.1.4 Going Global:
These changes in the way global corporations operate have altered the market and changed competition dramatically and will continue to do so. The FTA is more a reflection of, or a response to these forces, than in any sense their instigator. Any country or company seeking to enter the global marketplace must take account of these world-wide integrative pressures. Several Canada-based companies already have begun the process of coping:

- **Northern Telecom** (Nortel) has made extensive moves to ensure that it obtains a share of the growing international market for telephone exchanges (PBXs). Already dominant in Canada and with a large share of the U.S. market, Nortel holds only 4 per cent of the total global market for its products but hopes to move up to 15 per cent over the next ten years[73].

  Nortel has established or purchased operations in a number of countries to ensure toeholds for future sales and expansion. It has acquired a large stake in STC PLC in Britain and has also opened a production facility in Verdun, France and invested heavily in an R&D centre near Paris. Unfortunately for some of the employees involved, as part of the same process the company has rationalized many of its production facilities, closing or reducing operations across the board, including large workforce reductions in Belleville, Ontario and Aylmer, Quebec and smaller layoffs in Amherst, Nova Scotia and Saint John, New Brunswick. Nortel spokespersons say that these changes are all designed to position it to take a larger share of a quickly growing but extremely competitive market, ultimately leading to increased employment and income in Canada.

- **Bombardier** has expanded its aircraft division by the acquisition of Short Brothers of Northern Ireland and its rail division by acquiring Belgium-based Constructions Ferroviaires et Métalliques SA. It hopes to use the Short Brothers acquisition to help position its regional jet, which is based on the

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[73] General Electric has stated that if it will close up an operation or divest if it cannot hold 15 per cent or more of global share for any of its core industries.

Canadair Challenger, in the European market. As well as providing an entrée for Bombardier light-rail cars into Europe through BN, Bombardier hopes to be able to transfer the Train à Grande Vitesse (TGV) technology of BN and GEC-Alsthom for use in the North American passenger rail market. Bombardier is also attempting to reach agreement with Embraer, the Brazilian aircraft company, for the licensing and production of the CL-215 water bomber. Spokespersons at both Bombardier and Short Brothers have indicated that their combined R&D efforts will improve the chances of success for both companies.

3.2.2 Restructuring:

Corporate restructuring -- beyond simple expansions and contractions related to changing demand -- takes many forms, including mergers and acquisitions, consolidations, subsidiary buy-backs, and the relocation of existing plants.

The FTA may play a role, through a wide range of its provisions as well as its over-all intent, in creating changes to the environment in which these business decisions are made.

3.2.2.1 Mergers and Acquisitions:

The source of many current employment losses can be found in the mergers and acquisitions activity (M&A) taking place in Canada. It is reported that the total value of mergers and acquisitions in Canada in the first four months of 1989 exceeded the total value of similar transactions in 1988, and it is expected that the final 1989 figures will show a phenomenal amount of activity, exceeding $12 billion.

However, this phenomenon is neither new nor limited to Canada. M&A activity has been rising world-wide. While the 1989 merger "dance" of Time, Warner Communications, and Paramount in the United States and the 1988 merger of Kraft and General Foods may dwarf the many other huge takeovers on Wall Street, they are but two of hundreds of such deals.

In the United Kingdom, as well, M&A activity has increased significantly. Seven of the UKs ten largest leveraged buy-outs (LBOs) of all time occurred within the past two years, ranging upwards from 450 million pounds sterling to the largest deal which exceeded 2100 million pounds. Only five years ago the largest LBO ever in the UK had been valued at 310 million pounds.

The reasons for this increased M&A are undoubtedly complex. They include: national and international rationalizations of many kinds; the existence of under-valued assets and of large cash pools; and the spread in the use of "junk bonds" and high-leveraging. The promise of national treatment rules under the FTA may have made Canadian acquisitions particularly attractive takeover targets. But more fundamentally, corporate attempts to grow through restructuring, in order to attain the scale required for efficient production, financing, global marketing and R&D, is a root cause of increased M&A activity.

- The merger of **Molson** and **Carling** is one example of an attempt to secure the benefits of scale. By eliminating nearly half their breweries and consolidating distribution the new company will be able to compete more effectively in the Canadian market and, should the terms of the FTA be expanded to encompass the brewing industry, in the United States as well[74].

- The **Imperial/Texaco** and the **PWA/Wardair** takeovers are both industry consolidations that were underway prior to the FTA. While job losses in each of these mergers are real, they are a part of on-going generalized corporate restructuring, and free trade between Canada and the United States is only one of several factors which has created the business environment driving these decisions.

The FTA has played a role in other growth-oriented restructuring:

- **Consumers Packaging** of Montreal, already the largest Canadian producer of glass containers, acquired the Domglas division of CB Pak in 1989, moving it into the number three spot in North America, although it presently sells only 5 per cent of its production in the United States. However, the acquisition doubled its number of plants from five to ten. To reduce over-capacity Consumers Packaging closed two plants, one in Montreal and one in Redcliff, Alberta. The company has stated that the resulting 15 per cent cut in its workforce is all it needs to become more competitive and has asked that the reduction of the 11.4 per cent tariff imposed on its U.S. competitors be accelerated so that it can expand its business in the United States.

- **Black and Decker Canada Inc.**, as part of its worldwide consolidation of newly acquired Emhart into its existing operations, is closing two of its three Canadian plants, in Montreal, Quebec, and Trenton, Ontario, moving about 75 of the 250 jobs to its remaining plant in Brockville, Ontario.

Other companies have undertaken expansion, taken on partners, or acquired new subsidiaries since the FTA. Some have located a good deal of the new operations and employment in the United States.

- **CCL Industries**, Canada's largest maker of cans, expanded into the United States in 1989 by acquiring several U.S. companies in the packaging and labelling industry. Later in the year, CCL traded its wholly-owned subsidiary, Continental Can, and $110 million in debt to U.S.-based Crown Cork and Seal for an 8.8 per cent stake in Crown Cork and $120 million cash, stating that selling the company to a world-scale manufacturer was necessary to ensure growth opportunities for the Canadian company.

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[74] Competing directly with U.S. breweries would likely entail more closures and consolidations in Canada, and would not be possible without the removal of barriers to inter-provincial trade.

- **Domtex** has sought a U.S. partner for its Caldwell towels division, merging it with C.S. Brooks, and has set up a joint-venture with Citicorp of New York to purchase the commercial textile division of Uniroyal-Goodrich, which manufactures tire cords, reinforcing its Canadian operations.

- **Stelco** has acquired an interest in a cold finished bar steel mill in Illinois.

- **Artopex**, a Quebec-based furniture company, has announced plans for a new plant in Albany, New York.

In these latter two cases the companies hope that they will be able to export component parts and/or increase sales of Canadian-made products through increased presence in the United States.

- **Quantified Signal Imaging** of Toronto, which develops and builds electro-diagnostic medical equipment, has tackled the U.S. market on its own by establishing a U.S. subsidiary to market its products there, but has chosen to enter Japan and Europe through partnerships with Mitsui and ESAOTE Biomedica.

- **Husky Injection Moulding**, a leading-edge manufacturer of moulding machines and dies used by the containers and housewares industry, has recently sold Japanese construction equipment giant Komatsu a 26 per cent stake, which will likely grow to 50 per cent. Komatsu wanted access to Husky Injection Moulding's technology for large scale moulding machines, and will offer its technology in other moulding equipment in exchange. The backing by the much larger Japanese company should also provide Husky with needed resources and access to increased R&D funding.

3.2.2.2 Consolidations:

Numerous examples can be cited of job losses and investment shifts which are related to corporate responses to restructuring pressures from competition. Some of that competition may have arisen from the FTA, but measuring which portion of such losses can or should be attributable to the FTA is a difficult task. Conversely, it cannot be definitively stated that the FTA has played no role in these changes. Similarly, statements that plant closures or job losses would have been greater without the FTA to guarantee markets can be neither confirmed nor rejected[75].

A number of major corporations have reduced employment in global restructuring, some with major job-losses in Canada.

- **Unisys** will close part of its Montreal plant, putting 230 of its 3,000 Canadian employees out of work as a part of a global reduction of 8,000 workers.

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[75] For example, one steel company, **Ivaco**, has stated that it might have moved all of its operations to the United States, in addition to the 200 jobs already moved, if the FTA had not been passed.

Unisys will lay-off or retire approximately 6,000 employees in the United States.

- **Campbell Soup Company**, because of what they call a "mature soup market", closed four U.S. plants and one in Portage la Prairie, Manitoba, laying off 2,800 and 168 employees, respectively.

- **Cheesborough-Ponds (Canada)**, a subsidiary of Unilever, will close one Canadian plant, laying off 150 people in Concord, Ontario, as it moves to consolidate its recently acquired Fabergé product line into existing production facilities.

- **Kodak (Canada)**, the only manufacturer of photographic film in Canada, has indicated that it does not expect any lay-offs among its 2,300 Canadian employees, even though its parent corporation expects to cut 4,500 workers in the U.S..

- **Owens-Corning Fiberglass** (Ohio based), as part of an industry consolidation resulting from a shrinking market for insulation products, purchased the 50 per cent of **Fiberglass Canada** it did not already own from another U.S. company, PPG Industries, and continued to down-size Fiberglass Canada by cutting 371 jobs in Sarnia, Guelph, and Toronto. Owens-Corning has cut its own work-force by 25 per cent in the past three years, and Fiberglass Canada had already laid-off 100 employees in Mission, B.C., transferring the work done there to a U.S. plant.

3.2.2.3 Subsidiary Buy-backs:

One of the principal goals of a national policy of high tariffs is to encourage the establishment of subsidiary corporations inside the tariff boundary in order to create employment. In an attempt to maintain national control[76] governments often require that a portion of the shares and directorships be held by nationals. Canada, of course, has followed such policies to greater or lesser degree since Confederation through such programmes as the National Policy of 1879 and, more recently, the Foreign Investment Review Agency and the National Energy Programme.

However, the need or incentive to establish Canadian subsidiaries in many sectors has been decreased by steady tariff reductions negotiated under the GATT. Further tariff reductions under the FTA and the extension of national treatment to new U.S. investment, have combined with the changed role of Investment Canada, to all but eliminate the benefit to be derived from separate Canadian subsidiaries for U.S. companies.

General Electric (GE), in 1989, began the process of buying out the 8 per cent of GE Canada shares held by the public. GE believes that public shares in a subsidiary prevents this subsidiary from being fully integrated into the multinational GE organization. Once

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[76] Discussed below in 3.3 National Control.

fully privatized, it is expected that GE Canada, which has supplied the Canadian market with a wide range of products, will cease to be a distinct unit, and will concentrate on producing a narrower range of GE products for the global market, or on the production of components for use by other GE units.

GE has reorganized its worldwide network along these lines already, integrating its foreign operations into 14 core operations, making large divestitures and investments and numerous strategic alliances along the way. At the same time it has reduced its workforce by 20 per cent, to about 400,000. GE has about 10,000 employees in Canada. There is some fear that with privatization and incorporation into the GE empire, GE Canada will lose much of the autonomy it has enjoyed, and that R&D activity and management decisions will move out of Canada to the international headquarters. This, and other recent privatizations of Canadian subsidiaries, has renewed discussions on many corporate boards as to the level of autonomy they can expect to be given by their international parents.

Although this process of subsidiary buy-back, or "privatization", was in many cases underway prior to the coming into force of the FTA -- including the purchase of **Nabisco Brands** by RJR Nabisco last year, and of **Westinghouse Canada** by Westinghouse U.S. in 1987 -- brokerage houses have indicated that the FTA has increased pressure to take out minority shareholders of Canadian subsidiaries.

A large number of other subsidiary corporations have been the subject of privatization attempts or, based on stock exchange or Bay Street activity, are believed to be targeted by their parent companies to go private. These companies, with the parent company shown in brackets, include:

> **Ford Canada (Ford); Goodyear Canada (Goodyear); Budd Canada (Budd); Du Pont Canada (Du Pont); Celanese Canada (Hoechst); Corby Distilleries (Allied-Lyons); Corporate Foods (Maple Leaf Mills); Union Carbide Canada (Union Carbide); Hayes-Dana (Dana Corp); Kelsey-Hayes (Kelsey-Hayes); Hawker-Siddley (Hawker Siddley); Phillips Cables (BICC); Scott Paper (Scott Paper); Xerox Canada (Xerox); and Teledyne Canada (Teledyne).**

3.2.2.4 Relocations:

Often it has been suggested that foreign direct investment attracted by tariff barriers will leave once these barriers are removed, and that many multinationals therefore will abandon Canada. However, evidence suggests that for the largest multinationals, continental rationalization is already nearly complete, particularly in the automotive industry, and that little net job loss or altered production patterns will result from the tariff removals of the FTA[77].

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[77] See, for example, RUGMAN, A. 1988 Trade Liberalization and International Investment Discussion Paper 347. Ottawa: Economic Council of Canada, and MCFETRIDGE, D.G. 1989 Les entreprises multinationales et la libéralisation des échanges Ottawa: Economic Council of Canada.

However, restructuring has led to a good deal of production and employment relocation to production zones outside Canada and the United States by many large companies. These zones are discussed in Section 3.4 - Export Promotion Zones, below.

There are, in addition, some examples of U.S. companies supplying the Canadian market from the United States and closing Canadian subsidiaries:

- **Outboard Marine Corporation** and **Toro** now intend to serve the Canadian market for small engines from their U.S. plants, closing operations in Peterborough, Ontario and Steinbach, Manitoba, respectively.

- **Gerber**, which provides nearly one third of Canada's baby food, is closing its Canadian food processing operations and will serve Canada from its U.S. plants.

Some of the largest multinationals have chosen to serve the entire North American market for certain of their products from single production centres, and the removal of tariff barriers has allowed some of these to be located in Canada.

- **Xerox** will produce all the toner for its Canada and United States copier operations in an expanded operation in Oakville, Ontario.[78]

- **Proctor and Gamble** has announced that its Belleville, Ontario plant has been chosen as the North American production centre for one of its major products.

Some companies have relocated as part of corporate restructuring to take advantage of lower wages or other regulatory benefits provided by some U.S. states.

- **Bendix Safety Restraints** has moved 400 jobs from Collingwood to Alabama and to Mexico.

Declining markets also can cause restructuring that may benefit larger U.S. operations over smaller Canadian branch plants of the same company.

- Some cases have been cited above in **Section 3.2.2.1** and **3.2.2.2.**

- The **Parke-Davis** capsule operation has been moved by Warner-Lambert from Brockville, Ontario where it employed 35 people, to South Carolina, where plant capacity can easily handle Canadian needs.

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[78] The improved toner and production process to be used in the plant were both developed by Xerox Canada in Canada.

- **Midas Muffler** has decided to serve a declining market for replacement mufflers from its more modern and underutilized plant in Hartford, Connecticut, closing its Scarborough plant.

- **Glidden (Canada)** will close two of its four Canadian plants, serving the Canadian market with excess capacity in U.S. plants.

At least one study completed by the Department of Industry, Science and Technology suggested that tariff removals and increased foreign competition in the electrical products industry might pose a challenge to Canadian manufacturers. Two recent examples seem to bear out this fear.

- **Square D**, an international electrical components manufacturer, has announced that it will consolidate production of two Canadian plants at Edmunston, N.B. and Port Colborne, Ontario into existing U.S. plants where production costs are lower due to higher volumes. The company has denied that FTA changes prompted its move.

- **GE Canada** has announced the closure of a portion of its Canadian light-bulb operations, in Montreal, Quebec. About 65 per cent of the production will be transferred to Oakville, Ontario, with the balance to the United States.

Relocations are not restricted to foreign-owned companies, however. Some Canadian companies have expanded operations, but done so by increasing employment in the United States while simultaneously reducing employee numbers in Canada.

- **K.T. Industries** of Winnipeg has laid off 20 of its 130 Canadian employees despite recent expansion into the United States.

- **Ivaco** is closing one of its Canadian steel plants, offering jobs in the United States to about 150 of its 350 laid-off employees.

The governments of Ohio, Illinois, Michigan and North Carolina have recently announced plans to open economic development offices in Toronto, joining New York which has had an office there for at least fifteen years. Pennsylvania and Indiana are considering opening offices as well, and the eight Great Lakes states are expected to open a joint-office soon. These offices attempt to persuade more Canadian companies to move to their states[79].

Relocations have not all been a one-way exodus from Canada, however.

- The **Electro-Motive Division** of General Motors, which manufactures diesel locomotives, has nearly completed the transfer of its operations from an older and much larger plant in McCook, Illinois to London, Ontario. McCook has been reduced to one engine a week, from a peak of over five per day and lost

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[79] Canadian provinces have maintained such offices in various U.S. states since at least 1958, and total about two dozen in number.

over 8,000 employees. The London plant has expanded from one engine a week to two per day, and increased its workforce by 500 to 2,000.

- The Chicago, Illinois production line of **FM Foods** will be closed and moved to the company's main facility in Newmarket, Ontario.

- **Bachan Aerospace** closed its Detroit plant and moved its full production to Windsor, Ontario.

3.2.2.5 New Investment Decisions:
Critics of the FTA have suggested that even if many existing plants and operations may not be threatened by tariff removal, new investment and locational decisions may favour the United States over Canada. Again examples can be found that go in both directions.

- **Whirlpool**, in deciding to phase out an obsolete washing machine line produced by its Canadian subsidiary, **Inglis**, did not choose to develop and manufacture a new version in Canada, but decided to replace it with a new machine designed and built in the United States, closing one of its plants in Canada and laying off 650 workers at three others.

- On the other hand, **Camco**, General Electric's Canadian appliance maker, is investing in an updated facility in Montreal to make dryers and dishwashers for the entire North American market, with at least 30 per cent of production destined for the United States.

- To meet its commitment to serve the North American toner market, noted above, **Xerox** will invest about $17 million in new facilities in Newmarket, Ontario.

- Citing lower tariff barriers, **Dow** announced it would invest $800 million in a new ethylene-based petrochemical plant in Fort Saskatchewan.

Other examples can be found in the automotive industry. While the auto industry has had free trade for 25 years, and the FTA probably plays only a small role, if any, in recent changes in the industry, increased competition from imports and excess capacity are leading to a massive re-organization of the North American industry and what happens may provide a picture of what to expect in other soon-to-be-rationalized sectors of the economy. It is expected that at least twelve "big three" plants are likely to close and questions have been raised as to which side of the border those closures will be on and where new investment will be made.

- **Ford** is closing an engine plant in Windsor which had been kept open to meet excess demand from a U.S. plant. At the same time, however, Ford will be opening a new plant to produce a similar product elsewhere in the United States. Ford has also failed to indicate the future of its Oakville assembly plant, even though the cars it produces are slated to be phased out in two years.

- **General Motors** has announced the move of van production from Scarborough, Ontario to Flint, Michigan in 1991, and has not yet designated a replacement vehicle, but has announced that its van plant in Lordston, Ohio will also be closed.

- **Freightliner,** a truck manufacturer, has chosen St. Thomas, Ontario, over a potential U.S. site to build its new plant, where it will eventually employ about 1,200.

It is as yet unclear whether the political pressure brought by a declining auto sector, combined with the current imbalance between production and consumption across the Canada-United States border[80] will reverse the recent trend towards an increased production share for Canada, with U.S. automakers favouring their "home" country over Canada[81].

Even though there is evidence to suggest that some companies still favour home country locations for investment, the global trend is towards internationalization, to the location of parts of a company where organizational interests, input costs and market conditions -- including wage rates, health and safety rules, taxation and regulatory regimes -- are most favourable[82].

U.S. business investment abroad is also at an all time high, approaching 17 per cent of total business assets. It is important to note that fully 40 per cent of that new investment was not in traditional direct or portfolio investment, but in joint ventures.

3.2.3 Service Economy:

All industrial countries have experienced a steady shift towards services as the principal source of employment. In addition, services have represented a steadily rising proportion of international trade.

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[80] Canada assembles about 800,000 more cars per year than it consumes, the balance exported to the United States. The levels of employment also reflect a similar imbalance, but is reduced significantly once full account is made for parts production.

[81] There is also debate over whether transplants will locate in Canada or in the United States. While there has been increasing resistance in the United States to foreign investment, leading to speculation that the transplants might consider Canada first, new plants and new jobs are welcomed much more positively than are takeovers of existing operations.

[82] In fact, several major U.S. companies are reported to have moved all their production outside of the United States. For example, even though U.S.-owned and controlled and among the world's largest toy manufacturers, Mattel makes virtually no toys in the United States.

The service sector includes financial services, construction, transportation and telecommunications, consulting, education and health care, retailing and tourism. Nearly 70 per cent of output in Canada is derived from the service sector, and nine out of ten new jobs have recently been in services.

The FTA is the first international trade agreement to attempt to establish some rules in this area.

Other than some rumoured developments, there is as yet little to report in the financial services sector. U.S. interests are thought to be considering the purchase of Canada Trust, although this may be subject to new ownership limits imposed on trust companies by upcoming Canadian legislation. Indeed, the entire area of financial services, both the evolution of institutions in Canada and their federal and provincial regulation, as well as their "globalization", is an area for continuous monitoring.

3.3 NATIONAL CONTROL

Reducing barriers to foreign investment in Canada has been a goal of the current government since its election in 1984[83]. The FTA extended the principle of national treatment to U.S. investment in Canada.

Takeovers and takeover attempts on Canadian companies such as **Lumonics, de Havilland, Falconbridge,** and **Connaught BioSciences** recently have rekindled fears that Canada's economy in general, and the leading edge high technology firms and industries in particular, may fall under foreign control[84].

These and other takeovers and acquisitions have revived public discussion of the need for, and virtues of, an "industrial" or "national" policy and the possible need to "protect" strategic industries.

Though not directly related to the FTA, the recent debate over the sale of Connaught to Institut Mérieux of France centred over whether research and development jobs will remain in Canada and whether spillover employment effects will accrue to Canada or to France.

Critics of the takeover suggest that a foreign owner for **Connaught BioSciences**[85] will devote a lower proportion of its R&D expenditures to work in Canada and that any benefits from new discoveries will belong to the parent. Mérieux had proposed a plan to continue R&D spending in Canada, combining projects and efforts with its home country operations.

A second bidder for Connaught, Ciba-Geigy of Switzerland, had also proposed combining efforts of Connaught with one of its U.S. partners, Chiron, to move into bio-technology research, at the leading edge of pharmaceutical research today[86].

After its initial proposal was rejected by Investment Canada, Mérieux pledged that it would spend an additional $160 million on R&D over five years at a new bio-technology centre

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[83] This matter is discussed further in Section **4.2.5.** below.

[84] While Statistics Canada has not yet made recent figures on levels of foreign ownership in Canada available, it is estimated that foreign ownership of non-financial corporations may climb to 35 per cent this year, with foreign control in all sectors totalling about 25 per cent.

[85] Connaught is named after the labs where insulin was discovered, and which was operated by the University of Toronto prior to being sold to the Canada Development Corporation in 1972. Connaught BioSciences was formed when CDC was wound up and its holdings privatized. Mérieux, which is a leading serum manufacturer, is controlled by Rhône-Poulenc, a French state-owned company.

[86] Ciba-Geigy spends nearly ten per cent of its total revenues of $14 billion on research and development, as does its Canadian subsidiary on revenues of $385 million.

to be built in Willowdale, Ontario, and appoint six Canadians to the ten-member board of the new company and make Mérieux shares available to Canadians[87].

Though in a sense **Connaught** became the case which raised generic issues, it is also important to note that many Canadian companies -- such as Campeau, Olympia and York, Rogers Cablesystems, BCE, and Bombardier -- are active in foreign takeovers as well, and it is difficult to demand a protected market at home while Canadian companies are making strategic acquisitions abroad.

Some U.S. legislators have found the United States the recipient of too much foreign investment and have introduced legislation to screen and limit foreign takeovers of U.S. industry. While the Administration has resisted these incipient attempts at creating a U.S. version of Canada's former Foreign Investment Review Agency (FIRA), major foreign purchases in the United States, coupled with the relocation of U.S. production to third countries will surely increase pressure for action.

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[87] The government eventually approved both bids and Connaught shareholders accepted the Mérieux offer.

3.4 EXPORT PROMOTION ZONES

A large number of countries in various parts of the world and at various levels of development have resorted to what are known as export promotion zones, or export platforms, to improve their competitiveness and share of world production and trade.

These zones range from simple free-trade or customs-free ports to manufacturing or service districts with regulations different from, or employment standards lower than, those in place elsewhere in the country, to world financial centres where domestic regulation does not apply.

3.4.1 Mexican Maquiladora:

The case most often cited with reference to the FTA is the Mexican "maquiladora"[88] area.

The maquiladora was established twenty-five years ago, following the termination of the U.S. bracero programme, which had permitted Mexicans to enter the United States to work. Mexico decreed that foreign ownership would be permitted in a 28 kilometre wide strip along the U.S. border on the condition that any goods manufactured there be immediately exported. This zone was expanded fifteen years ago to include all of Mexico, but the majority of companies still locate along the border, primarily in Tijuana, Nogales, Ciudad Juarez, Reynosa, and Matamoros.

About 500,000 Mexicans are currently employed by enterprises established under the maquiladora provisions. While an average salary for these employees is difficult to calculate given variations in charges for transportation and meals, approximately Cdn$0.60 per hour is generally paid for assembly work. Although this wage attracts a large number of Mexican workers because it is relatively high, and unemployment is very high, it is dramatically lower than Canadian or U.S. levels.

The devaluation of the peso in 1982 speeded up the establishment of maquiladora plants; between 1,800 and 2,000 U.S., Canadian and Japanese companies now have factories there. Some of these were operations that had previously been located in other Third World countries and which were relocated to Mexico to be closer to U.S.-based final assembly plants and supervisors. Among them can be found:

- each of the "big three" automakers and many affiliated "twin" parts plants;
- the major electronics manufacturers, including **Northern Electric** which has a plant in Matamoros; and
- the **RCA** division of GE, one of the first companies to open a maquiladora plant, and now employing about 5,000 persons in Mexico.

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[88] One of the several possible "translations" for maquiladora is "grist mill", another is "sweat-shop".

The maquiladora plants provide Mexico's second highest source of foreign currencies after oil revenues, ahead even of tourism.

It has been estimated that fully 60 per cent or more of all inputs used in the maquiladora originate in the United States. These inputs are not dutiable when returned to the United States. Many maquiladora goods also benefit from the U.S. Generalized System of Preferences (GSP), which provides lower or zero tariffs for goods from designated developing countries. In many cases, the only duty paid is on the labour content of assembled products, which, due to low wage rates and no benefit costs, seldom exceeds 15 per cent of the value of the goods.

3.4.2 Canadian Maquiladora Operations:

The existence of the maquiladora regime was widely publicized in Canada when, in late 1988, the equipment of a **Fleck Manufacturing** plant in London, Ontario was transported to **Sistemas y Conexiones** in Nogales, putting the 200 employees in London out of work. The Canadian employees had been making between $6.65 and $7.04 and were on strike demanding higher pay.

With respect to the impact of the FTA on this move, it is important to note that Mr. Fleck has stated that he had been planning this move for some time and was going to go ahead whatever the outcome of the FTA negotiations.

At least two other companies have experienced employment losses resulting from the relocation of work, contracts or operations to Mexico.

- Sixty-five employees of **Bovie Manufacturing** in Lindsay, Ontario were laid off following the transfer of a contract with Kimberley-Clark to supply lab coats. They had been producing the coats at a unit cost of about $0.60; the coats are now to be made in Mexico for approximately $0.04. The new Kimberley-Clark supplier operates what is known as a "twin" operation. The disposable material for the lab coats is cut from pattern in Tuscon, Arizona, with the parts then shipped across the border to be sewn together. When the finished coats are returned to the United States, duty is paid on only the labour content of the value-added. However, if these coats were shipped to Canada, they would be subject to Canadian duty on the full-value.

- The **Bendix Safety Restraints** division of Allied Signal has laid off 400 employees in Collingwood and transferred the work to Mexico, although a company spokesman indicated that the transfer had nothing to do with the FTA, but rather "[was] strictly economic." Bendix will continue to make seat-belts for the Canadian market in Collingwood, but its export business (parts destined for the United States) has moved to Mexico.

Other Canadian companies with maquiladora operations include: **Dicon Systems, Custom Trim,** and **Ideal Equipment.**

It has been reported that at least one company has been formed to aid other companies wishing to relocate entirely outside of Canada. **Bottom Line Technologies** advertises that it advises on what it calls "the highly skilled, low-cost labour reservoir" of Mexico and promises to oversee "the secret transfer of entire plant operations to Mexico".

3.4.3 Rules of Origin:

Since maquiladora goods enter the United States effectively tariff free, there has been concern that goods produced in the maquiladora will be able to enter Canada duty free.

Recent directives from the U.S. Commerce Department make clear that the United States intends not to grant U.S. status to goods which are further processed in a third country before being shipped to their final destination. It says:

> in particular, goods produced by either U.S.- or Canadian-owned maquiladora operations in Mexico or other countries do not qualify, regardless of the value of the U.S. and/or Canadian content.[89]

However, the same directive describes several situations in which goods that are returned to the United States for further processing or incorporation into other products might be deemed of U.S. national origin and accordingly be able to enter Canada duty free under the FTA.

Under Article 3 of the FTA, acquiring or reacquiring domestic origin can occur in one of three ways:

- accessories, spare parts, or tools that are delivered as standard equipment with any equipment, machinery, apparatus or vehicle are deemed to be of the same national origin;
- goods which are materially transformed in the United States or Canada can qualify. However, the change of tariff classification must not have been devised to circumvent the rules, such as simply diluting, finishing, packaging or combining goods;
- some goods must also contain at least 50 per cent (and in some cases, 70 per cent) value-added in Canada or the United States to qualify.

Under these rules, it may be possible for component parts built or assembled in Mexico to be returned to the United States, and transformed sufficiently to change their classification and be deemed of domestic origin if subsequently exported to Canada from the United States.

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[89] UNITED STATES *Department of Commerce* 1989 Guide to Exporting Procedures page 11.

The problem of determining the domestic content of goods entering Canada from Mexico via the United States existed prior to the negotiation of the FTA, but there have been fears that lower tariff barriers between Canada and the United States will exacerbate the difficulties. Uncertainty in this area cannot be dispelled until there has been enough actual experience with the operation and use of rules of origin procedures and certificates to determine if there are ways in which goods produced in Maquilatora operations can be imported through the United States into Canada duty free. A determined effort will be made to keep this situation under surveillance and to report the evidence as it is collected.

4.0 RESPONSE & INITIATIVE

As frequently noted in this Report, the 1980s have been a period of intense industrial adjustment and restructuring throughout the world. The Free Trade Agreement adds a particular source of pressure, challenge and opportunity to the forces playing on Canada. Just as it is difficult to separate the reaction of economic actors in Canada to the FTA from their reaction to world-wide forces more generally, so is it difficult to characterize the response of policy makers to adjustment pressures as solely, or even primarily, FTA inspired.

This section, therefore, carries out a general survey of "response and initiative" since the inception of the FTA -- without trying to conclude if the FTA was the particular cause or not -- primarily focused on the federal government but addressing the reactions of other levels of government, the private sector and various interest groups in subsequent sub-sections.

The FTA was and is a federal government initiative -- part of the government's attempt to support a competitive economy -- and how it encourages and facilitates adjustment, and ameliorates its costs, is fully a part of the FTA package.

4.1 THE CANADIAN GOVERNMENT

Together with the presumed benefits of free trade, the process of adjusting to new competition -- restructuring (as discussed in Section 3.0) -- generally brings a number of specific negative effects that many believe the federal government should play a primary role in ameliorating. This has principally been done through the provision of social services such as unemployment insurance.

As important as providing social safety nets is, the federal government can also play a major role, often with the provinces, in the provision of fundamental public goods that foster and support adjustment: communication policies; support of education, training and retraining; labour mobility policies more generally; primary research and policies of assistance and encouragement to commercial R&D necessary to keep Canadian industry at the forefront of the new competitive environment; and support to local levels of government in providing a whole panoply of policies of assistance to industrial location and development. There is, of course, a widely divergent range of opinion over how great a role the government should play in each of these matters.

4.1.1 Employment Adjustment Programmes:

As an economy responds to restructuring pressures, the skills and training of displaced workers may not be adequate or relevant to the new jobs created. The government promised that it would aid in this transition, which is a natural and expected part of adjustment to an expanded market, by providing new and enhanced employment adjustment programmes for those experiencing dislocations as a result of the FTA.

Over the course of the free trade negotiations and during the 1988 election campaign the government indicated on numerous occasions that it would "provide generously for massive adjustment" (if required) and that it would "create the finest programmes that exist anywhere".

To assess what was required to meet this commitment to employment adjustment, the government appointed a select panel, the Advisory Council on Adjustment, to examine and recommend improvements to existing programmes and to make suggestions for new ones. The Council's report, *Adjusting to Win*, was released in March, 1989.

Rather than concentrating on adjustment for individuals, the report made recommendations to improve structural adjustment mechanisms more generally[90].

The *Toronto Star*, in an article entitled, "For the new jobless, it's the same old story", suggests that this approach more often serves the needs of industry and not "those who are being adjusted -- the workers"[91]. The Council's proposals did not meet the expectations of many for new programmes which would provide direct benefits to displaced workers.

At the same time, the fact that the amount of money devoted by the national government to existing programmes, such as Labour Adjustment Benefits and the Program for Older Worker Adjustment, has not kept pace with inflation, has led many to label the current programmes as inadequate and in need of more improvement than the Advisory Council thought necessary or the government has proposed[92].

After accepting the premise that much of the pressure for industrial restructuring in Canada comes from a rapidly changing world environment, and not specifically from the FTA, the Advisory Council moved on to suggest that adjustment programmes must be universal in order that all who are dislocated receive equal assistance.

The Council therefore decided against offering specific programmes for FTA-displaced workers. Instead, it adopted the view previously set forth by the Economic Council of

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[90] A basic definition of the term structural adjustment is the movement and reorganization of economic resources, within and between firms and industries in order to take advantage of emerging areas of comparative advantage and in response to structural changes in national and international economic systems. Recent examples of such changes range from rapid shifts in the relative price of oil to increasing international competitiveness and export orientation of the newly industrializing countries (NICs). Not only is this a broad definition in terms of the sources of structural change contemplated, but it also encompasses the allocative role of both government and market mechanisms. See SALEMBIER, G.E., 1985. Negotiating Structural Adjustment Internationally: Challenges for National Trade Policy, International Economics Program Discussion Paper 8504. Ottawa: IRPP, page 1.

[91] April 5, 1989.

[92] See Section 5.3.2.1 - Unemployment Insurance Reform, below.

Canada that the effects on particular workers or companies from implementing the FTA could not be separated from other global effects or from industry- or company-specific factors.

The Council recommended further that the emphasis of Canada's employment "safety net" be changed so that the system behaves more like a "trampoline", helping workers get back to work, primarily by improving skills training. To back up this suggestion the Council pointed to the high proportion of Labour Market expenditure that Sweden allocates to training, and recommended that Canada aim for the same mix. However, it ignored Sweden's commitment to full employment and its success in keeping its unemployment rate in the 2 per cent range. Not only do the unemployed in Sweden receive individual benefits at twice the rate of their Canadian counterparts, they are also offered four times the total retraining assistance. Simply altering the mix of the Canadian system is not, therefore, likely to provide the same results as in Sweden.

The *Report* does recognize the importance of Canada's UI "safety net", and suggests that the any additional programmes, and the increased competitive pressures the FTA may present to existing ones, will require the commitment of new resources to both broaden and strengthen the support provided. Instead, the changes proposed in Bill C-21 simply transfer monies within the system. Bill C-21 attempts to meet one of the Council's recommendations for an increase in the amounts available for training and retraining by reducing individual support levels.

Some critics of the FTA have suggested that the Council and the Government may both have sought to avoid proposals for specific adjustment programmes from a fear of United States complaint rather than an inability to identify more than a very few industries that might be affected. Such programmes would, of course, be subject to U.S. countervail even in the absence of the FTA.

However, trade agreements such as the GATT have generally provided for temporary protection for industries or workers threatened by new trade concessions or by temporary disequilibria in trade balances. As well, governments can have recourse to necessary adjustment assistance during those transitional periods without undue fear of retaliation. The FTA does not provide an exemption from existing countervail laws for adjustment programmes, even if specifically designed to ameliorate FTA dislocations, relying instead on the premise that programmes for structural adjustment will be "general" in nature, and therefore not subject to countervail.

International trade organizations such as the GATT have never reached a firm understanding of what constitutes a subsidy[93] and U.S. trade courts and commissions have produced varying rulings as to what constitutes a countervailable subsidy. While the test for a negative finding has often been the "general availability" of a programme,

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[93] See Section 2.3.2 Subsidy and Trade Remedies Working Group, above.

interpretations by U.S. trade courts as to what constitutes "general" have been widely divergent[94].

4.1.2 Training and Education:

A key characteristic of the labour market in the 1980s has been the growing demand for well-educated and highly-skilled workers. This trend reflects changes in the occupational mix of employment towards managerial and professional jobs, which require higher levels of education and skill, as well as increases in the skill content and educational requirements of most occupations.

Thus, education and training are becoming increasingly important, both to ensure full utilization of the labour force and to take advantage of the emerging opportunities open to Canadian companies. Mr. Jean de Grandpré told the Senate Foreign Affairs Committee in December, 1988 that, "there will be a shortage of certain skills in this country in the very near future, especially if universities continue to be underfunded"[95].

Even though these trends are clear and, as well, are commonly agreed upon by government, industry and educational authorities, the supply of well-qualified workers in certain occupations has not been keeping pace with demand. The strongest evidence of substantial and growing mismatch between available and required skills is the growing number of job vacancies that go unfilled. In fact, according to Statistics Canada, 14 per cent of manufacturing firms reported their production activities were impeded by a lack of skilled labour[96].

Another study, by the Canadian Federation of Independent Business in early 1988, found 43 per cent of small businesses citing shortages of qualified labour as a major problem.

The Advisory Council on Adjustment viewed education and training as key to the success of Canada and for individual companies. However, the Advisory Council also pointed out that few corporations undertake training and/or retraining in Canada. According to the *Report*:

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[94] "General availability" would seem to be almost self-explanatory. Nevertheless, differing interpretations have been made. It has been variously determined that "specific" benefit can derived from government programmes based on take-up rates -- on the distribution and number of eligible firms which actually make use of the programme -- even though programmes are available for all. In other cases, a programme for the fishing or forestry industry as a whole have been considered not sufficiently general, but would need to be available to both, or all, industries in order to be deemed "general".

[95] CANADA. *Senate Committee on Foreign Affairs*, Proceedings, December 29, 1988.

[96] STATISTICS CANADA, Business Conditions Survey, October 1988.

> In 1984, three out of four establishments did not provide any formal training....Moreover, in firms offering training, evidence shows that it is directed in large part to employees who already have above-average education and pay[97].

While "the Council believes that the responsibility for training the unemployed -- some one million -- rests primarily with the government....[and that] the responsibility for most of Canada's training effort -- training the 12 million or so employed -- rests with the private sector", it also recognizes "that the private sector will not increase its training efforts simply because it is exhorted to do so" and recommends "establishing a corporate tax liability that would be offset completely if a firm provided a base level of training". But, even though "the Council recognizes that without appropriate safeguards [it] might produce only a minimum level of incremental training", it suggests that "such a tax liability should be set at a relatively low level, so that employers would have little difficulty matching it"[98].

While business response to the Council's proposed shift of training responsibilities to business has generally been positive[99], there is resistance from some business circles to what amounts to a payroll tax[100]. The Province of Ontario is considering such a programme of its own, but it appears likely to raise some of the same objections. At a recent conference organized by the Canadian Manufacturers Association and the Premier of Ontario, agreement could not be reached even that businesses should be primarily responsible for training their own employees, although the consensus among the participants had clearly shifted towards that view.

Although governments at various levels remain committed to higher education and training, government spending in these areas has not kept up with either inflation or the growth in enrolment. Statistics Canada reports that federal government payments for education and training will total $6.7 billion this year, up 1.8 per cent over last year. This contrasts with a 3.6 per cent increase in total federal government spending, exclusive of debt servicing charges. Nor is this a one-time reduction. The average federal funding increase reported for the period 1985 to 1989 has been 2.3 per cent, while the rise in the Consumer Price Index over the same period -- which many believe to under-represent the level of inflation for post-secondary institutions -- has been 4.2 per cent[101].

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[97] ADVISORY COUNCIL ON ADJUSTMENT, 1989. Adjusting to Win, Ottawa: Supply and Services Canada, p. 42.

[98] *Ibid.*, p. 44.

[99] *Financial Times*, 1989 "Bouncing into job retraining", April 3.

[100] *Montreal Gazette* 1989 "Report Links Tax to Training", March 30; and "de Grandpré report split", April 14. In fact, the Canadian Federation of Small Business has withdrawn from the Alliance for Trade and Job Opportunities because the CFIB does not support the proposal for a training tax.

[101] This matter is fully discussed in CANADA. *Standing Senate Committee on National Finance* 1987 Federal Policy on Post-Secondary Education.

In addition to the short-fall against inflation of over 4 per cent, post-secondary institutions also expect to have a 3 per cent increase in enrolment this year, with projections for continued real growth.

There is increasing concern that Canada's primary and secondary education systems are also under-performing relative to those of competing countries, with the possible exception of the United States. The Prime Minister had indicated that the issue of a national educational strategy was to be discussed at the most recent First Ministers' meeting. However, the continuing difficulties over the Meech Lake Accord prevented this item form receiving full consideration.

4.1.3 Research and Development:

Canada's comparatively low rate of expenditure on research and development is common knowledge. Canada consistently ranks last or next to last among OECD countries in rankings of proportion of GDP devoted to R&D, and barely approaches half the rate in the United States, Japan or West Germany. In money terms, Canadian industrial R&D spending was only $3.8 billion compared to $107 billion in the United States in 1986.

Most commentators and industry analysts agree that increased R&D spending is required if Canada is to prosper during this period of structural adjustment. This also requires improved co-operation among the principal sources of R&D investment: business, academe, and government[102].

Recent Canadian tax reforms have meant a less generous tax treatment for R&D expenditures, reducing the allowable write-off by about 20 per cent. The Conference Board has targeted this as a factor contributing to reduced R&D expenditures by industry. The Advisory Council on Adjustment took note of this and recommended that the government monitor the impact of the tax treatment of R&D activity, with a view to providing increased incentives when appropriate.

There is much dispute over which sector -- business or government -- has been failing to carry its weight. This focuses on several issues, particularly spending differences between domestic and foreign firms[103], and whether expenditures have kept pace with commitments. There is, however, almost universal agreement that total R&D spending in Canada is not keeping pace with that of other countries and that new initiatives are required by all sectors.

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[102] The private sector provides about 53% of total R&D spending in Canada; other shares are: universities and colleges 23%; federal government 16.5%; provincial governments 3%; non-profit groups 1.5%.

[103] MCFETRIDGE, D.G., 1989. Les enterprises multinationales et la libéralisation des échanges, Ottawa: Economic Council of Canada.

While no new government R&D programmes specifically related to the FTA are reported, the government has recently announced the formation and funding of 14 different research programmes under its new Networks of Centres of Excellence, in the fields of health care, space and ocean research, construction, robotics, and telecommunications.

In the corporate sector, R&D spending continues to lag behind other countries, with one or two notable exceptions. In the high-technology telecommunications and aerospace industries several companies are consistently high spenders, and, perhaps as a result, are globally competitive. The **Connaught-Mérieux** merger is expected to contribute to an increase in R&D in the pharmaceutical industry, where spending has increased marginally since patent protection was increased. The government has also recently committed some funds to the establishment of a Canadian Institute of Bio-technology to assist the Canadian industry.

However, the fact that R&D spending of the various subsidiaries of **BCE**[104] together account for nearly 20 per cent of corporate R&D spending in Canada, with the top ten firms accounting for over half, indicates that the vast majority of companies are not significant spenders.

While some portion of this lower R&D spending level may be accounted for by the structure of Canadian industry -- a large percentage of Canadian GDP is derived from branch plant assembly operations[105] -- nevertheless some foreign firms are among the top spenders.

- **IBM**, which spends over $5 billion worldwide, spent about $180 million in Canada in 1989[106] and has its second largest software development programme located in Canada.

- **Pratt & Whitney Canada** spent $247 million.

However, other branch operations spent very little.

- **Xerox** spent only $15.2 million.

- **Johnson & Johnson** spent only $3.5 million.

Low R&D spending by subsidiary companies remains a serious problem.

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[104] Primarily Bell-Northern Research (BNR) and Northern Telecom (Nortel).

[105] For instance, the biggest players in the largest manufacturing industry in Canada, the automotive industry, do virtually no R&D work in Canada. It is reported that General Motors has begun to do some industrial process engineering research as part of the massive expansion of its Oshawa Autoplex, but this would still represent only a very small portion of the substantial R&D work done by GM.

[106] This represents about 6.9% of IBMs Canadian sales of $2.6 billion, approaching the world-wide R&D figure of 7.75% of sales.

4.1.4 Trade Promotion:

The Government has identified five new or improved programmes to enhance Canadian exports to the United States.

- It has increased the number and depth of studies used to identify market opportunities for Canadian producers.

- It has expanded Canadian participation in international trade fairs. Over 10,000 Canadian firms participated in over 400 different such events in the United States in 1989.

- A programme encouraging links with border states -- New Exporters to Border States (NEBS) -- has been expanded.

- A similar programme -- known as NEXUSS (New Exporters to United States Southern States) -- has been established to improve Canadian penetration in the South.

- To encourage U.S. purchases of Canadian goods, U.S. buyers have also been brought on missions to Canada.

Over $20 million was allocated to these programmes in the 1989 fiscal year and the Government estimates that $1.5 billion in new business will result. The Government has also announced the opening of three more satellite trade offices in the United States, bringing the total number of trade missions there to 27. As well, a large number of "hands-on" seminars have been conducted for Canadian firms interested in expanding their sales to the U.S. government and in the detail of export financing, customs procedures, and the new rules of origin.

It is important to note that NEXUSS and the other new U.S.-oriented programmes are intended not only to aid export penetration in the United States, but are to be used as stepping stones to the broader global market. The Minister of International Trade told a House of Commons committee that "the ultimate goal is to develop an outward looking trading culture where the knowledge and expertise of Canadians match the importance of international trade to our economy"[107].

A number of initiatives have also been taken with respect to trade prospects in Europe and the Asia Pacific basin[108].

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[107] CANADA. *House of Commons. Standing Committee on External Affairs and International Trade* Proceedings, 3:11. May 25, 1989.

[108] These are discussed below in Sections 7.1 and 7.3.

4.1.5 Trade Intelligence:

The Department of External Affairs has retained a number of consulting firms to begin the task of identifying subsidy programmes provided by various levels of government in the United States that may have an impact on Canadian trade prospects. While this task was initially expected to be completed by March, 1990, Minister Crosbie has recently stated that the process may take a full year. It is unclear whether the government will take steps to ensure continued monitoring of such practices in the United States, beyond the normal surveillance by diplomatic staff.

Monitoring international developments and competitors' plans may soon be just as essential as prospecting for new trade opportunities for Canadian exporters. Early intelligence on foreign export plans can be of strategic assistance to domestic Canadian firms. Increased government and industry association monitoring in this regard is therefore warranted.

4.1.6 Government Procurement:

To meet the FTA requirements for opening up government procurement practices, the Government has combined the Bulletin of Business Opportunities and the Gazette Notices of Proposed Procurement and Contract Award Notices into a new weekly publication, *Government Business Opportunities*.

Available contracts will be classified under these categories: restricted to Canadians; open to Americans under the FTA; and open to all under the GATT. While in some cases, the required pre-qualification of potential contractors may restrict access to government contracts, the new Procurement Review Board has had some success in making the entire process more transparent and, in general, open to a wider range of eligible suppliers.

While the United States has also reclassified contracts in accordance with FTA requirements, it has not made any changes to its contract notice process. Instead, individual bidders are left to determine which, if any, contracts may be available for Canadian suppliers. Since the United States agency responsible for procurement has not co-operated in revamping their lists, the Canadian government has now undertaken to sort the daily U.S. list and produce a more comprehensible list for use by potential Canadian suppliers.

4.1.7 Other Government Measures:

The federal government has announced increased funding for universities offering international business education and has helped to establish a new Centre for International Trade Policy and Law, jointly based at Carleton University and the Université d'Ottawa.

As well, a number of university- and NGO-based research projects on international competitiveness, U.S. subsidy practices, and other trade-related matters have been financed.

No changes as yet have been reported to the data collection methods of DIST, Investment Canada, or Statistics Canada which would help to differentiate between the United States

and the rest of the world with respect to the origin of transhipped or further processed goods. Nor have additional questions, attempting to measure the effect of the FTA on investment or other decisions, been added to on-going government surveys of business intentions.

Few detailed studies of individual industries, seeking to identify FTA effects, yet appear to be supported or underway, although the Institute for Research on Public Policy has recently received funding from the Donner Canadian Foundation to begin such work.

4.2 RESPONSE & INITIATIVE ELSEWHERE

4.2.1. Provincial Government Initiatives:

Provincial governments have also undertaken a number of initiatives in response to the FTA. While there has been some dispute over whether the provincial governments are bound by the FTA, by and large they have followed through where action was required, with the notable exception of barriers to trade in alcoholic beverages where progress has been slow.

Liquor, wine and beer pricing practices in Ontario and shelving requirements in Quebec may lead to United States action under the FTA or a continuation of the long running GATT complaint.

Provincial industry ministries also have been actively pursuing the same goals as their federal counterparts in attempting to assist adjustment to FTA forces. As they do so, more intense scrutiny by the United States of potentially countervailable practices seems likely[109].

The **Province of Ontario** has established The Premier's Council, an advisory panel of corporate, academic and government experts. It has produced a report, *Competing in the New Global Economy*, which identifies the strengths and weaknesses of the Ontario economy in a global context[110] and includes adjustment and restructuring advice in its recommendations. As a follow-on to this report, the Premier's Council has commissioned a number of studies and recently co-hosted a forum with the Canadian Manufacturers Association (CMA) to address the question of how to make Ontario's companies, worker-force and government policy more competitive. Policy initiatives to meet those goals, including the possibility of a pay-roll tax for training, are expected from the Ontario provincial government in the spring.

In **Nova Scotia,** the government appointed an Adjustment Advisory Council, chaired by Gilbert Winham of Dalhousie University, to address the same issues as the de Grandpré task force. Its report, *Adjusting to the Challenge*, was issued in September, 1989, and while generally following the thesis of the Economic Council and the de Grandpré report -- that adjustment programmes need to be universal -- it did make several specific recommendations for adjustment assistance to industries thought likely to be subject to

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[109] For example, Ontario's new wage assistance programme for engineers, called an "incentive" rather than a subsidy by the Ontario government, is likely to cause alarm as it is directed to exporting firms. Other "subsidy" programmes may also attract U.S. attention. For example, see "L'attitude des provinces dans certains dossiers mettrait en danger le traité de libre-echange; le talon d'Achille: les subventions gouvernementales aux enterprises", *Le Devoir*, 15 juillet, p. A2.

[110] PREMIER'S COUNCIL, 1989. Competing in the New Global Economy 3 Volumes. Toronto: Province of Ontario.

serious competitive challenges under the FTA. These included various sectors of the agriculture industry and the clothing and textile industries.

4.2.2 Local and Municipal Government:

A number of border cities such as Windsor and Brockville have begun the process of establishing new industrial parks designed to facilitate new investment from U.S. firms. However, so far, little new investment has been reported.

Other municipalities have expanded existing trade promotion activities in the United States, and a number of mayors have led delegations to Europe and Asia in the search for new investment.

A number of U.S. border cities, including Buffalo and Ogdensburg, New York, have been actively pursuing new Canadian investments and promoting themselves as locations for export oriented U.S. companies.

4.2.3 Corporate Initiatives:

While business interest in the idea of free trade remains high, the Canadian Manufacturers Association has expressed concern that free trade means little to a large portion of Canadian business. A survey of CMA members in the spring of 1989 found that only a minority had done any detailed study of the impact of free trade on their customers, suppliers and competition even though 40 per cent expected to rationalize their product lines as a result. Surprisingly, nearly 60 per cent of its members reported that there would probably be no substantial change in the way they operate[111].

A major report, *The Aggressive Economy: Daring to Compete*, released in June, 1989, set out the CMAs concerns and recommended actions to redirect the attention of its members towards outward-looking and competitive strategies.

In January, 1990 the CMA co-hosted a forum with the Province of Ontario and has commissioned a number of consulting reports on the strategies followed by companies which have both succeeded and failed to enhance their competitiveness.

Much of the corporate response to the FTA is discussed in the Section 3.2 - Changes in the Structure of Employment and Production.

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[111] As reported by the *Globe and Mail*, "No clear pattern on free trade", July 4, 1989 B1.

4.2.4 Lobby and Research Groups:

Pro-free trade business groups, such as the Business Council on National Issues and the CMA, continue to be active, although the focus of their trade-related work has shifted to the nuts-and-bolts of managing trade. Much less promotional work and research on the positive benefits of free trade is being done by these groups. The **Alliance for Trade and Job Opportunities** seems to be dormant.

While the pro-free trade groups have steered away from releasing reports, individual companies which had been part of these groups, such as the **Royal Bank**, have released evaluations of the first year of the FTA. The **C.D. Howe Institute** is also expected to produce a comprehensive report early in 1990.

Independent "for-hire" research groups, such as Informetrica and the Conference Board, have scaled down the general attention they give to FTA-related matters based on reduced demand, although consulting groups which are more directly tied to technical trade management issues have experienced some increased demand.

Several specialized news services provide in-depth information for the trade policy and law community. These include the law reporting company, CCH International, which produces *The Free Trade Observer* monthly, for incorporation into its binder *Free Trade Law Reporter*, and the *Globe & Mail*, in conjunction with the *American Banker*, which has begun weekly publication of the *Canada-U.S. Report on Free Trade*.

A large number of research projects on various aspects of the FTA, business restructuring, cross-border investment flows, and international trade are under-way at an assortment of independent research institutes and at the universities, although there is little evidence of co-ordinated effort.

Some of the groups which had actively opposed passage of the FTA continue to be active in monitoring and publicizing events which they believe to be connected to the FTA. They contend, further, that a number of government policy actions, well outside the formal requirements of the FTA, are a part of the implementation process[112]. While the Government denies any direct link between the FTA and these other actions, the Minister of Employment, Barbara McDougall, speaking on Bill C-21, the Government's proposed changes to the unemployment legislation, stated that "privatization, deregulation, tax reform and free trade are all parts of the same agenda [as the UI changes] for revitalizing the Canadian economy to meet the needs of the increased globalization of markets and rapid

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[112] These include the artificial maintenance of high exchange rates, too easy acquiescence to unfavourable GATT rulings, changes to Unemployment Insurance eligibility and benefits, the removal of transportation subsidies, and several parts of the June, 1989 budget, including the elimination of postal subsidies and two dairy support programmes and cutbacks to regional development spending. See, for example "Atlantic Agency's uncertain future worries business" *Toronto Star* August 28, 1989.

technological change"[113]. Likewise, Trade Minister John Crosbie often notes these other elements when discussing how Canada is adjusting to free trade, but distinguishes between "linkages" and "causation".

Opposition groups continue to keep these matters before the public, and regularly report on their views, including the provision of lists and analyses of corporate and government restructuring activity.

- The **Pro-Canada Network** has been the most active in performing or co-ordinating research and publicity work related to the FTA.
- The **Council of Canadians** has reported a doubling of membership in 1989.
- The **Canadian Labour Congress** has undertaken to compile and analyze and make available data on job losses and plant closures.

4.2.5 Co-operative Adjustment:

Both unions and employer groups, such as the CMA, have recognized the need for including workforces in decision-making and for positive adjustment activities, rather than fighting over each stage of rationalization. However, the perceived inadequacies of government adjustment assistance programmes, the absence of employment guarantees in most collective agreements, coupled with a history of lay-offs and plant closures by individual companies undergoing restructuring or introducing new production techniques, has contributed to an atmosphere where little co-operation seems likely in the short-term.

A positive force in this area has been the **Canadian Labour Market and Productivity Centre**, which was established in 1984 to facilitate direct consultation between business and labour on issues of broad social and economic concern. It has undertaken a number of initiatives to enhance joint efforts between business and labour towards improving productivity. A number of working groups have been established to address the Canadian response to the many global forces and adjustment pressures which are acting on the Canadian economy, and directly or indirectly include consideration of FTA related matters.

Occasionally, takeovers by employees or local management has been a response to potential plant closures. These efforts have continued.

- The United Steelworkers, which represents workers at the Inglis plant in Toronto slated for closure by its U.S. parent, Whirlpool, sought partners to keep the 650 employee plant open. The union, together with the City of Toronto, Metropolitan Toronto, and the Province of Ontario contracted consulting reports and feasibility studies examining the possibility of a worker buyout and of potentially profitable product lines. These efforts ultimately failed and the plant closed in November, 1989.

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[113] CANADA. *House of Commons Debates, June 6, 1989.*

- In Cornwall, Ontario, employees of **Marimac**, a drapery manufacturer, are attempting a takeover prior to the slated February, 1990, closure.

- The management of **Ricwil Limited**, an insulated pipe manufacturer in St. Thomas, Ontario has been negotiating with head office in Ohio to create a new and independent Canadian company which would then re-open the plant.

5.0 POLICY HARMONIZATION

Harmonization of national policies has become a central concept emerging from the economic pressures of the 1980s and has arisen in Canada in particular association with the debate surrounding the FTA. In some contexts it is taken to imply beneficial international collaboration and concertation in the management of economic events. In other contexts, it is used negatively to imply international pressures to compel national policies to serve a narrow business agenda exclusively. Both senses are discussed under a number of sub-section heads in this section.

5.1 HARMONIZATION & SOVEREIGNTY

In response to the pressures of global restructuring and the growing interdependence of national economies, noted almost continuously in this report, some countries have begun to recognize the necessity of undertaking co-operative initiatives as the best way to respond to the fact of interdependence. While classical trade theory suggests that comparative advantage will dictate what gets made where, and what gets traded as a result, and that varied factor endowments result in varied industrial structures and trade, today, governments also play a major role in this process.

Many government policies can effect the competitive capacities of companies seeking to do business. For example, laws dictating high minimum wages in one location may move production of a good requiring low-skill labour to another location, while low levels of education and skills training will push high-technology or research related jobs to areas with a better educated workforce. Differences in investment and taxation policies, regulation of health and safety, and environmental protection rules also contribute new complexity to locational decisions by corporations seeking the maximum return for their efforts.

Whether or not a country is in a free trade relationship with some or all of its trading partners, all countries for which trade is important face pressures to harmonize, or to equalize the effects, of policies that have an important consequence for the business environment. Entering into a free trade agreement will only increase those pressures, particularly in areas of the economy that lack natural economic advantage such as abundant natural resources or energy supply, or which face high transport costs. Increasing market size brings increased sales opportunities, but at the same time increases competitive pressures.

As the range of policy environments that business can choose among widens, pressures for harmonization of government policies will increase. These pressures can be met (a) by moving towards the adoption of international market-based standards whose lowest-common-denominator tendencies often do violence to the social goals of states; (b) through the negotiation of co-operative agreements; or (c) by resorting to protectionism to isolate all or part of a national market from international competition. Of course, the protectionist option is eliminated for those sectors of an economy encompassed within an agreement for a free trade area.

Beyond policies focussed narrowly on the business environment lie broader areas of what might be called "framework" economic policies whose harmonization commands, at least in some respects, little dissent. One such area, of course, involves the continuous attempt by industrial countries, at Summits, in the OECD, at the G-7, and within the International Monetary Fund, to engage in multilateral co-operation in establishing the structures of monetary and fiscal policy.

Perhaps more contentious are attempts by OECD members to co-ordinate those economic policies, such as interest and exchange rates, and government spending levels, which affect a country's ability to deal with the accelerating pace of globalization of trade. There has also been enormous pressure to integrate world financial markets and institutions. These trends, which echo those in international trade generally, include deregulation, reduced exchange controls and extra-national use of national currencies, securitization, new types of transaction processing, and twenty-four hour screen-based trading. One consequence of these global forces has been to add substantially to domestic pressures for deregulation and integration of financial institutions in and between Canada and the United States[114].

Canadian participation in international co-operative attempts to deal with growing interdependence and the globalization of the economy, and a significant unilateral domestic response, were both already well under way before the inception of the trade negotiations with the United states. For instance, with reference to international attempts among the G-7 countries to manage exchange rates, the Governor of the Bank of Canada recently stated that:

> the major industrial nations are presently engaged in an exercise of international economic co-operation and co-ordination that is quite unlike any previous experience in its regularity and intensity, and in the scope of its agenda. This exercise has implications for all kinds of policies, including monetary policy[115].

Some have suggested that international monetary and fiscal co-ordination on this scale threatens national sovereignty; yet it is also contended that "nations do not lose sovereignty by reaching agreement with other sovereign nations to reassert some measure of political control over the evolution of economic events"[116]. A failure to respond to international pressures for harmonization, by not harmonizing directly, negotiating multilaterally or creating national programmes with equivalent effects to international standards may lead to isolation, protectionism and economic decline. Policies to restrict competitiveness may contribute to the erosion of the very sovereignty they were intended to protect. How a country faces these pressures, whether actively with initiative or passively by rear-guard

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[114] Discussed in Section 5.2.1 below.

[115] Speech by John Crow, Bank of Canada, May 15, 1989.

[116] OGATA, COOPER, SCHULMANN, 1989 International Financial Integration: The Policy Challenges Report to the Trilateral Commission #37, p. 2. New York: The Trilateral Commission.

response, whether through unilateral action or international negotiation, is more at the centre of the question of the exercise of sovereignty.

However, policy harmonization often goes beyond co-operation and co-ordination and international pressures for it become most contentious when those pressures invade the structures of domestic social policy or threaten the way a country chooses to attempt to ameliorate regional inequities[117].

[117] Some of these concerns are examined in Sections 5.3 and 6.3.1 below.

5.2 ECONOMIC POLICIES

5.2.1 Financial Services:

The progress towards North American free trade in financial services and the integration of financial markets reflects a movement already well under way in Canada in response to global forces. It has also been suggested that these international pressures cannot be ignored, and that to do so might relegate Canadian banks and other financial institutions to a regional role, effectively denying them, and Canada, easy access to the world's principal capital pools and financial markets[118].

Depending on how one views the current status of North American financial institutions and regulations, the FTA financial services provisions may play a major role in either speeding or slowing the process of globalization in Canada.

Some analysts take the view that U.S. regulations are increasingly out of step with those of the other major financial service centres, such as London and Tokyo, and prevent the innovation and scale required to be globally competitive. If Canada adopts the U.S. way of doing things it may "leave us with a branch-plant service sector alongside our branch-plant manufacturing sector"[119] without moving it closer to being globally competitive.

In the United States a number of long-standing laws and regulations prevent inter-state banking and combined investment and commercial operations, a policy at odds with international trends. While the United States, through the FTA, undertook to make "best efforts" attempts to reduce these restrictions, progress has been slow. As a result, Canadian financial services companies may be hampered in their attempts both to enter the United States market and to participate in world markets at the same time.

If the United States brings about these changes in its domestic regulations, new markets may open for Canadian financial services. On the other hand, the mere presence of the larger U.S. financial institutions operating in Canada, under the auspices of the Financial Chapter of the FTA, may create more of the competitive pressure needed to hurry the restructuring of the Canadian financial sector. The FTA may therefore indirectly lead to the development of the competitive strengths needed to export financial services into the international marketplace successfully, even if the United States and U.S.-based banks are not in a position to do so.

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[118] COURCHENE, T.J. 1988 Proceedings Senate Foreign Affairs Committee, July 28.

[119] ONTARIO. *Ministry of Treasury and Economics* 1986 "Background Notes" in Ontario Study of the Service Sector May p. 25.

5.2.2 Exchange Rate Management:

Three issues have brought the Canada/U.S. exchange rate into recent prominence:

- The upward trend in the rate itself, which has, perhaps, focussed more intense pressure on Canadian exporters than any other international influence;

- The fact that fluctuations in exchange rates have a larger and more immediate effect on inflation, employment, investment and locational decisions in Canada than in many other countries because Canada is far more dependent on international trade. Indeed, according to the Governor of the Bank of Canada, John Crow:

> the Canadian economy is very open to international exchange and international economic and financial influences. More than a quarter of our total production, of goods and services, is traded internationally. We have no exchange controls of any kind and our two-way flows of capital are large by any yardstick.[120]

- Allegations from some quarters that recent trends in the Canada-United States exchange rate are attributable to the FTA, through a "secret" deal between the two countries' finance ministers in late 1988 made to re-start the stalled FTA negotiations.

The United States, Canada's largest trading partner, is less dependent on both trade in general, and North American trade in particular, than is Canada. This together with the fact that a large proportion of Canada/U.S. trade is priced in U.S. dollars causes exchange rate fluctuations between the two countries to play a greater and more immediate role in effecting the Canadian economy.

5.2.2.1 The Exchange System:

Canada maintains an independently floating exchange rate, one of only fifteen countries which does so[121]. While Japan and the United States are in this group, the European Community (with the notable exception of Great Britain) has moved towards stabilizing exchange rates among its members' currencies[122].

The central virtue of the European "snake" is thought to be the greater encouragement to trade and investment activity brought about by the reduction of exchange-rate risk.

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[120] Speech by John Crow, Governor of the Bank of Canada, 15 May 1989.

[121] INTERNATIONAL MONETARY FUND, 1988. Annual Report 1988 Washington, D.C.: IMF.

[122] Exchange rates in the European Monetary System (EMS) are maintained within a margin of 2.25 per cent around the bilateral central rates against other participating currencies, with the exception of Italy, where the margin is 6 per cent.

Most of the larger developing countries, primarily the newly industrialized ones (NICs), also have floating rates, but generally these are closely managed against other economic indicators in order to support monetary, investment or industrial policies[123]. Most other small, open economies maintain fixed or pegged range rates against the currencies of their major trading partners[124].

5.2.2.2 The Canadian Exchange Rate:

Since the demise of the Bretton Woods system in the 1970s, the Canadian dollar has moved through long swings, first rising, then gradually falling against the U.S dollar. From a premium over the U.S. dollar in the mid-1970s, the Canadian dollar declined to its lowest level of U.S. $0.7152 by 1985.

Concurrent with the advent of the Free Trade Agreement with the United States, the exchange rate has risen, first to U.S. $0.7696 when the agreement was signed in December 1987, to U.S. $0.8218 when the 1988 election was called, and to U.S. $0.8450 when the Agreement came in to force. The dollar recently has traded at an average of U.S. $0.8550 with highs of over $0.86, although in the early part of January, 1990 the average rate had fallen off by about two per cent.

Some of the rise in value of the Canadian dollar can be attributed to business confidence in Canada, and a higher demand for Canadian-dollar-denominated investments. But the larger part is attributed to the strong anti-inflationary stance of monetary policy and the resulting high level of nominal and real interest rates in Canada, attracting strong portfolio inflows.

Exchange rate variations have appeared to follow a pattern which supports the allegation of an implicit agreement on the part of Canadian authorities to reduce the competitiveness of Canadian exports. Since the advent of the FTA the dollar has risen and stayed high in terms of the U.S. dollar. There is little if any evidence, however, to support such a contention. Moreover, the Ministers of Finance and Trade have both issued specific denials of such allegations on several occasions. Nevertheless, actions by the Governor of the Bank of Canada to sustain wide interest rate differentials between Canada and the United States -- which have been taken as a defence against inflationary pressures -- have in fact led, through exchange rate appreciation, to a decline in the competitive position of Canadian industry.

While a high rate of exchange may lead to increased competitive pressure to adjust, an overly high rate, coupled with high interest rates, will reduce the capacity of Canadian enterprises to improve productivity and make new investments in order to take advantage of the opportunities and challenges of the FTA and global economic restructuring.

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[123] Brazil, Argentina, India and Korea for example. About twenty five countries have some sort of flexible, but not fully floating exchange rates.

[124] Sweden, Norway, and Austria fit this category, as do most developing countries.

5.2.2.3 International Competitive Effects:
At the same time as the Canadian dollar has risen against the U.S. dollar, both have risen against most other major currencies. As noted above, the Canadian dollar has risen 16 per cent against the U.S. dollar in the last three years, half of that in the past twelve months. Over the same twelve months, it has risen 13 per cent against the yen and an average of 18 per cent against EC currencies.

While some pricing-for-market activity[125] by Canadian exporters has softened the short-term effect to some degree, in the long term artificially sustained currency appreciation could lead to a significant decrease in export opportunities, while increasing foreign competition at home and obstructing adjustment.

- For example, **Electrohome Canada** of Kitchener estimates that absorbing a portion of the exchange rate rise in its prices cost it over $500,000 between September, 1988 and September, 1989.

- **Galtaco**, an auto parts manufacturer in Paris, Ontario has cited the higher dollar as the reason it has closed its 400-employee factory.

- The value of the dollar also has received part of the blame for the closure of eight **Fishery Products International** plants in Atlantic Canada over the summer of 1989, one of which was closed permanently.

- **Stelco** also has noted increased competition from U.S. steel producers in Canada, where it sells over 85 per cent of its production.

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[125] This is a practice where prices for an export good are fixed in the importing country's currency, which occasionally leads to accusations of dumping. See IMF 1989 "Exchange Rates Affect Trade Balances" *IMF Survey* June.

5.3 SOCIAL POLICY

Nowhere do intense international competitive pressures raise greater concerns than in their potential threat to the structures of social policy -- the health and safety of workers, the unemployment insurance systems, the redistribution systems (generally to the aged, the young, and the infirm), the medicare systems, and, in Canada, the structures designed to diminish regional inequity.

Whatever the health of national economies, there is a fear that investment, industry and employment will shift to havens with the least-cost facilities, breeding a new form of beggar-thy-neighbour policies. These kinds of concern have generated a new interest in international agreements to resist this kind of predation by the establishment of international standards.

This is reminiscent of the intentions which informed the 1948 Havana Charter for an International Trade Organization[126]. Full employment and improved and consistent labour conditions were central to the plans of that time. However, the ITO was replaced by the GATT, a far less ambitious trade organization designed to facilitate a move to lower tariffs without making provision for the avoidance of ruthless competitive practices or with the ability to deal with new forms of anti-competitive and other trade distorting practices.

5.3.1 Euro-Charter:

The same need to reconcile national differences multilaterally, and a desire to ensure that social needs were met, were both recognized at the formation of the Council of Europe when a social charter was included in its constitution.

This charter makes explicit the minimum rights to be expected by workers and commits member governments to harmonize their social and labour standards upwards to the highest existing standards, rather than downwards to the lowest, as market forces would dictate.

As the European Community moves towards completion of the internal market, this matter is before the Community once again, as some countries push for the Charter to be given force inside the new single Europe. While the United Kingdom so far has resisted what Margaret Thatcher has called "socialism by the back door", an attempt is being made to develop a consensus on the scope of the new social charter, on the role of the various European institutions in its enforcement and administration, and on the role of national governments in setting future standards. A working group established as a part of the Single Europe process has been developing a series of directives to implement the objectives of the social charter, but it is unclear whether these will be implemented in the

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[126] The ITO, together with the IMF and the IBRD (the World Bank), were to be the institutions which would guarantee the post-war international economic settlement. Failure by the United States to ratify the ITO treaty, largely because of its disagreement with the social charter aspects of it, and the formation of the GATT as an "interim" organization by the major trading nations of the time, led to the collapse of the ITO.

weak form of recommendations that emerged from the December, 1989, European Summit, or whether some countries will continue to press for enforceable, binding directives.

5.3.2 Social Programmes under the Canada-U.S FTA:

Unlike the Euro-charter, no explicit guarantee that any particular social programme was exempt from trade action by the other country was included in the FTA. Critics of the Agreement see this as one of its most serious flaws, pointing to the asymetries of size and power between the two countries, the high degree of economic interdependence and the substantial differences in social programmes as likely to lead in Canada to a gradual erosion of hard-won benefits by competitive pressures.

It is important to distinguish between two different types of social programmes or employment standards:

- those which raise the direct cost of doing business for all employers -- such as minimum wage laws, UI premiums, or health and safety rules; and
- those which may reduce costs to some employers but are financed by higher taxes on all -- such as universal health insurance or regional development incentives[127].

This distinction will help determine the economic and political viability of Canadian social programmes and standards.

In the latter case, U.S. competitors who believe themselves subject to unfair competition as a result of the "subsidy" provided by these programmes may make use of U.S. trade remedy laws, such as countervailing duties, to bring pressure against the offending Canadian government to bring its programmes into line with those of the United States, or to remove the competitive advantage conferred by the imposition of countervailing duties.

In contrast, in the first case requests for reduced social spending and lower standards may come, not from the United States, but from Canadian sources. For instance, some Canadian manufacturers already have identified minimum wage levels, higher in Canada than in some U.S. states, as a handicap to competitiveness and have requested reductions. While it seems unlikely that reductions will occur, the increased freedom to relocate production to lower wage jurisdictions within the new expanded Canada-United States market created by the FTA in many industrial sectors can only increase pressure to keep standards to a minimum. This holds equally true for any company presented with wage

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[127] It has been estimated that Canada's medicare system reduces by $300 the cost of each car assembled in Canada over those assembled in the United States. The average per employee cost of similar health coverage now exceeds $2600 compared to $600 in Canada. Companies which do not pay any health benefits would be better located in those jurisdiction without the higher taxes needed to sustain the state funded portion of health care.

demands by its Canadian workforce. As well, many U.S. states have "right to work" laws, lower health and safety requirements, and much lower taxes. At least one state (Georgia) has been advertising these "advantages" to attract new investment from Canada.

5.3.2.1 Medicare:
Fears that Canada's universal health insurance programme might be attacked have abated, partly because the program is explicitly generally available and partly because many Americans -- in government and in business -- have recognized that the Canadian method provides wider coverage and is more cost-effective than their own market-based approach[128].

5.3.2.2 Unemployment Insurance Reform:
For a variety of reasons, often diametrically opposed, most of the groups on both sides of the free trade debate have called for changes to, or enhancement of, unemployment insurance and employment assistance programmes. Some do so because current programmes are expensive, either for themselves or for the country in general, thereby raising taxes; others see the current system as reducing the incentive to work. Still others find UI to be either inadequate to meet the retraining needs of displaced workers or misconceived in that it mixes insurance coverage with other public policy goals, thus confusing the nature of the programme and making it unclear who should pay for which portions.

In recent years a number of studies and Commissions at both the federal and provincial level have examined the deficiencies of Canada's unemployment assistance programmes. Bill C-21, introduced in Parliament in June, 1989, represents a legislative response to some of those criticisms. If passed, the bill will alter the funding structure of the UI system, transferring the full burden to employers and employees. It will also shift the balance of total spending towards retraining and away from individual assistance.

The Government has justified the bill on the grounds that in a competitive, rapidly-changing environment, greater emphasis must be placed on retraining and says that the changes are desirable even if there were no FTA. More generally, it defends the legislation, along with the FTA, as different weapons to strengthen the Canadian economy. The Government denies that the changes proposed by Bill C-21 are a response to U.S. demands made during the free trade negotiations, but it is true that the changes to UI, if passed, would in fact bring Canada's system more into line with practices in many U.S. states.

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[128] At least two groups of U.S. legislators and their aides travelled to Canada to study the Canadian health care system in 1989 and many in Washington are considering using some of the so-called "peace dividend" to extend a similar programme to the United States. The AMA and the U.S. private health insurance industry have recently launched a public relations attack, attempting to discredit several aspects of the Canadian system.

5.4 DRUG TESTING

An obvious instance of the pressure for policy harmonization is demonstrated by the application of U.S. drug testing laws in Canada. The United States has instituted mandatory random drug tests for employees in safety-sensitive transportation jobs. These include rail, truck and bus drivers; airport and airline maintenance workers and pilots; and people in the marine and pipeline industries.

Many Canadians view such mandatory testing as a threat to their basic human rights, and Canada has not instituted such programmes. However, open borders for transportation workers and maintenance personnel means that Canadian companies wanting to do work in the United States, or to do work for U.S. transport companies operating in Canada, will have to subject their Canadian personnel to the testing programmes.

For example, in May, 1989 U.S.-based Northwest Airlines notified Air Canada, which performs maintenance work for Northwest in Winnipeg, "that failure to comply with the regulations will mean that Northwest Airlines will no longer be able to use your services to perform maintenance work after June 29, 1989"[129]. While this matter has been referred to the Commission for resolution, the regulations were slated to be enforced beginning January 1, 1990.

Even though there has been some resistance to enforcing these new regulations in the United States itself, Canadian firms which do not make themselves subject to the new rules will clearly lose business. While Canadians still will have a right not to subject themselves to U.S. drug testing laws, they may also be prevented from operating commercial transport vehicles and pipelines in the United States and performing maintenance work on U.S. vehicles and aircraft.

There always has been pressure on companies interested in doing business outside their own country to adopt the practices and procedures of their customers. However, as the Canadian economy becomes more and more closely integrated with that of the United States, pressures to harmonize policies and procedures will also increase. If companies, countries, or people wish to continue to do business in this highly integrated setting -- on this single playing field -- the question to be answered is not whether to harmonize, but how.

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[129] Cited in CLC, *Tradewatch*, 1(2) May 1989.

5.5 INDUSTRIAL POLICY

In the pursuit of policies to promote economic growth, Canada and the United States have differed over what is and is not a legitimate intrusion in the marketplace by government. The implementation of the FTA, far from resolving these differences, is more likely to stimulate them by adding to pressures for policy harmonization. Those pressures will have important ramifications in the contentious area of industrial policy.

Taken in its widest sense, industrial policy can be defined as the direction and nature of the sum of a country's public and private efforts to shape economic activity and to influence growth. While the virtues of markets are everywhere hailed, few countries, or jurisdictions within them, and certainly not the most rapidly growing, are willing to forego the notion of seeking to shape, at least strategically, the nature and directions of growth. Industrial policy therefore includes a concern not only for its traditional subjects -- the manufacturing sector -- but also for the service sector, for finance, research and development, and education.

Many international trade professionals today believe that a country's industrial policy should be based on a concept of dynamic comparative advantage[130] -- on managed competitiveness -- either because they think it the best strategy, or because it is necessary, since very few governments profess to believe in the theory of totally unfettered free trade and fewer still practice it.

Industrial policy can range from the state-centred, plan-driven approach, where the government intervenes directly in all or part of the economy, to the fully market-driven approach, where an "invisible hand" is relied on to assure that decisions, made by the market on the basis of private interest achieve, the maximum good for the whole public, and where government involvement, if any, is restricted to the protection of property rights. Between these two extremes, however, there is a very wide range of framework and incentive policies that compose various conceptions of industrial policy.

Not only does industrial policy encompass this wide range of possibilities and various policy measures, but it can and is engaged in by a variety of institutional bodies, including private firms as well as governments and crown corporations at all levels.

All countries can therefore be seen to have "industrial policies", albeit made effective in different ways. One study on the issue tried to define several different national approaches used in recent years: through informal administrative guidance and credit subsidies (Japan); a heavy reliance on direct subsidy (the EC); trade protection (Australia); or

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[130] Neoclassical economics defines comparative advantage as a more static force, which derives from a country's endowments of resources, labour and capital and a search for the most efficient way of exploiting their specific configuration. "Dynamic comparative advantage" suggests that countries can choose the industries or sectors in which they wish to be competitive by shifting the patterns of competitive advantage within their boundaries to favour one factor over another, or to promote a particular sector, industry or firm.

through direct government involvement in production (France)[131]. Other countries view many U.S. programmes such as defence-related R&D financing, the industrial planning offices maintained by at least forty states, and import restricting policies such as sugar quotas or the Multi-Fibre Agreement, as being a part of what constitutes industrial policy.

Many opponents of the FTA believe that the ability of Canada to chart an industrial policy course opposite to, or even slightly different from that of the United States will be diminished by the FTA. Some fear that under the FTA Canada's future direction will be left to the vagaries of the market-place, with no opportunity for the government to steer things.

For instance, under the terms of the FTA Canadian governments can no longer set up a two-price system for oil to foster energy intensive industry to locate here, or to encourage further processing in Canada, and instead must make the resource available to Canadian and U.S. buyers at the same price. For many others, this was the very intent of the FTA -- they choose to believe that the free market is the best way to set energy prices and to determine avenues of future growth.

One of the principal ways governments have encouraged industrial and economic development has been the use of subsidies. In an increasingly interdependent world, and particularly in a new integrated Canada-United States market, many of these practices can have an effect on international trade, even if the programme or practice was not designed with that intent. Canada and the United States hope that the on-going negotiations will be able to develop a set of agreed rules relating to subsidy practices. To the extent that these negotiations are successful, industrial policy differences will not be so much limited as defined -- governments can choose to operate outside of the agreed rules if they wish, knowing what the down-side costs that may be imposed by the other party will be.

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[131] KELLY M., et al, 1988, Issues and Developments in International Trade Policies Occasional Paper #63. Washington, D.C.: IMF.

5.6 SUBSIDY NEGOTIATIONS

One of the hopes of the Government and the trade negotiators was that a definition of what constitutes a subsidy -- which government practices are acceptable, and which are not -- would be a part of the FTA. The goal was to define what "trade distorting subsidies" means, to set a timetable for the elimination of such subsidies, and to end the perceived need for countervailing actions against each other.

This question proved so difficult during the negotiation of the FTA in 1987 that it was set aside. A five- to seven-year period was provided in the FTA for completion of the negotiations on the subsidy issue. Chapter Nineteen set out new binational, but temporary, dispute settlement mechanisms to deal with particular conflicts which may arise while these negotiations are in progress[132].

Both the Minister for International Trade, Mr. Crosbie, and his Deputy Minister on numerous occasions have stated that only subsidies which are countervailable will be on the negotiating table. In their view then, medicare, social programmes, regional development incentives, and other generally available subsidies would be excluded. However, no definition of what is countervailable has yet been commonly agreed to in the international community, nor are the Canadian and U.S. views necessarily in harmony.

There is no explicit definition in U.S. legislation of what a subsidy is, and the provisions of the new U.S. *Omnibus Trade and Competitiveness Act* increase the already wide possible grounds for countervail actions. It might be noted in passing that Canada's *Special Import Measures Act* includes a definition of subsidy as broad as that in the U.S. legislation.

Since the effect of lower tariffs under the FTA may be to increase some Canadian exports to the United States at the expense of domestic producers there, the harassment to which Canadian exporters have in the past been exposed is likely to be increased. Accordingly, concluding negotiations on what constitutes a subsidy as soon as possible should be a major Canadian policy goal.

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[132] These DSMs will not make determinations as to what is or is not a subsidy, but rather will assess the propriety of the application of existing national trade remedy laws.

5.7 TAXATION POLICY

Some critics of the FTA also suggest that changes to Canada's income tax system is a form of policy harmonization that can be linked to the FTA. In fact, it was the present government's intention prior to the negotiation of the FTA to bring the levels of taxation more into line with those in the United States where possible in order to maintain a competitive position and to create "a level playing field" for new investment opportunities.[133] While tax harmonization may therefore not be a product of the FTA, the increased integration of the Canada-United States market under the FTA will increase the pressures to bring taxation policies and practices into line or to make the effects equivalent.

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[133] As discussed in **4.1** and **4.2.5** above.

5.8 ENERGY

The energy chapter of the FTA and the subsequent amendments to the *National Energy Board Act* had as their driving credo the desirability of limiting the power of the authorities, on either side, to interfere in private energy markets. The limits imposed involve three main features:

- exports cannot be restricted except in a period of restraint and then subject to proportionality;
- export taxes are forbidden; and
- prices are to be determined by market forces. The imposition of minimum prices is forbidden.

As well, a further amendment to the *NEB Act* declares that the FTA is preeminent if the NEB "in exercising its powers and performing its duties" finds that its "powers and duties" as otherwise defined are in conflict with the FTA.

Nonetheless, the NEB, under its market procedures for licencing new applications for the export of natural gas, in November, 1989, found insufficient benefit to Canada in four applications to export gas through eastern Canadian outlets to the north-east U.S. market and denied the licences. Given the transport costs to eastern Canada, and given the extremely competitive struggle for the north-eastern market, the net price being charged to American contractors was too low, in the NEB's view, to afford any net benefit to Canada. The applicants were quick to charge that the NEB had violated the proscription against minimum prices in the FTA.

In response to the storm which its decisions have raised, the NEB has called for public hearings in the spring to hear testimony on its application of cost/benefit analysis to the assessment of the export applications. Whether or not net benefits to Canada can or cannot be demonstrated, one of the central questions to be answered concerns whether the NEB any longer has the right to deny a licence essentially on price grounds.

6.0 DISPUTE RESOLUTION: NEW MECHANISMS FOR OLD PROBLEMS

It is contended by supporters of the FTA that the provision of a new dispute settlement mechanism is one of the major accomplishments of the Agreement. Indeed, the inclusion of mandatory action, potentially binding decisions, and firm timetables directly address the most central concerns expressed about the adequacy of existing GATT mechanisms to solve disputes.

The mere inclusion of procedures guarantees neither their use nor their use in any particular way. Much room remains for both countries to continue past practices of delay, to bargain outside the rules, and to bring harassing actions under existing rules. Monitoring how current disputes are dealt with under the new rules, as well as the attitudes of the two governments to their use, are paramount in determining the value of the new procedures.

Canada has stated its intention to honour its commitments and urged the establishment of binding dispute settlement provisions during the negotiations precisely for the purpose of ensuring that both sides do so. Chapter 18 and 19 do not go as far as Canada had hoped and the limits imposed by the bilateral arbitrations, agreements or settlements that do emerge may be narrower than many groups or industries anticipated.

The first two Chapter 18 panels, and a Chapter 18 dispute which is before a select working group, are discussed below. Other potential Chapter 18 disputes are listed in Section 2.2.3 above. A number of Chapter 19 cases are also discussed below. A full list of disputes being considered by panels under Chapter 19 is attached as Annex I.

6.1 CHAPTER 18 DISPUTES

6.1.1. West Coast Fish Landing Regulations

The first test of the new Chapter 18 panel procedures began in May, 1989 when the United States requested an examination of Canada's new fish landing regulations. This bilateral dispute had begun some time earlier, in April, 1986, when the USTR initiated a Section 301 investigation into Canada's export prohibition on unprocessed salmon and herring. As part of this process a complaint was brought to the GATT, where, in March of 1988, a determination was made that these provisions were contrary to the GATT. Canada undertook to bring its rules into conformity with GATT requirements at that time.

As a result of a failure on Canada's part to implement those changes by 1989, the USTR completed the 301 investigation, confirming the GATT finding that Canada's regulations violated U.S. rights under the GATT, and proposed retaliation against a range of Canadian products. Shortly afterward, on April 26, 1989, Canada announced new fish landing requirements which it said were GATT consistent. Canada stated that while unprocessed fish still would have to be landed in Canada, this was to be required solely for management and conservation purposes.

However, the United States disputed this assertion, claiming that the landing rules were, in reality, an export prohibition designed to protect jobs in Canada.

The United States then asked for consultations under the FTAs new dispute settlement provisions. A panel was established and asked to report by September 1, 1989, a deadline later extended, at the panel's request, to September 30, 1989. The United States agreed that it would suspend further action under Section 301 until the panel completed its work.

The panel submitted its finding to the two governments at the end of September, where it remains under consideration.

The panel found that the 100 per cent landing requirement that Canada had imposed was not justified. It said: "As presently constituted, Canada's landing requirement is a restriction on *sale for export* within the meaning of GATT Article XI:1 and hence *prima facie* is incompatible with Canada's obligations under Article 407 of the Free Trade Agreement"[134].

However, rather than stopping there, as GATT panels generally would, the Binational Panel made a further recommendation a part of its findings: "that Canada could bring its landing requirement within Article XX(g) by structuring it along the lines described in Paragraph 7.40 [which says] one way that a landing requirement could be considered *primarily aimed at* conservation would be if provision were made to exempt from landing that proportion of the catch whose exportation without landing would not impede the data

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[134] *In the Matter of Canada's Landing Requirement for Pacific Coast Salmon and Herring* Final Report of the Panel October 16, 1989. Mimeo. p. 54.

collection process."[135] The panel suggested that an 80 per cent to 90 per cent landing requirement for each fishery or related fisheries could be acceptable as a conservation measure.

While both countries claimed victory, portions of the fishing industry on both sides saw defeat: if the landing requirements were altered to reflect the full findings of the panel, Canadian shore workers would not have exclusive right to fish caught in Canada, nor would U.S. processors have unrestricted access to Canadian fish.

However, at the same time that the Canadian government was indicating that it was prepared to lower its landing requirements to 90 per cent, U.S.T.R. Carla Hills indicated that complete removal was required, since the panel had found the landing requirement inconsistent with GATT and FTA obligations.

At the November meeting of the Commission, both Hills and Crosbie softened their positions somewhat: Hills no longer demanded complete withdrawal and Crosbie indicated he would consider a somewhat lower landing requirement.

No final agreement has yet been reached on the adoption of either the panel report or an alternative solution. Chapter 18 panel decisions are binding only if both sides agree in advance. In this case, neither side to the dispute requested that the panel's findings be binding, and therefore are not obligated to adopt its report or to act on its recommendations. Since both sides had made a general commitment to follow the new FTA procedures, and this is the first dispute panel under the new rules, it was hoped that the panel findings would be implemented.

If Canada fails to implement changes that are acceptable to the United States, the U.S.T.R can resume its action, under Section 301 of the Trade Act, against Canada and take any retaliatory steps it deems necessary. Since the panel has found that a 100 per cent fish landing requirement is inconsistent with Canada's obligations, to avoid retaliation from the United States some portion of B.C. fish will have to be offered directly on the world market. While this may increase the income of the owners of the fishing licenses, given a fixed quota of fish to be landed, shore-based processors, who face higher labour costs than do their United States counterparts, may find themselves outbid for Canadian fish. Either wages will have to lowered in Canadian plants or jobs will leave the country. While this may be more economically efficient in the aggregate, it does present problems for an established industry in a remote region, as well as for a government which said that it would protect <u>all</u> these jobs and has committed itself to adjustment assistance for all those whose livelihoods are damaged by the FTA.

As well as testing the speed and fairness of the new dispute settlement mechanisms and the willingness of the governments to implement or accept adverse decisions, the fish dispute raises several other important questions.

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[135] *Ibid.*, p. 54 and p. 53.

It appears that the FTA has imposed limits additional to those of the GATT as to practices which will be tolerated in the management of natural resources. For example, while Canada makes extensive use of licensing, fees, and quotas to manage and market a number of its natural resources and farm products, any new programmes or requirements must be consistent not only with existing GATT requirements, but must also not alter, nullify or impair any rights or obligations under the FTA.

6.1.2 U.S. Lobster Sizing Requirements

An attempt by the U.S. Congress to extend U.S. conservation measures, designed to restrict the landing and sale of small-sized lobsters, to include lobsters caught in Canada was rejected during the passage of the U.S. implementing legislation. However, in late 1989 a bill containing similar provisions[136] was passed by Congress.

The Canadian government petitioned the President to veto the bill, or to ensure the exclusion of the provisions on lobster size, but President Bush signed the bill into law on December 12, 1989. It is estimated that between $30 million and $100 million of Canadian lobster exports will be affected by the law.

The Canadian government immediately issued a complaint to the Trade Commission and requested a Chapter 18 panel review of the consistency of the new U.S. law with the obligations of the FTA. The substance of the Canadian complaint flows from the contention of many Canadian fishermen that, given the ideal conditions in certain Canadian waters for the reproduction and rapid growth of lobsters, a law such as the U.S. law is unnecessary as a conservation measure; consequently, they believe that the U.S. law is intended, not to protect Canadian or Maine lobsters from undesirable fishing, but to protect Maine fishermen from competition from Canadian fishermen with a natural comparative advantage.

The Commission agreed to an expedited schedule for review, as they had done for the West Coast Landing Requirements case, and it is expected that the preliminary report of the panel will be completed in April, with the final report to be given to the two governments in May, 1990.

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[136] See *Inside U.S. Trade* September 8, p. 9.

6.1.3 Plywood Panel Standards

The United States has delayed implementation of tariff reductions on plywood and several other classifications of manufactured wood panel products due to a dispute over differences in performance standards for the wood products.

In response to this unilateral U.S. action, Canada has suspended implementation of its tariff cuts on the same products, and requested consultations under Chapter 18 of the FTA.

This dispute has been on the bilateral agenda for quite some time. Indeed, an exchange of letters that forms part of the FTA took notice of the progress of the dispute and provided for the review, upon request by the United States, of the then-pending Canada Mortgage and Housing Corporation (CMHC) decision regarding the approval of U.S. C-D grade plywood in Canada. Article 2008 of the FTA provides for a delay in tariff reductions on the wood panel products, if the panel of experts disagreed with the CMHC findings or if the review was not completed by the time of entry into force of the FTA.

In mid-1989 CMHC announced its decision not to approve the use of U.S. C-D grade plywood on the grounds that it does not meet Canadian product standards. Although the United States objected to the CMHC decision, it also declined to establish the panel of experts called for in the FTA. Likewise, the United States decided to delay the FTA tariff cuts on plywood and the related products. It was able to do this through provisions of the U.S. implementing legislation which authorize the President to begin the tariff reductions only after common performance standards have been "sufficiently incorporated" into building codes in both countries.[137]

Canada contends that the delay in implementing the full tariff cut is inconsistent with U.S. obligations under the FTA since the conditions in the FTA that would have allowed such a delay[138] have not been met. The United States maintains that CMHC did not undertake a full evaluation of plywood and that Canada therefore did not meet its obligations as set forth in the exchange of letters[139].

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[137] In a related matter, on October 3, 1989, the U.S. announced in the *Federal Register* that it intended to alter the tariff classification for tongued, grooved, lapped or otherwise edgeworked plywood unilaterally, putting these products into a separate category of building boards, with a tariff rate of 8 per cent rather than 20 per cent effective October 18, 1989. This restores the tariff to the rate that had applied to this type of plywood prior to the passage of the *Omnibus Trade and Competitiveness Act* in 1988. While this brings the classifications into conformity with the FTA, the dispute over the complete removal of the tariff remains unsolved. See *Inside U.S. Trade* October 13, p. 3; October 20, p. 16.

[138] That is, the review of the CMHC decision by a panel of experts.

[139] The United States bases its argument on the claim that it expected the CMHC to undertake physical testing of the U.S. products.

Prior to the implementations of the FTA, the two governments had agreed to develop and implement common performance standards. A bi-national committee composed of technical experts from the industries and standards organizations in both countries was established to undertake this task and to develop acceptable testing methods. It is not clear how long the process will take. Some progress has been made to establish a work program, but little else. While the work of this committee to develop a common plywood performance standard offers the best long-term solution to the underlying standards issue, it does not represent a solution to the current FTA tariff dispute.

The U.S. industry contends that Canadian plywood standards are designed to keep U.S. C-D grade plywood out of the Canadian market. Canadian producers respond by noting that the U.S. industry has not pursued the issue under international trade law, nor has it applied for a change in the Canadian standards, which are set by standards-making bodies, testing laboratories and the companies concerned, including foreign ones. Furthermore, they infer that by resisting the separation of the C-D grade from C-C grade standards, the U.S. industry is attempting to limit Canadian exports by ensuring the continuation of its 20 per cent tariff on the larger quantity of wood[140].

The first round of consultations was held, at the official level, on January 31, 1989. Subsequently, the issue was raised at the March 13 meeting of the Canada-U.S. Trade Commission and again at the November 30 meeting. At the latter meeting the Commission addressed a letter to the expert working group, requesting an expedited conclusion of their work by February 28, 1990. However, no steps have been taken formally to undertake an FTA review utilizing the deadlines and procedures for bilateral review[141].

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[140] C-C grade wood represents about 65 per cent of U.S. consumption. This standard is compatible with the Canadian one, and if the separation was made, both countries could gain entry to a part of the other's currently protected markets. For its part, Canada has maintained a 15 per cent tariff on these products.

[141] It is reported that the panel will not meet this deadline and that the more likely outcome is stalemate and a retention of the tariffs. See *Canada-U.S. Report on Free Trade* January 15, 1990 page 1. Retention of the tariffs by the United States could be subject to a full review by a Chapter 18 panel, should Canada make a formal request for such a review.

6.2 CHAPTER 19 DISPUTES

6.2.1 Red Raspberries

The first of the issues referred to a Chapter 19 panel for review, examining a U.S. International Trade Administration (ITA) anti-dumping order against red raspberries from Canada, has now been reported[142].

The panel found that one of the three companies had been properly subject to anti-dumping duties under U.S. law. In the other two cases the panel remanded back to the ITA its conclusions that home market sales were inadequate to determine the fair market price. The panel instructed the ITA to provide further explanations within 30 days before determining if the evidence that the ITA had used constitutes "substantial evidence" as required under ITA rules.

A number of U.S. practices were reviewed by this panel. The definition of "such or similar" merchandise under the anti-dumping law was scrutinized and the circumstance under which the ITA can disregard sales of such or similar merchandise in the home market and use "constructed value" to determine foreign market value was examined. The panel found that the equation of unlike products (fresh raspberries and bulk-packed raspberries) was properly denied by the ITA and that a constructed value could be used to determine the level of the anti-dumping duty (AD). The panel found that in the other two cases the ITA appeared arbitrarily to have decided on the inadequacy of home market sales of like products.

Giving the ITA a second opportunity to provide reasons, rather than making an immediate ruling that the record does not support the ITA decision, demonstrates a "benefit of the doubt" approach to ruling on previous practices, while at the same time indicating that rules respecting data collection and reasoning will have to be followed, and seen to be followed, rather than relying on arbitrary assumptions.

The panel process took 283 days, 32 less than the maximum allowed by the FTA and about half the usual time required for review through the U.S. courts. However, the remand to the ITA of 30 days was extended, at their request, by ten additional days. The parties to the dispute will have fifteen days to consider the information once it is received. How the panel will proceed following comment is as yet unclear, and estimates range from 20 to 90 more days before the final panel results will be available, for a total of 428 days.

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[142] Article 1904 Binational Panel USA-89-1904-1 *In the matter of Red Raspberries from Canada: Clearbrook Packers, Inc., Marco Estates Ltd./Landgrow and Mukhtiar & Sons Packers, Ltd. v. United States Department of Commerce, International Trade Adminstration.* December 15, 1989.

6.2.2 Pork Production Subsidies

Over the years various U.S. trade courts and tribunals have undertaken investigations of alleged subsidies to Canadian pork producers. In a number of instances the U.S. industry has contended that subsidies paid to upstream producers should also be assigned to downstream products and a countervailing duty (CVD) imposed.

In 1985 one U.S. trade court found that live hogs were subsidized and causing injury, and imposed a countervailing duty. In 1987 the U.S. pork producers petitioned for further relief, this time contending that Canadian pork producers were circumventing that CVD by decreasing exports of live hogs and increasing exports of fresh, chilled and frozen pork. In this case it was determined that there was no direct subsidy paid to pork processors, even if hog producers were subsidized.

Changes to U.S. trade law made by the *Omnibus Trade and Competitiveness Act* of 1988 now allows such a connection to be made. Section 1326 of this *Act* permits the U.S. International Trade Commission (ITC) to examine and emphasize the economic relationship between producers and processors and to conclude that the two constitute a single industry.

A complaint was brought under the new rules and, after a preliminary ruling in which the Commerce Department imposed a duty of $.039 per kilogram based on the subsidy to hog producers, the ITC raised the countervailing tariff to $.079 per kilogram in its final determination of injury caused by fresh and chilled Canadian pork exports.

Several Canadian meat packers had laid off workers on the basis of the lower initial tariff. Shortly after the higher final determination was made, even a relatively new slaughter-house in Springhill, Manitoba, announced that the CVD made it uneconomic to continue its operation, and that it would wind up operations before the end of 1989, laying off its 180 employees. A number of other meat packers and pork producers are also experiencing difficulty.

This matter is being reviewed by no less than three panels: two Chapter 19 panels are examining the CVD and injury determinations, and one at the GATT is examining the compatibility of the U.S. process for calculating the pass through of subsidy with GATT rules. Canada requested the panels immediately after the decisions were made.

While Canadian pork producers are hoping that referral to an FTA panel may reverse the Commerce and ITC findings, the task of such panels is to determine whether national laws have been properly applied. Most observers consider that the *Omnibus Trade and Competitiveness Act* has been properly applied; consequently, the appeal is likely to result in a confirmation of the duty on Canadian pork and pork products.

Moreover, even if the duty were to be overturned on appeal, it could take up to a year for the process to be completed. While this may, indeed, be quicker than under previous U.S. procedures, the duty is being collected in the meantime. The level of the duty is sufficiently high that exports of these products to the United States are being severely affected.

The more promising appeal route for the pork dispute would seem to lie in the GATT because of a previous GATT finding on a related matter. Following a complaint brought by Canadian cattlemen in 1986, the Canadian Import Tribunal (CIT) found that cattle producers and manufacturers of boneless beef in Europe constituted a single industry and initiated Canadian countervailing duties against beef products from Europe. The EC successfully brought a complaint against this action to the GATT in October, 1986 which found that producers and processors constituted two distinct industries. Adoption of this panel finding was blocked by Canada.

Even though an appeal to the GATT would seem to contradict the position taken by Canada with respect to the beef industry, Canada has requested a panel review on those grounds. However, there is no obligation for GATT panels to be consistent; and it could just as easily find one meat to be the product of a single industry, the other not[143].

Chapter 18 provides that once proceedings have been initiated under the GATT or the FTA, recourse can not be made to the other body. However, Chapter 19 has no such prohibition and different aspects of the dispute over pork have been sent to both.

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[143] One of the hopes of some trade lawyers and policy experts is that FTA panel findings will eventually constitute a body of precedent which can then be drawn on to achieve consistency and greater predictability in decision-making.

6.3 EMERGING PROBLEMS

6.3.1 Regional Development

It has been suggested that Canadian programmes designed to foster regional economic development could be threatened by U.S. trade remedy actions and that Chapter 18 review will not be able to prevent this from happening.

Canada and the United States each have a large number of programmes, provisions, and regulations which, while having other stated purposes, also have regional economic effects[144]. Both countries agreed in the FTA negotiations that regional economic development programmes are permissable, but have reserved the right to institute tariffs and other measures against exports to off-set any benefit confirmed by such programmes.

Complaints and actions against these practices should serve, over time, to increase the transparency of their effects on exports to the other country. However, successful countervail duty actions against established programmes which may not be regarded as subsidies by the recipients, and which may have been established for powerful domestic reasons, will also generate bad feelings and tensions between the affected segments of the populations of both countries.

It is important to remember in this regard that the dispute settlement mechanisms (DSMs) do not change existing rules and practices or domestic trade remedy law, but only ensure the proper application of them. If the various U.S. trade courts find Canadian regional development programmes to be countervailable[145], then CVDs will be imposed. The value of the DSMs lie not in assuring market access, but in slowing a further erosion of access through the review of new laws and practices under Chapter 18, and through ensuring that proper research is done and full consideration given to each action through Chapter 19 reviews.[146]

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[144] These include, but are not limited to, Canada's unemployment assistance programmes, which provide greater benefits for seasonal workers, many of whom are concentrated is specific regions of Canada, and U.S. minority entitlement programmes and defence contracting practices.

[145] See **Section 2.5.4 Super 301** above.

[146] As well, the Subsidies and Trade Remedies Working Group may make some progress towards raising the *de minimis* level of countervailable subsidies, which could reduce the threat to many programmes such as these since the absolute level of support provided is often thought to be quite small. See BENCE, J-F., & SMITH, M. 1989 Subsidies and the Trade Laws: The Canada-United States Dimension Ottawa: The Institute for Research on Public Policy. May.

6.3.2 GATT Ice Cream and Yogurt Decision:

At its October, 1989, Council meeting the GATT released a panel report which found Canada's restrictions on the import of ice cream and yogurt products to be inconsistent with Canada's GATT commitments. This panel had been convened at the request of the United States.

After consideration, Canada agreed to the adoption of the report, but indicated that its findings would not be implemented until the end of 1990 when the Uruguay round of the MTN is completed.

This decision may have an impact on some of Canada's market management mechanisms, which make extensive use of quotas to regulate production. Maintaining the system in many sectors of the agriculture industry requires a defined market for the goods, a market which in many cases depends on import restrictions on down-stream products using managed products as inputs. If this issue is not resolved in the current GATT negotiations, Canada could find itself subject to more such GATT actions, and the United States could make use of FTA mechanisms to achieve enforcement.

It should be noted that the United States is not subject to the GATT on similar matters, since it sought and received a waiver for its own agricultural practices from the GATT in 1955.

6.3.3 Ontario Provincial Trucking Regulations:

The Ontario government has recently decided to allow longer truck semi-trailers. However, the legislation has not yet been approved by the Ontario legislature and interim regulations allow the use of the longer trucks, but only if they are Canadian-made. This interim change was made to ensure continued sales by Ontario-based manufacturers which were experiencing a loss of sales while the industry awaited the new legislation. U.S. manufacturers and truckers have objected that the interim regulation is a trade distorting measure.

6.4 JUDICIALIZATION

Whatever the final results of these specific cases, it is important to keep in mind that:

- once a review is undertaken and a decision has been made, the case can not be brought again unless the relevant legislation is changed; and

- any changes to the law are themselves subject to FTA review.

The down side of this first provision is that cases must be prosecuted correctly the first time. Vigilance must be maintained to ensure that no opportunities are missed to take action against the existing or future practices of the other side.

While this may seem to be less than co-operative, it has often been the case that factors external to specific cases have played a larger role in determining the initiation and progress of complaints than have the central concerns of an industry with specific complaints. The new Canadian provision allowing companies and individuals to bring actions directly to the CITT should reduce this tendency somewhat, but it must be noted that governments still retain the exclusive right to prosecute the final appeals.

Finally, it had been hoped that by judicializing the process, building in firm deadlines and timetables, and by placing the process in an international forum, the role of politics in the process could be reduced. As noted above in section 2.2.3 Dispute Settlement, there still is room for much political interference. An examination of the current cases between Canada and the United States indicates that the delay, consultation, and negotiation that have been a feature of the past treatment of disputes will likely remain. Once again, rather than utilizing the mechanisms as designed, bargaining and negotiation have delayed resolution and each side has resorted to unilateral action to try to have its way. The early experience with the new procedures suggest that some of the intentions of the FTA negotiators may be abrogated by those seeking protection or delay.

Similar situations exist with respect to border broadcasting provisions[147], the U.S. system of classification of wool products, and a number of the Canadian practices which were listed in the U.S. Super 301 inventory of items for priority action noted above[148].

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[147] Both countries have brought complaints in this area.

[148] See 2.5.2.3 Canada and Super 301.

7.0 OTHER TRADE RELATED DEVELOPMENTS

At many points throughout this report it has been noted that the Canada-US FTA is but one response to change in the global trading environment, and that to properly understand the effect and impact of the FTA, as well as the reason behind the initiative, it is necessary to be aware of some of those other significant events and forces. This short section outlines some of the major forces currently at play in the global trading system, developments which will have a key role in the success or failure of Canada's international trade policies.

Rather than trying to present a great deal of information about events and changes which are very broad in scope, this section attempts only to provide a short overview of the most recent developments and what Canada's response has been. These include Europe 1992, the Uruguay Round of Multilateral Trade Negotiations, and growth in the Asia-Pacific region.

7.1 EUROPE 1992

Europeans have sought to ameliorate the effects of global structural disequilibrium and to promote adjustment through a new and increased emphasis on the European Community and its various institutions. Among the twelve member countries of the EC, this process has culminated in what is described as "completing the internal market", "Project 1992", or simply "1992".

The establishment of a common market in Western Europe began in 1957 with the signing of the Treaty of Rome by the original six members of the European Community. The 1992 Project represents the most recent reforms of the treaty and calls for the eventual elimination of all remaining barriers to trade between the twelve. "Project 1992" consists of 285 measures which are in the process of being considered by the European Commission. These measures flow from the ratification of the Single European Act (SEA) in 1987 and are to be negotiated and adopted before the end of the current Commission's mandate on December 31, 1992. The proposed measures are of four types:

- dismantling all non-tariff barriers among EC member states[149];
- allowing the provision of services, including financial services, by European nationals and companies anywhere in the Community;
- harmonizing[150] company law throughout the EC; and

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[149] All tariffs were abolished during the early 1960s.

[150] In the EC, "harmonization" means to "make identical".

- opening procurement by governments within the Community to free competition among Community firms.

Many of these 285 measures already are in place and in force, each measure coming into effect after the passage of only required implementing legislation in all member states.

It is difficult to determine at this time, over halfway to 1992 from the inception of the initiative, if the most contentious of the measures will gain sufficient support -- whether all the hopes and predictions about the levels of integration and co-operation will come to pass. For example, the Social Charter, which has been vehemently opposed by Prime Minister Margaret Thatcher in particular, will probably emerge in the form of "recommendations" rather than the more binding directive that had been hoped for by some and a significant amount of opposition has also developed with respect to the standardization of levels of indirect taxation.

Whatever its final form, completion of the internal market will entail considerable adjustment and investment by European business. Many non-Europeans fear that pressure is building within the EC to exclude outsiders from benefits they will have done nothing to earn, or that any benefits to outsiders will have to be paid for through reciprocal arrangements. This may be a significant problem as the Commission has defined reciprocity to mean that it "reserves the right to make access to the benefits of 1992 for non-EC firms conditional upon a guarantee of similar opportunities, or at least non-discriminatory opportunities, in those firms' own countries". The EC Commissioner for External Trade has stated that "where international obligations do not exist, as for example in the field of services, we see no reasons why the benefits of our internal liberalization should be extended to third countries".

Beyond 1992, the Commission recommends further action towards the full integration of Europe, including economic and monetary union, a common commercial policy, and the establishment of regional development programmes to promote less developed regions and regions in decline[151]. Negotiations have also been held with EFTA (the European Free Trade Association) to discuss the future relationship between the members of the two organizations.

Even without active protectionism in the form of a "Fortress Europe", Canada and Canadian producers will still face a more competitive environment. They will meet stiffer competition from rationalized and more efficient European firms both in the European market and at home as those firms, together with U.S., Japanese, EFTA and developing country firms, all seek a share of a more competitive global market.

It is also likely that Canadian companies will be subject to much stronger competition from non-Community companies operating in Europe. For instance, many American, Japanese,

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[151] COMMISSION OF THE EUROPEAN COMMUNITIES 1989 Europe Without Frontiers: A Review Half-Way to 1992 Brussels: CEC. July.

Swedish and other EFTA firms already have positioned themselves in the EC through sharply increased direct investment. This has been done to both benefit from growth within the single market, and to avoid possible protectionist measures against newcomers or outsiders.

To benefit from Europe 92, it will be necessary to raise the profile of these developments in Canada. This process has been encouraged by the Government which has:

- undertaken an in-depth research project on the effects of Europe 92 on Canada; and
- hosted major seminars for business to outline opportunities and obstacles to European trade.

However, in general, many analysts have noted a tendency among Canadian business to wait -- to discover just what Europe 92 will mean if completed -- before acting. It is important that Canada and Canadian business act to ensure that Europe 92, in conjunction with the FTA and the MTN, be used to define and liberalize trade practices, and not merely further the growth of continentalist blocks.

External Affairs has made the EC the second pillar of its Global 2000 Strategy. The EC programme has three principle components:

- a continued emphasis on the GATT as a framework for Canada-EC trade relations;
- the sponsoring of on-going analysis of 1992 to keep Canadian business abreast of new developments as the single market is implemented; and
- an attempt to promote strategic corporate alliances and two-way investment flows, especially in high technology sectors such as aerospace and telecommunications.

Several prominent Canadian firms have taken major initiatives to enter and/or consolidated their position in the European market:

- **Bombardier** has purchased several major transportation-related manufacturers, including BN, the Belgium-based manufacturer of the TGV rail cars, and Short Brothers, the Belfast aircraft manufacturer. These acquisitions enhance Bombardier's presence and access in Europe and complement its Canada based rail and aircraft divisions.
- **Moore Corp** of Toronto, the world's largest business forms supplier, has expanded its European operations through the acquisition of Lithorex SA, bringing its European workforce to over 4,500 persons. Moore has also reorganized its European units, all formerly independent and reporting separately to Toronto, into a single unit with a headquarters Lausanne, Switzerland.

7.2 THE MULTILATERAL TRADE NEGOTIATIONS

7.2.1 Progress of the Uruguay Round:

The Uruguay Round is the eighth and latest round of multilateral trade negotiations (MTN) under the auspices of the General Agreement on Tariffs and Trade (GATT). The negotiating agenda, set out at Punta del Este, Uruguay, in September 1986, includes agreement to negotiate on the most challenging issues facing the world trading system.

While previous negotiations had concentrated largely on tariff reductions, the scope and nature of this round goes far beyond traditional areas. It includes:

- agriculture;
- safeguards, grey area measures, and subsidies;
- extending GATT rules to trade in services; and,
- improved institutional mechanisms to allow the GATT to "monitor and supervise" national trade policies.

While the Montreal mid-term ministerial meeting, in December, 1988, failed to resolve the most contentious issues, eleven of the fifteen working parties did reach agreement, and the remaining four were able to reach a compromise in April, 1989.

While most of these agreements set out frameworks for further negotiations, rather than substantive new rules, procedures or definitions, GATT officials are confident that the MTN will be able to complete its work by the December, 1990, deadline.

Since the April, 1989 meeting, several of the working groups have made substantial progress.

- The group on agriculture has made some headway elaborating the U.S. suggestion for tariffication of existing subsidy programmes[152], although the remaining differences between the EC and the United States remain large.
- The subsidy group is studying a working document, submitted by Canada, which has set out a proposed methodology for defining and monitoring the use of subsidies.

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[152] It had previously demanded an end to all subsidy programmes, a proposal strongly resisted by the EC. Tariffication refers to the replacement of subsidy programmes and quota systems with tariffs of equivalent effect. Tariffs can presumably be reduced, over time, using existing GATT methods.

- A draft agreement on trade in services circulated in the summer of 1989 now has been refined and is expected to emerge in March with a deadline for initial commitments set for May, 1990.

7.2.2 Canada at the MTN:

Canada's objectives at the MTN are coincident with and complementary to the goals of the FTA. These objectives include:

- the improvement of market access for Canadian goods;
- clear and equitable rules for agricultural products;
- reforming the GATT system through:
  - improved dispute settlement mechanisms and
  - international monitoring of national trade policy; and
- developing new rules for trade in services, investment and intellectual property.

Many of these items have been dealt with in a bilateral context under the FTA and provide proof that agreement is possible, while others, still subject to further bilateral negotiation, may be speeded to conclusion by multilateral efforts, proposals, and agreements in the same areas.

Advisory panels that were established during the FTA negotiation, such as the ITAC and SAGITs, have been maintained and are now principally involved with the provision of advice on MTN issues to the federal government[153]

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[153] See Section 2.4.3.2 - ITAC and SAGITs, above.

7.3 ASIA PACIFIC

It is becoming increasingly clear to many Canadians that the Pacific Basin represents a large and growing opportunity for trade. The combined gross domestic product of the Asia-Pacific countries more than doubled between 1960 and 1982. Growth rates since then have exceeded those of the OECD countries and show no sign of abating.

The GNP per capita in Japan, at current exchange rates, already exceeds that of the United States, and at least four of the Asia-Pacific NICs (the newly industrialized countries: Singapore, Hong Kong, Taiwan, and Korea) already have reached or surpassed the GNP per capita of Portugal, Turkey, Ireland, Greece, and Spain.

It is estimated that by the turn of the century, growth in the region will have moved its GNP to over 50 per cent of the world total, and will comprise 40 per cent of world consumption, 60 per cent of the people and 70 per cent of total world trade.

Trade across the Pacific already has increased dramatically. For both Canada and the United States, Pacific trade now exceeds their trade with Europe. At the same time, several of the developing countries in the region, notably Thailand, the Philippines, Malaysia and Mexico are moving to an outward-looking orientation based on industrial production and trade, following the example of Taiwan and Hong Kong towards light manufacturing in labour-intensive consumer goods and will provide competition, as well as markets, for Canadian manufacturers.

However, Canadian business has had a chequered history of success in the Asia-Pacific area. While Canada continues successfully to export raw material to Japan, and has had some success in obtaining direct investment from Japan and Korea, primarily in assembly plants for manufactured goods destined for the domestic market or in extractive resource investments, Canada has failed to penetrate the markets of Asia-Pacific countries with manufactured goods or with services.

To address both the failure of Canadian business as an exporter of high value-added manufactured goods to the Asia-Pacific basin, the Government of Canada has announced that Pacific trade will be one of the "three pillars" of its "Going Global" trade strategy.

The Pacific 2000 Business Strategy includes:

- strengthening and improving Canada's presence and trade representation in major Asia-Pacific markets;

- focusing high-profile trade developments events in sectors offering the greatest potential for Canadian export growth, especially for small and medium-sized firms;

- expanding Canada-Japan science and technology links leading to joint technology development and strategic partnerships in key sectors of domestic priority; and

- improving Asian language skills and awareness to allow Canadian businesses to deal more effectively with opportunities in the region.

It is widely perceived in Asia-Pacific countries that developments in Europe and North America are leading to a "bloc-oriented" trading system. The Prime Minister of Australia, Mr. Hawke, has been encouraging a dialogue on a Pacific basin trading group as an offset to this trend, to ensure that Asian nations have secure access to a sufficiently large market for economies-of-scale in production.

Australia's regional economic co-operation initiative was expanded in July, 1989, to include Canada and the United States. Canada has offered support to this initiative. A Ministerial meeting held in Canberra during the first week of November, 1989, was attended by trade ministers from twelve countries to discuss this proposal. These were Australia, Canada, Japan, New Zealand, South Korea, the United States, and the six members of ASEAN[154]. This group agreed that emphasis should be placed on a successful completion of the Uruguay Round, that the role of the group should be complementary to the ASEAN, and that it should not, at this time, move towards becoming an OECD-like organization in the Pacific.

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[154] Indonesia, Malaysia, the Philippines, Singapore, Thailand and Brunei.

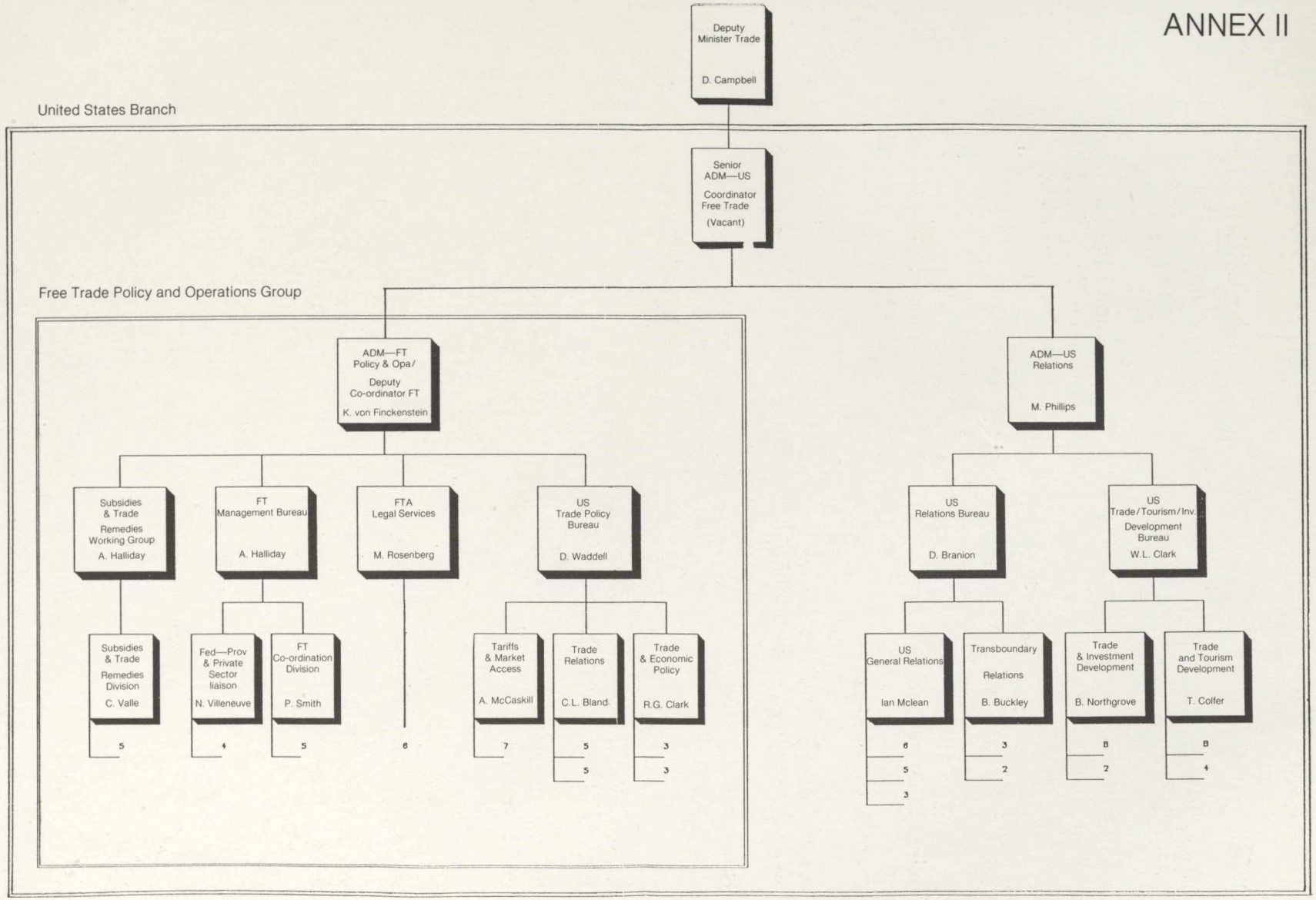
LIST OF PANELISTS NAMED FOR ALL CASES

AMERICAN	CANADIAN
1. USA-89-1904-01 (Red Raspberries)	
Robert Charles Cassidy Jr. Warren E. Connelly	Peter Clark Glen A. Cranker Ivan Feltham (chairman)
2. USA-89-1904-02 (Replacement Parts No.1)	
William (Bill) Alberger (chairman) Thomas Graham Theodore W. Kassinger	Donald Brown C.J. Michael Flavell
3. USA-89-1904-03 (Replacement Parts No.2)	
William (Bill) Alberger Thomas Graham Theodore W. Kassinger	Donald Brown C.J. Michael Flavell
4. USA-89-1904-04 (Codfish)	
John D. Greenwald (chairman) Donald deKieffer	John M. Coyne John Richard Prof. Gilbert Winham
5. CDA-89-1904-01 (Polyphase Motors)	
Prof. Diane P. Wood Prof. William J. Davey Jospeh E. Pattison	Robert Pitt Margaret Prentis
6. USA-89-1904-05 (Replacement Parts No.3) (Amd't to Adm Rev)	
William (Bill) Alberger Theodore W. Kassinger (chairman) Thomas R. Graham	Donald J.M. Brown C.J. Michael Flavell
7. USA-89-1904-06 (Fresh, Chilled and Frozen Pork) (Final Affirmative Countervailing Duty Determination)	
Joel Davidow Dennis James Jr.	A. de Lotbiniere Panet Margaret Prentis

Mark Jeolson

AMERICAN	CANADIAN
8. USA-89-1904-07 (New Steel Rail) (Final Affirmative CVD Determination)	
David Gantz Michael Sandler	Gerald Lacoste John D. Richard Gilbert Winham
9. USA-89-1904-08 (Steel Rail/Algoma) (AD Determination) (Final Determination of Sales at Less than Fair Value)	
William P. Alford Gail T. Cumins Lawrence R. Walders	Albert L. Bissonnette E. David D. Tavender
10. USA-89-1904-09 (Steel Rail/Sysco) (Injury) (Final CVD Injury Determination)	
Morton Pomeranz Italo H. Ablondi	Martin Freedman Richard Gottlieb Margaret Prentis
11. USA-89-1904-10 (Steel Rails/Algoma) (Injury) (Final AD Duty Injury Determination)	
Morton Pomeranz Italo H. Ablondi	Martin Freedman R. Gottlieb M. Prentis
12. USA-89-1904-11 (Pork) (Injury) (Final CVD Injury Determination)	
Thomas Schaumberg Kathleen Patterson	Simon Potter E. David Tavender John Whalley

amended January 3, 1990


Deputy Minister Trade
D. Campbell
United States Branch
Senior ADM—US
Coordinator Free Trade
(Vacant)
Free Trade Policy and Operations Group
ADM—FT Policy & Opa/ Deputy Co-ordinator FT
K. von Finckenstein
ADM—US Relations
M. Phillips
Subsidies & Trade Remedies Working Group
A. Halliday
FT Management Bureau
A. Halliday
FTA Legal Services
M. Rosenberg
US Trade Policy Bureau
D. Waddell
US Relations Bureau
D. Branion
US Trade/Tourism/Inv. Development Bureau
W.L. Clark
Subsidies & Trade Remedies Division
C. Valle
Fed—Prov & Private Sector liaison
N. Villeneuve
FT Co-ordination Division
P. Smith
Tariffs & Market Access
A. McCaskill
Trade Relations
C.L. Bland
Trade & Economic Policy
R.G. Clark
US General Relations
Ian Mclean
Transboundary Relations
B. Buckley
Trade & Investment Development
B. Northgrove
Trade and Tourism Development
T. Colfer
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