



Marc Lee
Economist
Canadian Centre for Policy Alternatives -- BC Office

CANADA-U.S. CUSTOMS UNION: A CRITICAL ASSESSMENT

Subject: *Benefits and Costs of a Canada-U.S. Customs Union*

Background/Introduction:

(in the words of the C.D. Howe Institute)
with the U.S. across a number of policy areas, including border security, defence policy, and immigration. Among the deep integration proposals is a call for a Canada-U.S. Customs Union (CUCU)

A customs union is the next step past a free trade area towards deeper economic integration. The key features of a customs union are the creation of a *common external tariff* that applies to all nations not part of the free trade area, and the establishment of a common trade policy. It also involves the elimination of *rules of origin*. Rules of origin appear in free trade agreements to ensure that exports from country A to country B originate in A, or at least have substantial value added to them in A. This is to ensure that country C, who is not party to the free trade agreement, does not export only to the country with the lowest tariffs on its product as a means of serving the entire trade bloc.

In the North American Free Trade Agreement, rules of origin stipulate that exported goods within the free trade area should have at least 60% North American content (62.5% for automobiles) to benefit from tariff-free access. The NAFTA also sets up a process to determine that exported goods within the NAFTA region containing non-North American content are substantially transformed in order to qualify for tariff-free status. The rules

In both countries there are politically sensitive sectors that have been protected from the full force of international trade agreements. In Canada, these include public services, Crown corporations, agricultural marketing

exceed those in the United States in the future. What would this mean, for example, in the case of the Kyoto Protocol, which Canada has ratified but the U.S. has not? Under a common regulatory regime, Canada would not be able to use regulatory powers to meet its targets.

Full integration of regulations may not be possible, much less desirable. Even within Canada, there are differences among provinces in terms of regulations for environmental protection, labour and employment standards, and consumer safety. Indeed, these differences are attacked from time to time by corporate Canada as allegedly massive "inter-provincial barriers to trade." The question remains: how far does a common trade policy reach inside Canada's borders? Ultimately, there is much more to this than setting a common external tariff.

There could be benefits for Canada in achieving some sort of agreement on trade remedy measures (such as antidumping and countervailing duties) — though these are not considered part of a customs union. The failure of Canada to secure exemptions from U.S. trade remedy laws has proved to be a major weakness of the original Canada-U.S. Free Trade Agreement, and the subsequent NAFTA, from Canada's point of view. However, given prevailing attitudes in the U.S. Congress, changing trade remedy laws or even negotiating an exemption is a non-starter. That is, this source of gain for Canada is, for all intents and purposes, off-limits.

Ultimately, what is politically feasible would determine the outcome of a new round of negotiations with the United States. Canada would be seeking particular gains from Washington, and in turn would need to make concessions to seal a deal. The history of such negotiations is cause for concern. There is a great danger that Canada would have to give up a lot to get little in return. In a negotiation that is broad, even if couched as a customs union, Canadians would have no real idea where it would lead, what the final package would look like, or what surprises (like the revolutionary investor-state dispute settlement mechanism that came with the NAFTA) might be in store.

Choices for Canadians:

The expansion of Canada-U.S. trade to a customs union is a major proposition in terms of Canadian trade and foreign policy. If anything Canada needs a more multilateral trade policy — the gains from more trade are not with the U.S. but with the rest of the world. Yet, a customs union would not only be a shift ad

telecommunications industries). Canada would be required to make serious commitments in these areas — commitments that many Canadians would find unacceptable.

Canada's energy resources are also cited as something that Canada could bring to the table as part of a "strategic

into account, such an approach could harvest the “low-hanging fruit,” reaping most of the benefits, but without a dramatic loss of sovereignty.

The gains from trade for Canada are more likely to be found in enhancing trade with Europe or the Global South, which suggests a multilateral approach to trade policy rather than a narrow bilateral one. Canada’s concerns would also be better addressed via multilateral institutions and international cooperation with other countries that share those concerns. This is the only way to get the leverage necessary with Washington to make changes on issues of real substance, like its punishing trade remedy laws.