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Canadian Foreign Policy

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Min. des Affaires étrangères
July 1982
OCT 21 1987
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RELATIONS BETWEEN CANADA AND THE U.S.A.

The Magnitude and Complexity of the Relationship

No other two countries have so complex and extensive a relationship as Canada and the United States. They are each other's largest supplier and customer. They co-operate in the defence of the North American continent and through the North Atlantic Treaty Organization, Western Europe as well. They share and manage an environment along a 9000 kilometre border. Canadians and Americans are linked by countless personal, family, academic, cultural, professional, business and trade union ties. The two countries are each other's largest source and destination of tourists, with over 73 million border crossings in 1981. The bilateral relationship is based on abiding friendship and mutual benefit and, in many respects, sets the standard for the civilized conduct of international relations.

Management of the Relationship

Although most contacts between Americans and Canadians take place outside the government sphere, management at that level is essential to the harmony of the relationship. The Prime Minister and the President, who are the central figures in this management, are assisted by their respective Cabinet colleagues and officials. The embassies and diplomatic services of the two countries are their permanent representatives and their principal channels of communication on policy matters. Bilateral agreements, arrangements and understandings cover numerous subjects. Cross-border regional relations are also close between Canadian provinces and American states within their areas of jurisdiction.



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Canadian Representation in the USA

In addition to the embassy in Washington, Canada maintains 14 consulates-general in the USA (Atlanta, Boston, Buffalo, Chicago, Cleveland, Dallas, Detroit, Los Angeles, Minneapolis, New Orleans, New York, Philadelphia, San Francisco and Seattle). The consulates-general represent Canada in their territories and implement general relations, trade, immigration, tourism, consular and cultural programs. Several Canadian provinces maintain non-diplomatic offices in the USA.

Trade

In 1981 two-way trade totalled almost Cdn \$110 billion. The value of Canadian exports to the USA was Cdn \$55.5 billion, about two-thirds of total Canadian exports. Canadian imports from the USA were valued at Cdn \$54.3 billion or about 17 per cent of all US exports. The USA sells almost as much to Canada as it does to the entire European Community and almost twice as much as it does to its next largest single trading partner, Japan. Almost 70 per cent of all Canadian imports come from the USA. The scale of this economic interdependence means that economic policies in one country can have a significant impact on the other.

Full implementation of the results of the Multilateral Trade Negotiations will substantially benefit bilateral trade. It is estimated that over 90 per cent of Canadian exports will enter the USA at tariffs of five per cent or less and almost 80 per cent duty free. The agreements reached on such non-tariff measures as subsidies, countervailing duties, and product standards should serve to make market access between Canada and the USA more secure. Similarly, the strengthened General Agreement on Tariffs and Trade (GATT) dispute settlement procedures should provide a means to resist protectionist pressures, as should the efforts to reinforce and extend the multilateral trading system that will be undertaken in connection with the ministerial level meeting of the GATT contracting parties later this year.

Nonetheless, increasing US federal and state "Buy America" legislation and small business set-aside programs have been a source of concern in Canada for

their restrictive effect on access to the US market. US International Trade Commission investigations of Canadian potato and lumber exports to the USA have been sending protectionist signals to Canada. Other sources of concern are: the proposal to further restrict uranium imports into the USA; the continuation of the Domestic International Sales Corporations (DISC) which has been found to be contrary to US GATT obligations; a number of narrow "reciprocity" bills now before Congress, one of which, if passed, would disrupt cross-border trucking trade by discriminating against Canadian carriers; and a bill which would divert maritime cargo from Canadian to US ports.

Canada and the USA have a free trade arrangement in the automotive sector under the auto pact signed in 1965. In 1981 bilateral automotive trade reached \$22 billion, or one quarter of total two-way trade. However, this sector poses problems for Canada. Canada experienced a deficit of over Cdn \$3 billion in 1979 and over \$2 billion in 1980 and \$1.7 billion in 1981 in automotive trade with the USA (Statistics Canada, customs basis). While Canada normally has a surplus in assembled vehicles trade, the over-all deficit and the growing deficit in the high technology, skill-intensive parts sector is cause for concern.

Investment

Canada and the USA are the foremost destination for each other's foreign investment. The USA has about Cdn \$70 billion in direct and portfolio investment in Canada, and Canada has an estimated Cdn \$13 billion in the USA. Other foreign investment in Canada is estimated at Cdn \$26 billion, for a total of Cdn \$96 billion. Some 80 per cent of all foreign direct investment in Canada is of US origin, controlling about 24 per cent of Canadian non-financial industries. Canadians account for 15 per cent of all foreign direct investment in the USA, controlling less than .5 per cent of US non-financial industries. By sector the comparative Canadian and US situations are as follows:

Canada

(Source: Statistics Canada, data to end of 1979), based on asset values)

	<u>% of Industry Foreign Controlled</u>	<u>% of Industry US Controlled</u>
Mining	38.3	30.1
Oil and gas	62.7	47.4
Total Manufacturing	45.6	34.1
Rubber industry	90.4	68.6
Transportation equipment	73.4	68.4
Chemicals industry	76.5	59.4

	<u>% of Industry Foreign Controlled</u>	<u>% of Industry US Controlled</u>
Electrical equipment	60.0	47.5
Heavy machinery	55.4	46.7
Textiles	55.6	43.9
Metal fabricating	36.5	29.2
Pulp and paper	38.6	30.5

Note: The Petroleum Monitoring Agency of the Department of Energy, Mines and Resources considers data based on upstream production revenues to be a more accurate indicator of foreign ownership and control in the oil and gas sector. On this basis, foreign control was 79.5 per cent in 1979 and 77.7 per cent in 1980 (US control 64.1 per cent).

USA

(Source: U.S. Department of Commerce, data to end of 1974)

	<u>% of Industry Foreign Controlled</u>
Agriculture, forestry and fish	0.5
Mining	5.0
Oil and gas	18.0
Manufacturing	3.0
Construction	0.5
Transportation, communications and public utilities	1.0
Wholesale trade	3.0
Retail trade	1.0

The effects of the high degree of foreign participation in the Canadian economy have long been the subject of national debate in Canada. A result of this historical process was the establishment of the Foreign Investment Review Agency (FIRA) in 1974. The US private sector and, more recently, the US government have expressed concern about certain aspects of its operations. Bilateral discussion has taken place within the context of the GATT and the two parties have agreed to the examination of certain FIRA practices by a GATT panel. Canada has been and remains open to discussion and explanation of its policies. However, the reasons behind the Canadian approach are fundamental - a level of foreign ownership and control in its economy which is unique among industrialized countries and a need to ensure that foreign investment brings significant benefit to the Canadian economy.

Although foreign investment levels in the USA are very modest in comparison to Canada's, the USA has itself taken measures to restrict it in certain key sectors of the economy such as coastal shipping, aviation, broadcasting, telephones and telecommunications and nuclear and hydro-power generating facilities. Many states have restrictions on foreign investment in specific sectors. Apart from outright prohibitions, the USA also has indirect controls on foreign investment, including anti-trust laws, Congressional lobbying and monitoring by such bodies as the Committee on Foreign Investment in the United States.

Energy

Energy issues continue to be an important focus of national and international attention and to figure prominently in Canada-USA relations. While both countries are pursuing their respective domestic programs, there is a continuous process of consultation and co-operation in areas of mutual benefit.

The Canadian government's basic energy policy is set out in its National Energy Program (NEP) of 1980, which is designed to restructure Canada's energy system. The goals are: to be self-sufficient in oil by 1990; achieve an equitable sharing of energy benefits and burdens among Canadians; obtain a higher level of Canadian ownership and control of the energy sector; expand the role of the public sector in oil and gas; and ensure greater industrial benefits from energy

development. The program provides a blueprint to end Canada's dependence on imported oil and to right a system which, if continued, would work against increased Canadian participation in the energy sector and in favour of the largest, mostly foreign-owned petroleum companies. In 1979, for example, 72 per cent of the revenues of the oil and gas industry went to foreign-owned companies at a time when the industry was claiming a constantly increasing share of the nation's wealth. While this program will necessarily affect multinationals operating in Canada, including US companies, it continues to provide foreign investors with terms that compare favourably with those available in most other producing countries. This is all the more so since the Alberta-federal agreement on energy pricing and taxation provides for substantially higher prices than were originally foreseen under the NEP and, therefore, strong incentives to the industry for exploration and development.

Canada, like the USA, must import oil to meet its domestic needs. At the same time, Canada produces significant surpluses in other forms of energy including natural gas, heavy oil and electricity, which are exported to the USA. These exports are not large compared with total US consumption, but earned Canada about \$9.5 billion in 1981 while serving as important and reliable sources of supply in certain US markets.

There are numerous other areas of bilateral co-operation - for example, the Northern Gas Pipeline. Construction of the south-western segment is complete and construction of the south-eastern segment is now well under way. Both segments will be used to export some of Alberta's current natural gas surplus until the northern segments are completed and Alaska gas begins to flow through the pipeline to US markets.

In 1979, the two countries published a joint study on electricity exchanges identifying opportunities for increased trade. They also signed an understanding on tarsands and heavy oil research and development in which the provinces of Alberta and Saskatchewan are full participants. Since 1975, oil has been exchanged across the border to maintain some supplies to certain US refineries while saving on oil transportation costs. Both countries are now looking into the possibilities of further co-operation in base-load electricity exports from Canada and co-ordinated responses to energy-related emergencies.

Canada also co-operates closely with the USA and other nations on international energy questions and related financial issues in multilateral organizations, notably the International Energy Agency.

Environment

Canada assigns high priority to the close monitoring and resolution of transboundary environmental problems, which are of great public concern on both sides of the border. The 1909 Boundary Waters Treaty forms the basis of the water-resource management and environmental relations between Canada and the USA.

There are frequent bilateral consultations and negotiations on a wide variety of projects relating to the transboundary environment. An active and valuable role is played by the International Joint Commission (IJC), established by the Boundary Waters Treaty. The IJC has certain regulatory functions and, at government request, undertakes special studies and makes recommendations.

Under an August 5, 1980 Memorandum of Intent, the two governments agreed to develop a co-operative agreement to reduce transboundary air-borne pollutants. This problem, and particularly the phenomenon known as acid rain, has been identified as a major threat to large areas in both countries. Negotiations to conclude a transboundary air pollution agreement began in June 1981 and are continuing. In February 1982 Canada formally proposed to reduce SO₂ emissions by 50 per cent by 1990, contingent on similar US action, in view of the scientific evidence showing acid rain to be a serious threat to the environment. The US administration take a less urgent view of this threat to the environment than does Canada.

Canada and the USA are committed to co-operative efforts to clean up the Great Lakes under the 1972 and 1978 Great Lakes Water Quality Agreements. The problem of hazardous and toxic waste disposal, particularly in the Great Lakes region, has recently become a matter of increasing concern to Canada. Several bilateral meetings have been held to discuss the issue of hazardous and toxic waste disposal in the Niagara River area. A bilateral toxic committee to monitor the river was established in 1981.

Another major issue is the Garrison Diversion project in North Dakota, which if completed would pollute the Hudson Bay watershed in Canada and endanger

Manitoba's fishing industry. Other subjects of continuing interest are tanker traffic on the West Coast, and the tanker traffic that would be associated with a proposed oil refinery at Eastport, Maine; and the proposed flooding of the Skagit Valley in British Columbia by a US utility company.

Defence Relations

Close co-operation between Canada and the USA during the Second World War established a lasting pattern of joint defence planning. The Permanent Joint Board on Defence, established by the Ogdensburg Agreement of 1940, ensures continuous consultation at the policy planning level on bilateral defence matters. The Canada and the USA are founding members of NATO. The North American Aerospace Defence Command (NORAD) Agreement between Canada and the USA has, since 1958, provided for joint command of the air defence of North America. The Agreement was renewed for five years on March 11, 1981, during the visit of President Reagan to Ottawa. Bilateral discussions continue on plans to modernize North American aerospace defences.

The Canada-USA Defence Development and Defence Production Sharing Arrangements (DD/DPSA) are designed to ensure the maintenance of a long-term balance in reciprocal procurement of defence items and to utilize the industrial, scientific and technological resources of both countries in the interests of continental defence. During his visit to Ottawa in March, President Reagan reaffirmed with Prime Minister Trudeau the importance the two countries attach to the Arrangements as the basis for co-operation in the defence economic field.

Fisheries and Maritime Boundaries

In January 1977, Canada extended its fisheries jurisdiction to 200 miles; the US 200-mile zone came into force in March of that year. The two claims overlapped. It then became necessary to establish a new bilateral framework for fisheries management and co-operation as well as to delimit the maritime boundaries off the East Coast, in the Strait of Juan de Fuca and Dixon Entrance in the Pacific, and in the Beaufort Sea in the Arctic.

On August 1, 1977 the two governments appointed special negotiators to recommend a resolution

of these issues. After 18 months of negotiations, agreement was reached on fisheries management and maritime boundary settlement procedures for the East Coast. Treaties were signed in Washington, D.C. on March 29, 1979. Negotiations on the other three maritime boundaries have been in abeyance pending final determination of the East Coast boundary.

One of the treaties signed in March 1979 provided for the submission of the East Coast boundary dispute to adjudication by the International Court of Justice. It was directly linked to the fisheries treaty, which provided for co-operative management of, and entitlements to, East Coast fish stocks. For two years, the US Senate did not act on the treaties. In March 1981, the Canadian government expressed its profound disappointment when the administration concluded that the fisheries treaty would not receive Senate consent for ratification and withdrew it. On November 20 the two countries nevertheless exchanged instruments of ratification to bring the "de-linked" maritime boundary treaty into force.

US fishery conservation and management in the disputed area of Georges Bank continues to be less effective than Canada considers necessary. The USA's adoption of its first-ever scallop management plan represents some progress, after much increased US effort had brought the resource in the area to a critical state. At the same time, however, the USA is greatly relaxing its management of the Georges Bank groundfish fishery.

In West Coast fisheries, progress has been made as discussions continue towards a comprehensive salmon-interception agreement. In July 1981, Canada and the USA ratified a treaty providing for reciprocal fishing of albacore tuna off the Pacific coast and for reciprocal landing rights at designated ports.

Taxation

A Canada-US Double Taxation Convention was signed in 1980 but has not yet been ratified by the US Senate. One issue delaying ratification concerns the treatment of real estate capital gains. Further bilateral negotiations towards amendments which would bring the Convention into closer alignment with US domestic law will be held early in 1982. If agreement

is reached on these amendments, the ratification process could probably proceed fairly quickly.

Extra-territoriality

A cause of irritation between Canada and the USA is the assumption of jurisdiction by US government and regulatory agencies over persons, property and events in Canada. Examples of US attempts to exercise extra-territorial jurisdiction within the past two years include: the Federal Reserve Board's involvement in certain Canadian bank activities with other Canadian financial institutions; the Inter-State Commerce Commission's efforts to deregulate US railways in a way that could adversely affect Canadian railways in Canada; and proposals to have the Federal Maritime Commission regulate Canadian shipping between Canada and third countries when US cargo or ports are involved.

Although a number of out-of-court settlements were reached last year, the antitrust litigation in US courts launched by US private parties against Canadian and other uranium producers has raised serious concerns for Canada. The Canadian government maintains that in this case the actions of Canadian companies, which were taken outside the USA, and required by Canadian law and policy, should not be reviewed by US courts. Legislation (Bill C-41) has been introduced in Parliament aimed at protecting Canadian citizens and corporations from the effects of extra-territorial rulings by foreign tribunals.

Communications

The Canada-US relationship in the field of communications is the most complex and sophisticated between any two countries. Operational agreements between Canadian and US telecommunications carriers govern transborder telephone, telex, and data traffic and new technologies such as space and computer communications will probably be accommodated through similar arrangements. Relations are characterized by a high degree of co-operation and close co-ordination. However, the different communications policies in the two countries (i.e. the US "open skies and free market" compared to the more "regulated, culturally sensitive" Canadian approach) have given rise to some areas of disagreement. Where these occur, they often reflect

the different economic, political and social circumstances in each country.

An example is the border broadcasting issue. Canadian stations, subject to Canadian content and other Canadian regulations, were having to compete with American stations not subject to such regulations. In 1976 the Canadian Income Tax Act (Section 19.1) was amended to ensure the viability of the Canadian broadcasting industry by giving a tax advantage to the Canadian advertising industry for using Canadian border area television companies. As a result of pressure from a number of US television stations situated near the border, the US administration submitted tax legislation to Congress which would mirror the effects of Section 19.1. A hearing on this proposed legislation was held in May and its passage is expected shortly. Section 19.1 remains an important element of Canadian policy and there are no plans to change it.

Exports

1977	2182.8	50107.7	35.1	21.1
1978	22641.3	42378.7	36.5	21.8
1979	23963.9	42477.7	43.7	22.1
1980	23638.4	38775.9	47.8	22.4

PERCENTAGE CHANGES

WITHOUT CUSTOMS BASIS

WITH USA (CUSTOMS BASIS)

	Exports	Imports	Exports	Imports
1978	+19.2	+18.4	+20.1	+18.7
1979	+21.1	+25.5	+19.2	+22.5
1980	+8.7	+10.0	+7.9	+10.4
1981	+10.2	+14.1	+15.4	+13.0

DISTRIBUTION OF EXPORTS

(4 - 1981)

	Canada	USA
Canada	-	17
USA	68	-
Japan	5	9
EC	11	22

DISTRIBUTION OF IMPORTS

(4 - 1981)

	Canada	USA
Canada	-	18
USA	69	-
Japan	5	14
EC	8	16

CANADA/USA ECONOMIC INDICATORS

GNP

	<u>Canada</u> (Cdn current \$ billions)	<u>USA</u> (US current \$ billions)
1977	208.9	1918.0
1978	230.4	2156.1
1979	262.0	2413.9
1980	289.9	2626.1
1981	340.8	2925.5

CANADIAN TRADE

	<u>TOTAL</u> (Statistics Canada on customs basis; in \$ millions Cdn)		<u>WITH USA</u> (CDA/USA reconciled figures; in \$ billions US)	
	<u>Exports</u> (incl. re-exports)	<u>Imports</u>	<u>Exports</u>	<u>Imports</u>
1978	53182.8	50107.7	33.1	30.3
1979	65641.3	62870.7	38.5	37.9
1980	75963.9	69127.7	42.0	40.7
1981	83698.4	78875.9	n/a	n/a

PERCENTAGE CHANGE

	<u>TOTAL (customs basis)</u>		<u>WITH USA (customs basis)</u>	
	<u>Exports</u>	<u>Imports</u>	<u>Exports</u>	<u>Imports</u>
1978	+19.2	+18.4	+20.1	+18.7
1979	+23.4	+25.5	+19.2	+28.6
1980	+5.7	+10.0	+7.9	+6.4
1981	+10.2	+14.1	+15.4	+12.0

DISTRIBUTION OF EXPORTS (% - 1981)

	<u>Canada</u>	<u>USA</u>
Canada	-	17
USA	66	-
Japan	5	9
EEC	11	22

DISTRIBUTION OF IMPORTS (% - 1981)

	<u>Canada</u>	<u>USA</u>
Canada	-	18
USA	69	-
Japan	5	14
EEC	8	16

TOP TEN CANADIAN EXPORTS TO USA

	1977	1978	1979	1980	1981
1. Passenger autos and chassis					
2. Natural gas					
3. Newsprint paper					
4. Motor vehicle parts, except engines					
5. Trucks, truck tractors and chassis					
6. Crude petroleum	208.9	230.4	262.0	289.9	340.8
7. Petroleum and coal products					
8. Wood pulp and similar pulp					
9. Lumber, softwood					
10. Precious metals					

TOP TEN US EXPORTS TO CANADA

	1978	1979	1980	1981
1. Motor vehicle parts				
2. Passenger autos and chassis				
3. Electronic computers				
4. Motor vehicle engines				
5. Trucks, truck tractors and chassis				
6. Crude petroleum				
7. Aircraft				
8. Precious metals	23182.8	25641.3	25923.9	33987.4
9. Coal				
10. Other metals in ores, concentrates, etc.				

1981 CURRENT ACCOUNT - USA

	\$ Millions
Merchandise trade balance	2782
Services transactions:	
Travel	- 734
Interest and dividends	- 5452
Freight and shipping	- 419
Other service transactions	- 5010
Balance on service transactions	-11615
Balance on goods and services	- 8833
Net transfers	135
TOTAL CURRENT ACCOUNT BALANCE	- 8698

DISTRIBUTION OF EXPORTS (% - 1981)

Country	USA	Canada
Canada	18	-
USA	-	69
Japan	14	2
EC	16	8

PRICES & COSTS (% Change)

	<u>CPI-CDA</u> (% change)			<u>CPI-USA (yr-to-yr)</u> (% change)		
	<u>Total</u>	<u>Food</u>	<u>Non-Food</u>	<u>Total</u>	<u>Food</u>	<u>Non-Food</u>
1977	8.0	8.3	7.9	6.5	6.3	6.5
1978	8.9	15.5	6.4	7.7	10.0	7.2
1979	9.1	13.2	7.9	11.3	10.9	11.4
1980	10.2	10.7	10.0	12.4	10.2	12.9
1981	12.5	11.4	12.8	8.9	4.3	9.9

EMPLOYMENT

	<u>Unemployment Rate CDA</u>	<u>Unemployment Rate USA</u>
1976	7.1	7.7
1977	8.1	7.0
1978	8.4	6.0
1979	7.5	5.8
1980	7.5	7.1
1981	7.6	n/a

CDN DOLLAR IN US CENTS

1977	94.10
1978	87.72
1979	85.38
1980	85.54
1981	83.42

FOREIGN INVESTMENT (Latest Statistics Canada Estimates)

US Direct Investment in Cda	\$38.3 billion (end of 1978 cumulative)
US Portfolio Investment in Cda	\$31.5 billion (end of 1978 cumulative)
Canadian Direct Investment in USA	\$ 8.9 billion (end of 1978 cumulative)
Canadian Portfolio Investment in USA	\$ 4.03 billion (end of 1977 cumulative)

BORDER CROSSINGS (millions)

	<u>Canada to USA</u>	<u>USA to Canada</u>
1977	37.9	31.8
1978	37.3	31.6
1979	34.4	31.2
1980	34.7	38.5
1981	33.6	39.8
<u>POPULATION</u> (millions)		
	<u>Canada</u>	<u>USA</u>
1981	24.1	230.5

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