Global Affairs Canada
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The Canada-United States-Mexico Agreement: Economic Impact Assessment

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EXECUTIVE SUMMARY

On November 30, 2018, Canada, the United States and Mexico signed a Protocol to modernize the North American Free Trade Agreement (NAFTA). The new Agreement is known in Canada as the Canada-United States-Mexico Agreement (CUSMA, or the Agreement).[1] Subsequently, on December 10, 2019, the parties signed a Protocol of Amendment to modify certain elements of the new Agreement in the areas of state-to-state dispute settlement, labour, environment, intellectual property and rules of origin. The final CUSMA outcome preserves key elements of NAFTA, modernizes disciplines to address modern trade challenges, reduces red tape at the border, and provides enhanced predictability and stability for workers and businesses across the integrated North American market. Overall, the modernization of NAFTA marks an important milestone in Canada's economic relationship with the United States and Mexico.

NAFTA has had a positive impact on the Canadian economy and has supported a stable, integrated and competitive North American market. The entry into force of NAFTA in 1994 created the largest free trade region in the world. By strengthening the rules and procedures governing trade and investment in North America, the agreement has proved to be a solid foundation for building Canada's prosperity and has set a valuable example of the benefits of trade liberalization for the rest of the world. Since 1994, NAFTA has helped generate economic growth and raise the standard of living for the people of all three member countries. In particular, NAFTA has supported the development of an integrated and competitive North American market by providing manufacturers, producers, investors and consumers with a predictable and secure commercial environment.

From a trilateral perspective, NAFTA has contributed to an unprecedented increase in trade flows across North America since its implementation in 1994. Between 1993 and 2018, total merchandise trade between Canada and the United States tripled and total merchandise trade between Canada and Mexico grew almost 10-fold. Overall, total trilateral merchandise trade (the total of each country's imports from one another) had risen to reach nearly US$1.2 trillion in 2018.

Engaging in negotiations to modernize NAFTA was important to address the negative impact of a potential U.S. withdrawal from NAFTA and the threat of U.S. Section 232 tariffs on Canadian businesses and workers. While, overall, NAFTA has been a positive economic driver, discontent with the effects of globalization and job dislocation has led some, in particular in the United States, to question the benefits of trade liberalization and call for increased trade protectionism. This general climate of

[1] In the United States, the Agreement is known as the United States-Mexico-Canada Agreement (USMCA), while in Mexico the Agreement is known as Tratado México, Estados Unidos y Canadá (T-MEC).

anti-trade sentiment contributed to threats to withdraw from NAFTA, the imposition of unilateral U.S. tariffs on steel and aluminum imports (and Canada's retaliatory measures), as well as threats to impose Section 232 tariffs on automobiles and auto parts. Given this overarching context, Canada was presented with two options: 1) refuse to negotiate and risk a U.S. withdrawal from NAFTA; or 2) enter into negotiations to defend Canadian interests and modernize the agreement. Canada chose in this context to engage in negotiations with the United States and Mexico towards the modernization of NAFTA. The process was unique in that it was the first large-scale modernization of any of Canada's FTAs. The negotiations took place at a complex time in the trilateral commercial relationship and resulted in many politicians, stakeholders and the general public engaging proactively in support of the Agreement and the economic benefits that can be achieved by free and fair trade.

Canada established its negotiating objectives based on broad and extensive engagement with provinces and territories, Canadian businesses, business associations, labour unions, civil society, Indigenous groups, youth and academics. Overall, the Government of Canada engaged with over 1,300 stakeholders on NAFTA modernization between February 2017 and December 2019. In the lead-up to the initiation of the negotiations in August 2017, the Government also received over 47,000 submissions from interested Canadians on their priorities for the negotiations. Based on this extensive engagement, Canada set out three overarching objectives for the negotiations:

- preserve important NAFTA provisions and preferential market access into the United States and Mexico;
- modernize and improve the Agreement, where possible; and
- reinforce the predictability and stability of market access into the United States and Mexico for Canadian businesses.

The negotiations were unique, and Canada was faced with a set of unconventional proposals that sought to rebalance the agreement's outcomes in favour of the United States. These proposals would have had a significant negative economic impact on Canada and included: a 50% U.S. domestic content requirement for autos; the complete dismantlement of Canada's system of supply management; the elimination of the NAFTA chapter 19 binational panel dispute settlement mechanism for anti-dumping and countervailing duties; the removal of the cultural exception; a state-to-state dispute settlement mechanism that would have rendered the Agreement completely unenforceable;a government procurement outcome that would have taken away NAFTA market access and rendered Canada worse off than all of the United States' other FTA partners under the new Agreement; and, a five-year automatic termination of the Agreement, known as the "sunset clause". Outside the context of the negotiations, Canada was also faced with important challenges related to the implementation of U.S. Section 232 tariffs on steel (25%) and aluminum (10%) in May 2018 (affecting

approximately $17.2 billion in Canadian exports to the United States), and the threat of similar tariffs on Canadian automotive products that could have had a significant negative impact on Canada's automotive sector, including related upstream and downstream industries.

From the beginning, Canada approached the negotiations with a high level of ambition and innovation in order to address new and complex challenges. In over half of the negotiating areas, Canada put forward full and ambitious text proposals to modernize NAFTA, including dispute settlement, government procurement, temporary entry of business persons, labour, environment and intellectual property. Some of the proposals—in particular on government procurement—were the most ambitious Canada had ever put forward in any FTA negotiation. Canada also took an active role in proposing improvements to more structural or technical elements of NAFTA, with the goal of further simplifying rules and procedures, cutting red tape, and increasing trilateral cooperation.

Throughout the process, Canada worked constructively to break impasses, including by tabling new and novel proposals to address key outstanding issues and find creative paths forward on the more difficult and unconventional issues. In particular, Canada put forward: a new approach to the autos rules of origin in order to move the discussions away from U.S. domestic content requirements and towards rules that would incentivize production in North America; an ongoing modernization mechanism to counter the potential negative impacts of the proposal for a five-year sunset clause; and, a strengthened approach to enforceable dispute settlement to address proposals that would have enabled parties to disregard panel outcomes and rendered the Agreement unenforceable.

The final CUSMA outcome effectively achieved Canada's overarching objectives by preserving key elements of NAFTA, modernizing and updating the Agreement to support Canada's access to and integration with the North American economy, providing important stability and predictability with respect to overall market access, and addressing the harmful impacts of U.S. Section 232 tariffs on steel and aluminum, as well as threats of similar tariffs on automobiles and auto parts. The new Agreement preserves NAFTA's virtually tariff-free market access for Canadian exports, strengthens the integration of the North American automotive sector, reinforces Canada's relative position as a competitive investment destination for automobile and auto-parts production, and provides new market access opportunities into the U.S. market while at the same time preserving Canada's system of supply management. The new Agreement also includes modernized provisions that update the Agreement in line with Canada's more recent FTAs in a manner that will help reduce red tape, facilitate trade and protect the Government's right to regulate in the public interest, including for health and safety. As a part of the outcome, Canada secured an exemption from any future U.S. Section 232 tariffs on automobiles and auto parts. Importantly, and as a

condition for moving forward towards implementation of the new Agreement, on May 17, 2019, Canada secured the removal of U.S. Section 232 tariffs on aluminum and steel, returning these sectors to duty-free trade and removing a significant barrier to Canada's participation in North American supply chains.

A U.S. withdrawal from NAFTA would have had a negative impact on the North American economy, in particular on the automotive sector. Continued U.S. Section 232 tariffs on steel and aluminum and the imposition of similar tariffs on automotive products would have done irreparable damage to Canadian companies and workers. If the United States were to withdraw from NAFTA, all three NAFTA parties would experience a negative impact on their economies. Trade between Canada and the United States would be governed by WTO rules alone, whereas trade between Canada and Mexico would continue to be governed by NAFTA or the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). Goods trade between the United States and Canada would be subject to WTO most-favoured nation (MFN) duties. Under MFN, approximately 40.5% of Canadian exports to the United States and 66.7% of U.S. exports to Canada enter duty-free, meaning that the remainder would be subject to each country's respective tariffs. The average weighted MFN duties on Canadian exports to the United States is estimated at 1.7%, compared to 2.5% for U.S. exports to Canada. Canadian exports to the United States that would face high tariffs include trucks (25%), footwear (up to 35%) and apparel (up to 32%). In the areas of services and investment, WTO provisions would provide predictability and security for Canadian businesses operating in the United States with one notable and important change: Canada and the United States would no longer benefit from the preferential treatment under the chapter on temporary entry for business persons. The loss of temporary entry provisions would mean that persons of both parties would face increased barriers at the border that could restrain business travel or otherwise create challenges for those seeking to relocate on a temporary basis for specific business purposes. Additionally, U.S. Section 232 tariffs put in place on Canadian steel and aluminum would have continued, and the risk of similar tariffs on Canadian automotive products would have increased.

The CUSMA outcome preserves the important benefits of NAFTA, modernizes the agreement's disciplines, and makes it easier for Canadian companies to benefit from preferential access to the U.S and Mexican markets. As a result, the obligations that govern North American trade will be updated in a manner that increases predictability and stability for business and workers, reduces red tape at the border and facilitates trade, and better reflects the interests of all Canadians. These modernizations will make it easier for Canadian exporters to claim preferential tariff treatment under the Agreement. However, the gains will be partially offset by new market access to Canada's supply-managed sectors and more restrictive rules of origin for automobiles and auto parts that will likely increase auto-part production in North America but also lead to higher production costs. In particular, implementing the CUSMA outcome:

- **preserves duty-free NAFTA market access for $294.5 billion in industrial goods exports and $87.4 billion in energy exports** to both the United States and Mexico, and removes unnecessary fees related to certain energy exports and textile and apparel goods;
- **secures duty-free market access for $21.2 billion in agricultural, fishing and forestry exports** to the United States and Mexico, and includes forward-looking provisions for agricultural biotechnology to increase transparency and establish practical, trade-facilitative approaches to getting safe products to market;
- **creates new market access opportunities in the agricultural sector** through incremental market access to both Canada and the United States for dairy, to Canada for refined sugar and sugar-containing products, and to the United States for poultry and eggs; and protects and maintains Canada's system of supply management;
- **maintains and strengthens the integrity of the North American auto production platform** and provides new incentives that will increase the use of North American materials, which will benefit Canada's steel and aluminum sectors, but that could increase overall production costs and negatively affect competitiveness as compared to non-North American producers;
- **provides added security for Canadian businesses and workers through an exemption from U.S. Section 232 tariffs for Canadian automobile and auto parts exports,** in addition to the removal of U.S. Section 232 tariffs on steel and aluminum;
- **facilitates trade across the border by reducing red tape for exporters and increasing certainty that their products can get to market** without facing unnecessary and arbitrary delays, making it easier for Canadian businesses to claim NAFTA preferences and take advantage of opportunities in the NAFTA marketplace;
- **preserves the NAFTA chapter 19 binational panel dispute resolution process for trade remedies** that protects Canadian companies and workers from the unfair application of anti-dumping and countervailing duty measures, particularly in the softwood lumber industry;
- **enhances predictability and security of access for Canadian service providers**, which represent $68 billion in Canadian exports to the United States and Mexico, including through modernized disciplines on services, telecommunications and the addition of a new chapter on digital trade;
- **maintains Canada's preferential access to the United States and Mexican markets for the temporary entry of business persons**, which is essential to ensuring that Canadian investors can oversee their investments first-hand and that Canadian service suppliers can enter those markets to fulfill contracts on-site;

- **preserves NAFTA's cultural exception**, which helps safeguards Canada's flexibility to implement programs that support our linguistic and cultural identity;
- **improves predictability in investment rules in North America while removing the potential financial implications associated with future investor-state dispute settlement** cases that have, to date, cost Canadian taxpayers more than $275 million in penalties and estimated legal fees;
- **ensures that Canada's trading partners in North America will maintain high levels of labour and environmental protection**, levelling the playing field and helping to ensure that labour and environmental laws will not be deviated from as a means to attract trade or investment;
- **includes an innovative rapid response mechanism between Canada and Mexico** to examine whether national labour laws related to collective bargaining and freedom of association are respected and labour violations are addressed in a timely manner;
- **strengthens the state-to-state dispute settlement mechanism between parties** and ensures that disputes are settled in an effective and efficient manner, and that Canadian companies can continue to benefit from the preferences provided under the Agreement; and
- **increases and enhances opportunities for SMEs, women and Indigenous peoples** to engage in and benefit from North American trade.

The implementation of the CUSMA outcome secures GDP gains of $6.8 billion[2] (US$5.1 billion), or 0.249%, which would be lost if the U.S. withdrew from NAFTA. With respect to quantifiable effects on Canada's economy, this study focused on the impacts of the new rules of origin for automobiles and auto parts, new tariff rate quotas for certain agricultural products, data storage requirements for financial services, as well as certain provisions in the areas of customs administration and trade facilitation, and origin procedures. With respect to the automotive sector, the outcomes are expected to incentivize production in Canada and North America, while leading to the sourcing of more expensive automotive parts from within the region. This could benefit Canadian automotive parts producers as well as Canada's steel and aluminum sectors; however, it would likely increase the overall cost of production of auto parts and assembled vehicles.

From a labour perspective, CUSMA secures nearly 38,000 jobs that would otherwise be lost while preserving real wage gains for Canadian workers, particularly machinery operators, manual labourers and sales workers**.** Additionally, from a gender perspective, the jobs secured would be almost evenly split between men and women (18,708 jobs saved for men and 18,853 jobs saved for women). Overall, these outcomes should have a positive impact on middle-class jobs and improve income equality in Canada.

[2] Based on the Bank of Canada US$/Can$ exchange rate of 1.3269 for 2019.

In conclusion, the analytical findings resulting from economic modelling suggest that the Agreement's economic impact on the Canadian economy is positive when compared to the effects of a scenario under which the United States withdraws from NAFTA and imposes Section 232 tariffs on Canada's steel and aluminum sectors. Importantly, CUSMA preserves Canada's access to the U.S. and Mexican markets and protects Canadian economic gains, jobs and income that could otherwise have been lost.

INTRODUCTION

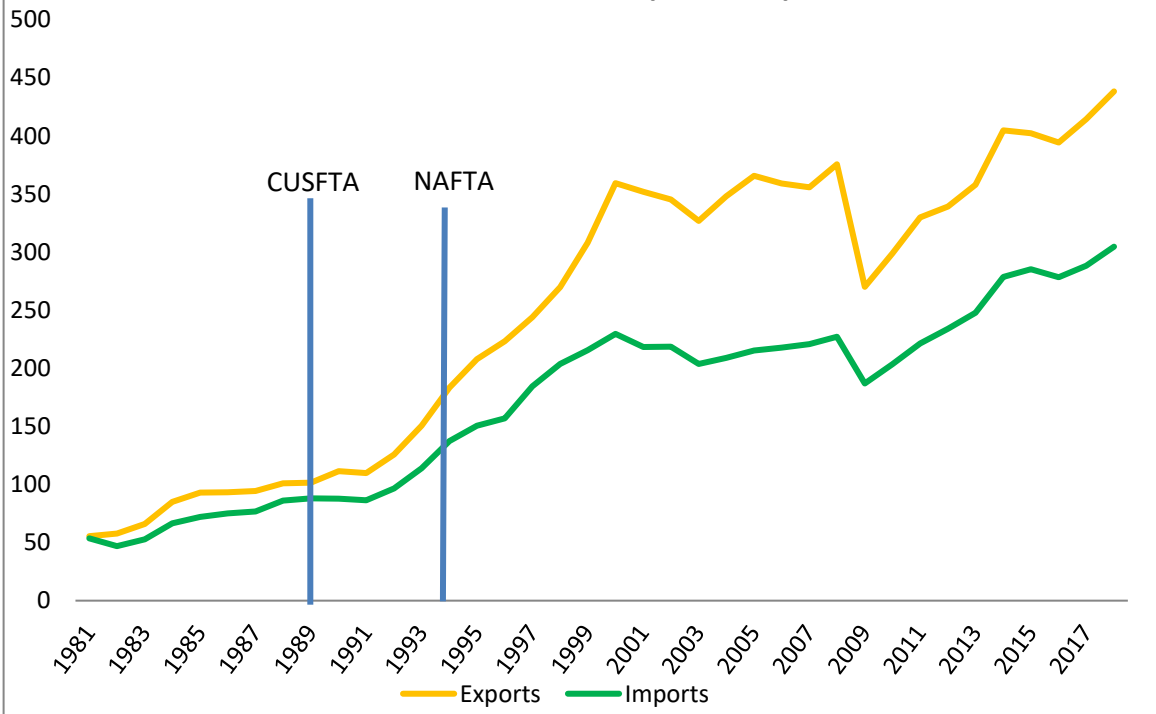
Global Affairs Canada prepared this report based on an assessment of the likely economic impact of CUSMA on the Canadian economy. The report provides a brief historical overview of Canada's trade performance under the Canada-U.S. Free Trade Agreement (CUSFTA) and NAFTA to highlight the economic importance of these agreements for Canada. The report also provides a summary of CUSMA outcomes and assesses the potential economic impact of CUSMA compared to a "no-NAFTA" reference point under which the United States withdraws from NAFTA and continues to impose Section 232 tariffs on steel and aluminum. In the context of this assessment, the report assesses the likely impact on Canada's GDP, exports and imports, several specific sectors, as well as the potential implications for the labour market, gender equality and youth.

Trade with the United States

Following the entry into force of the CUSFTA in 1989, Canada-U.S. trade experienced tremendous growth. The implementation of NAFTA in 1994 led bilateral trade to grow at an accelerated pace, notwithstanding a slowdown in the pace of growth in the 2000s. In 2018, total Canadian merchandise exports to the United States reached $438.3 billion,[3] representing a four-fold increase from $101.6 billion in 1989. Such a dramatic expansion of Canadian exports to a single country is unprecedented.

Canada's merchandise imports from the United States have grown significantly since 1989. Canadian imports from the United States grew from $88.1 billion in 1989 to $304.7 billion in 2018, a net increase of $216.6 billion (see Figure 1).

Figure 1: Canada's Merchandise Trade with the United States, 1981-2018 ($ billion)



Source: Statistics Canada. Table 12-10-0011-01 - International merchandise trade for all countries and by principal trading partners, monthly (x 1,000,000).

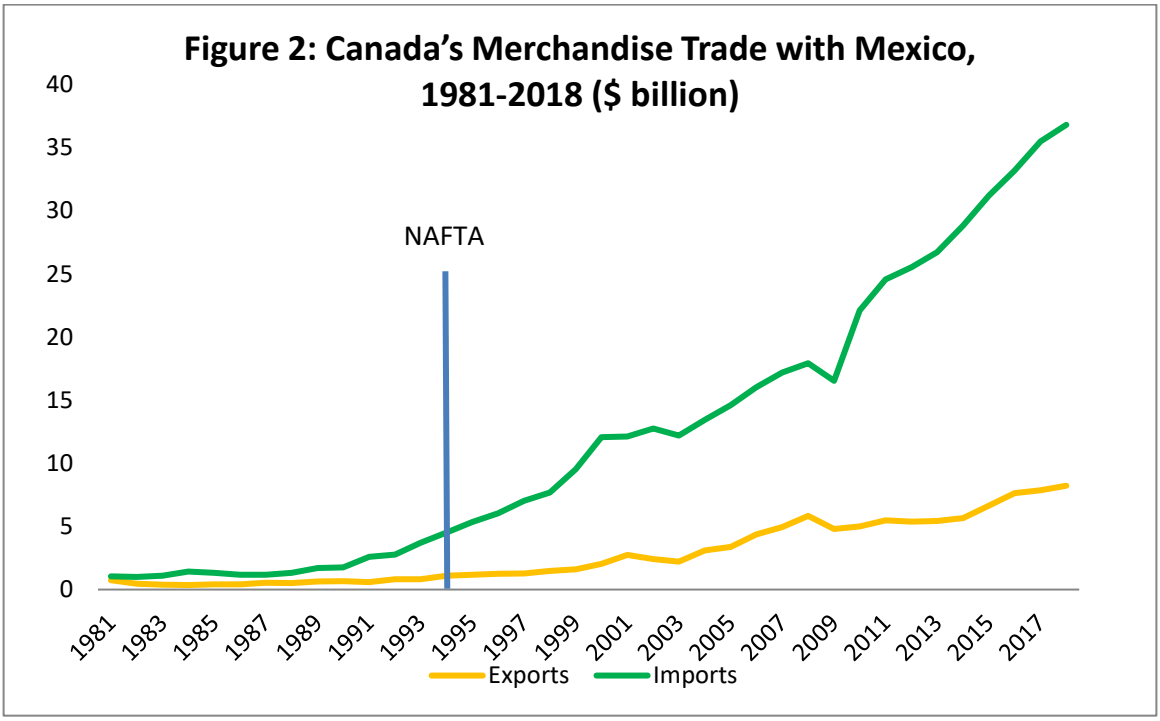
[3] All monetary references in this report are in Canadian dollars, unless otherwise specified.

As a result of the implementation of the CUSFTA and NAFTA, Canada has seen a remarkable shift in its trade orientation and the structure of its economy. In particular, the Canadian economy has become considerably more trade-oriented and integrated into the North American economy. The United States accounted for 87% of Canada's global merchandise exports in the early 2000s, up from 60% in the early 1980s. The United States' relative importance as a Canadian export destination has declined somewhat since the early 2000s, though it still represented 75% of Canada's total merchandise exports in 2018.

Canadian merchandise exports as a share of GDP increased from 21% in the late 1980s to a peak of nearly 30% in 2008 (before the financial crisis), before declining to 26.3% in 2018.

Trade with Mexico

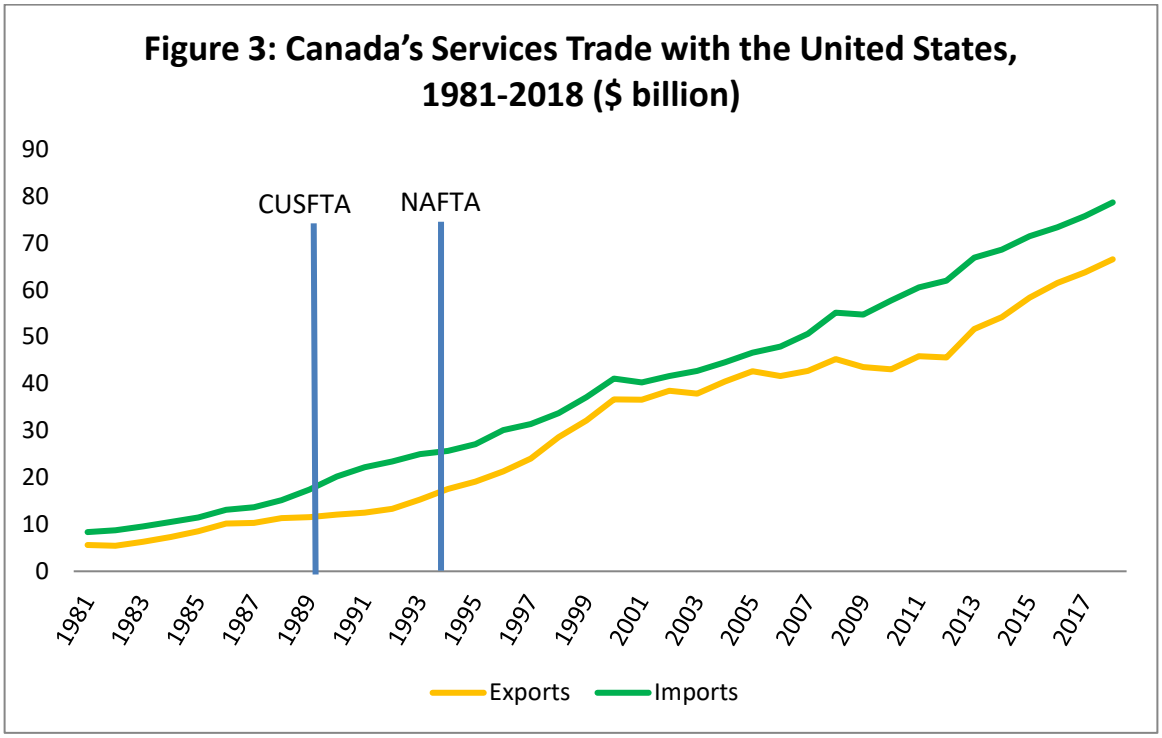
NAFTA's effects on the Canada-Mexico trade relationship were significant, although trade between the two countries was less balanced in that Canadian merchandise imports from Mexico grew more quickly than did merchandise exports to Mexico. Total imports from Mexico, which were on the rise even before NAFTA, accelerated at a considerable pace following NAFTA's entry into force. Total imports from Mexico grew nearly 10-fold, from $3.7 billion to $36.8 billion, between 1993 and 2018. Over the same period, total Canadian exports to Mexico grew 10-fold, from $0.8 billion to $8.2 billion (see Figure 2).



Source: Statistics Canada. Table 12-10-0011-01 - International merchandise trade for all countries and by principal trading partners, monthly (x 1,000,000).

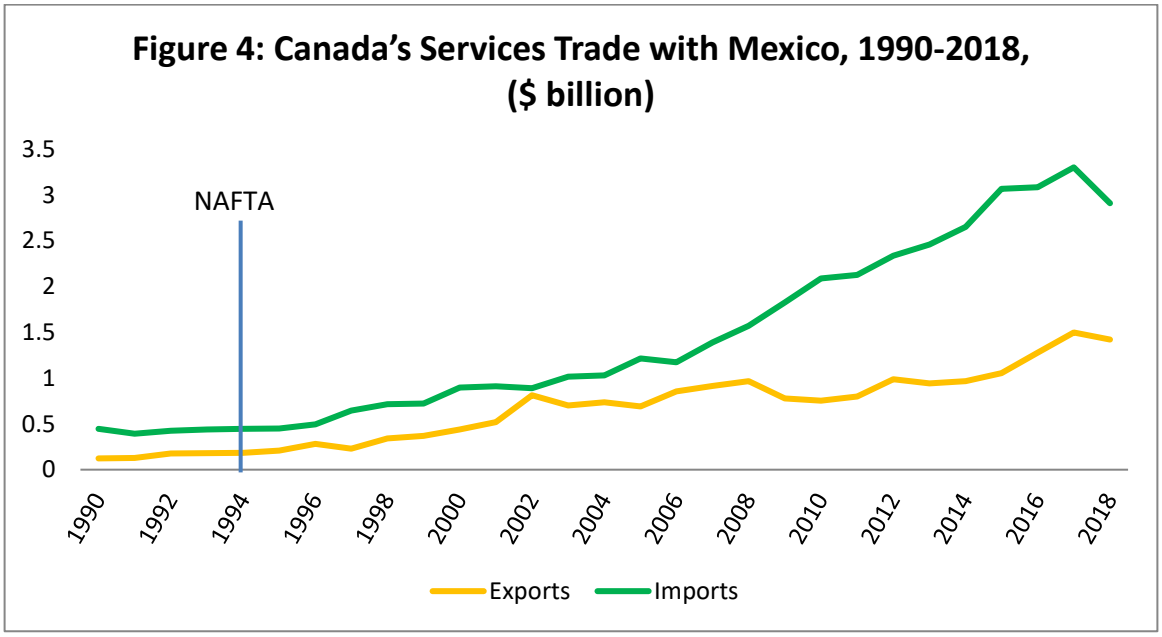
Trade in services

Canada's trade in services with the United States and Mexico increased substantially during the CUSFTA and NAFTA eras. Canadian imports of services from the United States have increased continuously since 1981, and grew from $15.2 billion in 1988 to $78.7 billion in 2018. Total Canadian exports of services to the United States grew similarly, from $11.4 billion in 1988 to $66.6 billion in 2018 (see Figure 3).



Source: Statistics Canada. Table 36-10-0014-01 - Balance of international payments, current account and capital account, annual (x 1,000,000).

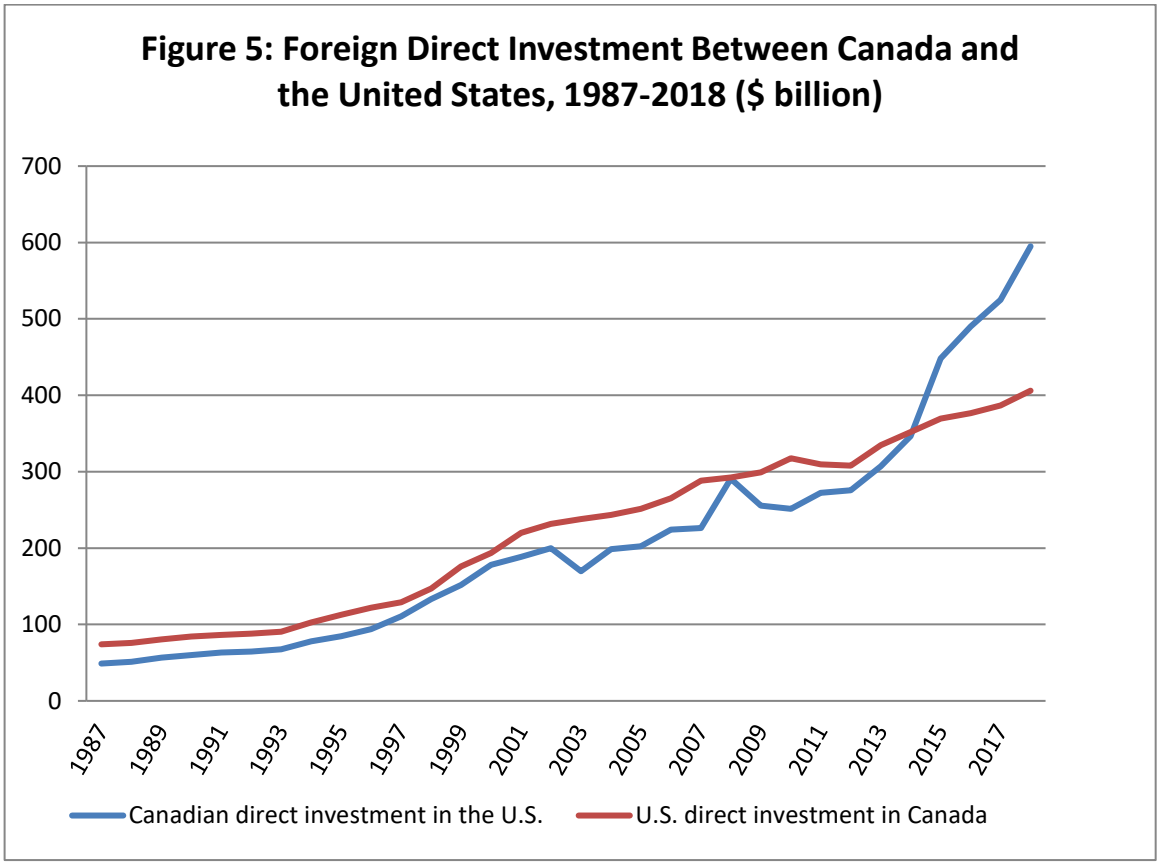
Canadian imports of services from Mexico have increased gradually since the implementation of NAFTA in 1994. Canadian services exports have also grown gradually, but at a slower pace from 2006 onward. Total imports of services from Mexico grew from $0.4 billion in 1993 to $2.9 billion in 2018, while total Canadian services exports to Mexico grew from $0.2 billion in 1993 to $1.4 billion in 2018 (see Figure 4).



Source: Statistics Canada. Table 36-10-0007-01 - International transactions in services, by selected countries, annual (x 1,000,000) and Table 36-10-0024-01 - Balance of international payments, current account, services by principal trading partners, quarterly (x 1,000,000)

Investment

Foreign direct investment between Canada and the United States has risen tremendously in absolute terms since the implementation of the CUSFTA and NAFTA. While the stock of U.S. direct investment in Canada has increased steadily—reaching $406 billion in 2018—the stock of Canadian direct investment in the United States has accelerated since 2012, reaching $595 billion in 2018 (see Figure 5).

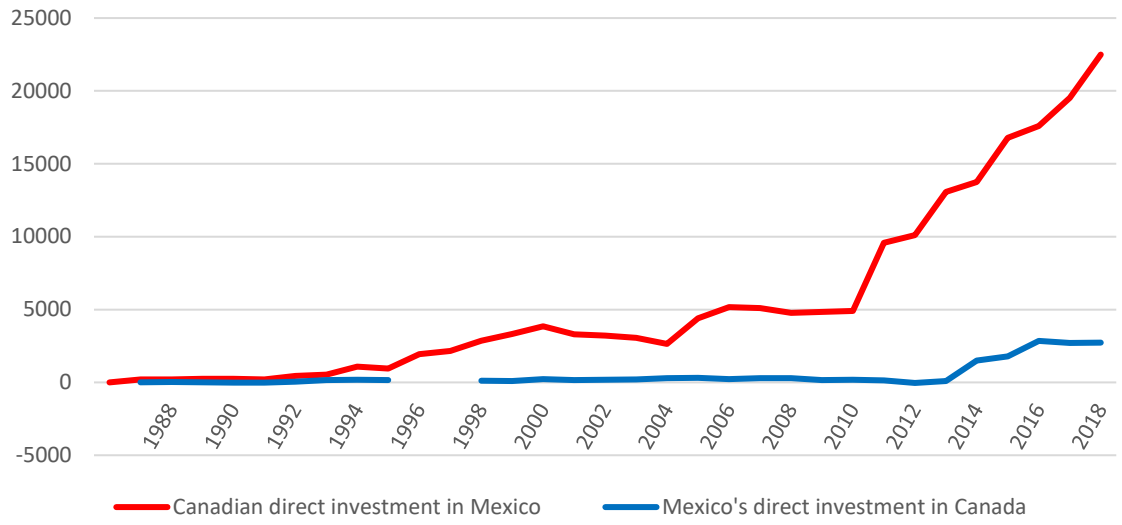


Source: Statistics Canada. Table 36-10-0008-01 - International investment position, Canadian direct investment abroad and foreign direct investment in Canada, by country, annual (x 1,000,000).

Foreign direct investment between Canada and Mexico has grown significantly over the last several decades. The stock of Canadian direct investment in Mexico amounted to $22.5 billion in 2018 (see Figure 6), while Mexico's direct investment in Canada has been more modest, reaching $2.7 billion in stock in 2018.[4]

[4] 1996-97 data for the stock of Mexico's direct investment in Canada is not available.

Figure 6: Foreign Direct Investment Between Canada and Mexico, 1987-2018 ($ billion)



Source: Statistics Canada. Table 36-10-0008-01 - International investment position, Canadian direct investment abroad and foreign direct investment in Canada, by country, annual (x 1,000,000).[5]

Trade creation and diversion[6]

By all accounts, NAFTA has worked well and achieved the expected results by expanding trade, increasing investment, generating economic growth, raising living standards, and supporting the development of an integrated and competitive North American market.[7] This is evidenced by the significant increase in trade in merchandise, services and investment between all three partners since the implementation of NAFTA.

While NAFTA continues to be important to the North American market, developments in the United States and Canada have eroded the benefits of NAFTA from a bilateral perspective. These developments include:

- multilateral trade liberalization and unilateral tariff reductions;
- expansion of U.S. trade with the rest of the world; and

[5] 1996-97 data is not available.

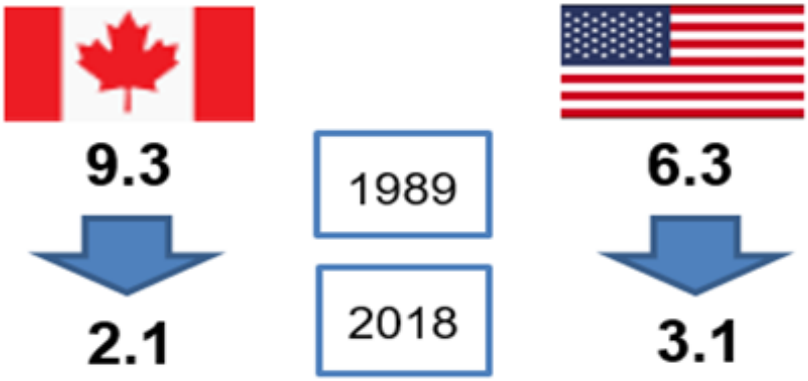
[6] Trade diversion happens when, as a result of an FTA, trade is diverted away from a more efficient supplier from outside the FTA countries towards a less efficient supplier within the FTA.

[7] For instance, according to Marc J. Melitz and Daniel Trefler in "Gains from Trade when Firms Matter," Journal of Economic Perspectives, Vol. 26, No. 2, Spring 2012, the Canada-U.S. Free Trade Agreement (CUSFTA) boosted Canadian manufacturing labour productivity by 13.8%.

- shift of the U.S. manufacturing base towards southern U.S. states.

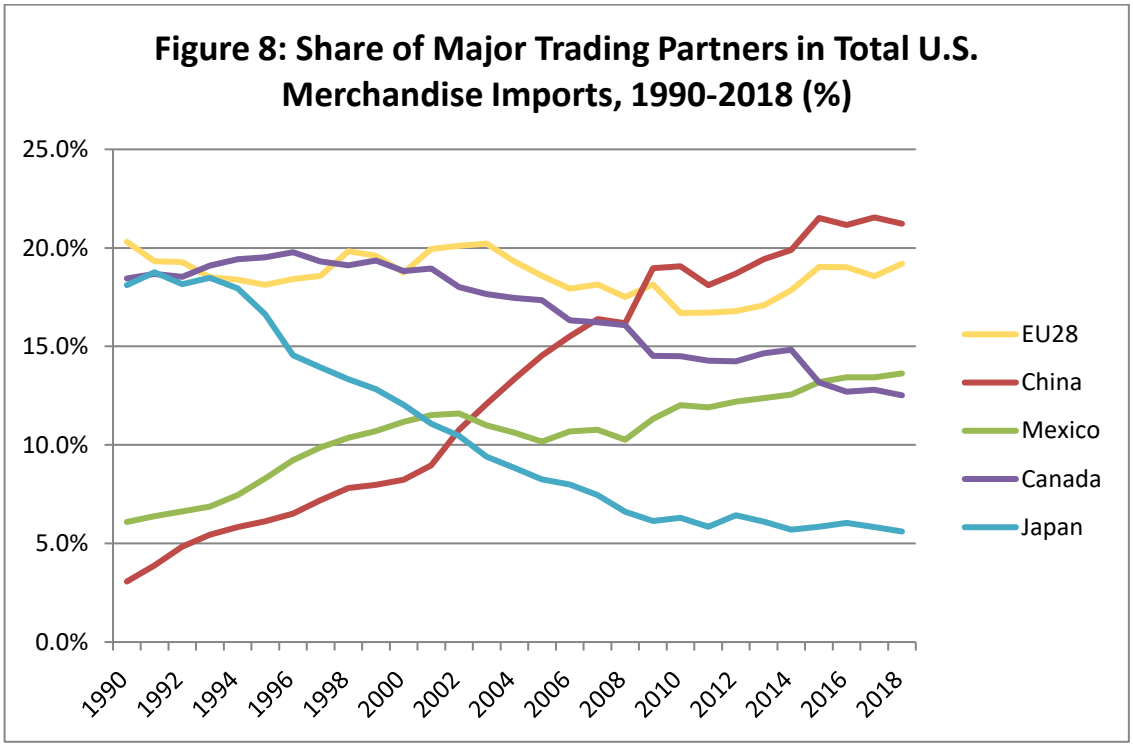
Multilateral trade liberalization and unilateral tariff reductions undertaken by the United States and Canada since 1994 have made the NAFTA preferential tariffs less important today than when the agreements first came into force. For example, the simple average Canadian-applied most-favoured-nation (MFN) tariff for non-agricultural products has decreased from 9.3% in 1989 to 2.1% in 2018. Over the same period, the simple average U.S.-applied MFN tariff for non-agricultural products has decreased from 6.3% to 3.1% (see Figure 7). In practical terms, this means that today NAFTA provides partner countries with fewer preferential advantages when compared to the tariff treatment afforded to imports from non-NAFTA countries.

Figure 7: Non-agricultural MFN Tariffs
Simple Average of Applied MFN Tariff Rates



Source: Global Affairs Canada, Office of the Chief Economist

Expansion of U.S. trade with the rest of the world, whether under an FTA or not, has eroded Canada's preferences in the U.S. market. This is particularly evident in the case of China, even though China does not enjoy preferential treatment in the U.S. market. China's share of total U.S. imports surged from 3.1% in 1990 to 21.2% in 2018. Similarly, Mexico's share of total U.S. imports increased from 6.1% to 13.6% over the same period (see Figure 8).



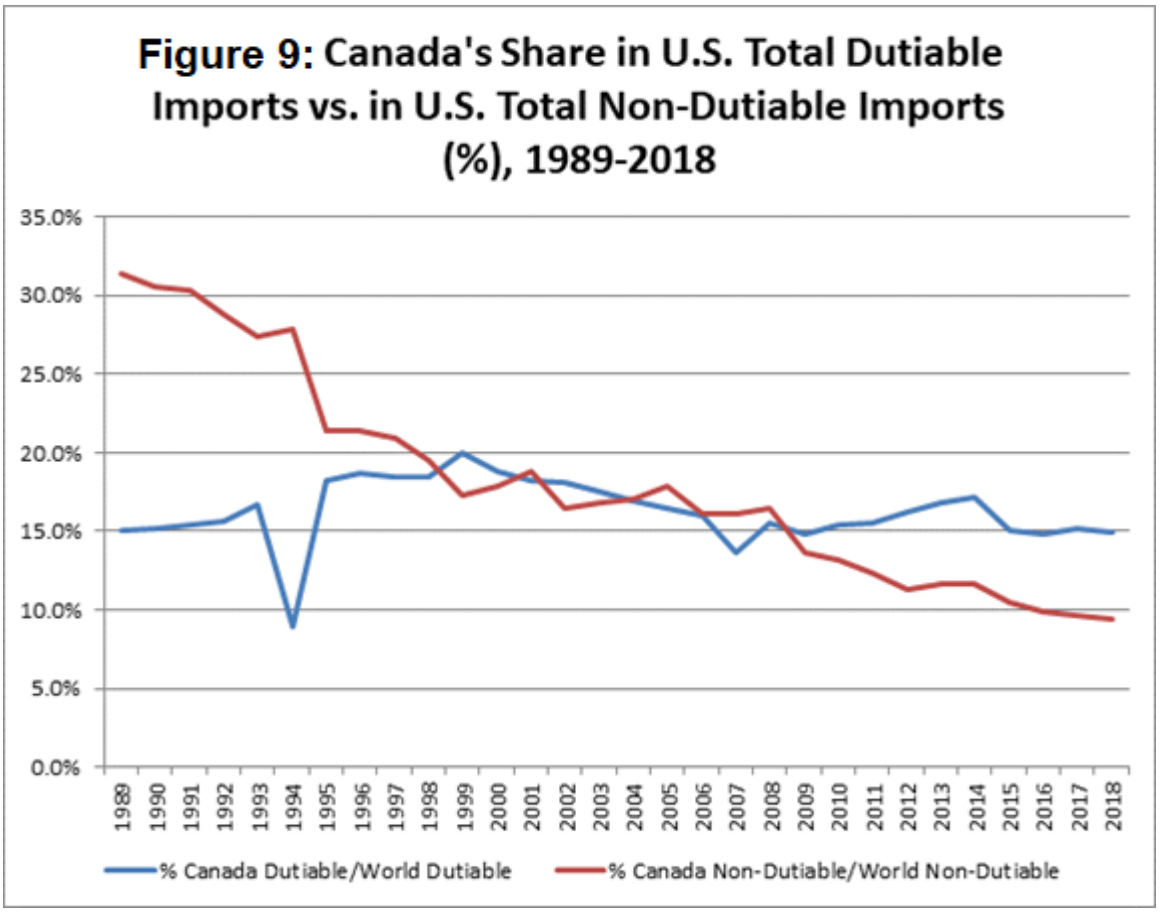
Data: Global Trade Atlas.
Source: Global Affairs Canada, Office of the Chief Economist.

The U.S. manufacturing base has gradually moved towards the southern U.S. states, which has negatively affected Canadian industries by making integration with U.S. supply chains more difficult. Traditionally, the U.S. manufacturing base has been located in the northern part of the country, along the Great Lakes.

As a result of these factors, Canada's market share of total U.S. imports has fallen to 12.5% in 2018, having peaked at 20% in 1996.

The true trade creation effect of trade agreements is difficult to discern based on the aggregated data as the aggregated trade data covers all products, not just those that benefit from the NAFTA preferences. If the products are separated into two groups—"dutiable" products subject to regular U.S. MFN tariffs but exempted from tariffs under NAFTA, and "non-dutiable" products that were MFN duty-free under WTO rules—the benefits of NAFTA would clearly stand out. While Canada's market share of total U.S. imports from around the world has decreased over time, the NAFTA preferences have helped Canadian exporters mitigate against competition from non-NAFTA imports in respect of dutiable products. Figure 9 shows that Canadian dutiable goods' market share of total U.S. imports has held steady despite the incursion of products from non-NAFTA countries. On the other hand, Canada's market share for non-dutiable products has declined from more than 30% in 1989 to less than 10% in 2018. In other words, while

Canada's overall market share of total U.S. imports from around the world has been on a downward trend over the past decades, NAFTA preferences have helped sustain Canada's market share for dutiable products in the U.S. market.



Data: Global Trade Atlas; The Center for International Data (UC Davis); UNCTAD, World Integrated Trade Solution; Government of Canada, USITC Tariff Database.

Source: Global Affairs Canada, Office of the Chief Economist.

SUMMARY OF CUSMA OUTCOMES

The overall CUSMA outcome effectively achieves Canada's overarching objectives for the negotiations by preserving key elements of NAFTA, modernizing and updating the agreement to support Canada's access to and integration with the North American economy, and providing important stability and predictability in relation to the threat of U.S. Section 232 tariffs. The new Agreement preserves NAFTA's virtually tariff-free market access for Canadian exports, strengthens the integration of the North American automotive sector, reinforces Canada's relative position as a competitive investment destination for automobile and auto-parts production, and provides new market access opportunities into the U.S. market while at the same time preserving Canada's system of supply management. The new Agreement also includes modernized provisions that are in line with Canada's more recent FTAs and help reduce red tape, facilitate trade and protect the Government's right to regulate in the public interest, including for health and safety. An overview of the key outcomes of the Agreement is provided below.

National treatment and market access

The modernized national treatment and market access (NTMA) for goods chapter sets out the fundamental disciplines for trade in goods, with the aim of eliminating or reducing barriers to trade in goods. The NTMA chapter builds upon existing commitments between the parties and includes provisions addressing restrictions on the flow of goods across borders, as well as the treatment of those goods once they have entered a foreign market. The NTMA chapter:

- maintains NAFTA's current tariff commitments, including those incorporated in the Canada-U.S. Free Trade Agreement (CUSFTA) of 1989;
- maintains key obligations governing trade in goods within North America; these include: provisions on national treatment, temporary admission of goods, import and export restrictions, administrative fees and formalities, and goods returned after repair or alteration; and
- contains enhanced transparency provisions for import and export licensing procedures that will provide greater certainty and predictability, and new rules to address non-tariff barriers related to trade in remanufactured goods (i.e. used but still functional goods that have been reassembled, rebuilt or refurbished such that they perform the same as or similar to a new good).

Energy

Provisions governing trade in energy goods, as well as other activities in the energy sector, are found across the Agreement instead of in a dedicated chapter as they are in NAFTA. This includes disciplines and provisions in the areas of national treatment and market access, rules of origin, customs and trade facilitation, cross-border trade in services and investment. Recognizing the importance of the energy sector in North America, CUSMA also contains an enforceable bilateral Canada-U.S. side letter on

energy regulatory measures and regulatory transparency. The commitments, contained in an annex to the letter, will provide for enhanced regulatory transparency and cooperation in the North American energy sector and include disciplines with respect to access to electric transmission facilities and pipeline networks. Of importance to Canadian oil exporters, CUSMA addresses a longstanding irritant through an amendment to the rules of origin to allow for the use of some non-originating diluent[8] in pipelines when moving crude oil, a longstanding Canadian industry request.

CUSMA does not include the provision known as the "energy proportionality clause." Under the original NAFTA energy proportionality clause, Canada and the United States committed to providing each other with access to a proportional share of recent trade for an energy product in the event of government-imposed export restrictions.

Agriculture

Under CUSMA, Canadian agricultural and agri-food products will continue to benefit from duty-free access for nearly 89% of U.S. tariff lines and 91% of Mexican tariff lines. For the remaining 11% of U.S. agricultural tariff lines, Canada secured new market access in the form of tariff rate quotas (TRQs) or tariff elimination. This includes incremental market access into the United States for products such as dairy, refined sugar and sugar-containing products, as well as improved access for margarine traded between Canada and the United States. At the same time, the United States will have new volume-limited market access into Canada for certain dairy, poultry and egg products through TRQs. Importantly, the outcome preserves Canada's supply management system.

CUSMA's provisions for agriculture improve on NAFTA in several areas. Specifically, Canada secured a number of beneficial outcomes, including a consultation mechanism for parties to address domestic support that may be trade-distorting, commitments that reflect the unique character of the sale of wine and spirits in Canada, and forward-looking provisions for agricultural biotechnology that increase transparency and establish practical, trade-facilitative approaches to getting safe products to market.

As part of the overall Agreement, Canada has also agreed to:

- ensure the elimination of current milk classes 6 and 7;
- ensure certain products previously classified in milk classes 6 and 7 are priced using a U.S. reference price, while other products are reclassified based on their end-use;

[8] Diluent is a petroleum-based liquid that is often added to crude oil to ensure that it flows properly through pipelines.

- establish a mechanism to monitor exports of skim-milk powder, milk-protein concentrate and infant formula. Should exports exceed certain thresholds, these products will be subject to surcharges; and
- allow U.S.-grown wheat of varieties registered in Canada to receive an official Canadian grain grade.

Dairy

Under CUSMA, the United States will obtain additional market access into Canada for milk, cream, skim-milk powder, butter and cream powder, cheese and other dairy products through new duty-free TRQs. Canada will obtain reciprocal access for dairy products in the form of duty-free TRQs into the United States. The TRQs will be gradually implemented in six equal increments over five years. After year six, there will be a growth factor of 1% compounded for a period of 13 years (e.g. in year seven, milk will be duty free up to 50,000 metric tons (MT) + 1% = 50,500 MT).

In addition, under CUSMA both Canada and the United States agreed to the elimination of tariffs on whey products within 10 years.

Poultry and eggs

For chicken, CUSMA establishes a U.S.-specific duty-free TRQ of 57,000 MT that will be gradually phased-in from 47,000 MT over a five-year period, with a 1% annual growth factor for a period of 10 years thereafter. The maximum TRQ volume will be reached in year 16. As NAFTA commitments will no longer apply, Canada's global access commitment for chicken will be defined solely by Canada's WTO commitment volume.

For eggs, CUSMA establishes a U.S.-specific duty-free TRQ of the equivalent of 10 million dozen eggs that will be gradually phased-in over a five-year period, with a 1% annual growth factor for a period of 10 years thereafter. The maximum TRQ volume will be reached in year 16. As NAFTA commitments will no longer apply, Canada's global access commitment for eggs will be defined solely by Canada's WTO commitment volume.

For turkey, Canada will replace its NAFTA global access commitment, equivalent to the greater of 3.5% of that year's anticipated production or the WTO commitment volume, with a new CUSMA commitment to provide a global volume determined each year: the greater of 3.5% of previous year's domestic production or Canada's minimum access commitment at the WTO. For 10 years after entry into force of the Agreement, Canada will calculate the difference between 3.5% of the previous year's domestic production and 3.5% of the anticipated domestic production for the current year. If the difference exceeds 1,000 MT, Canada will cap access at no more than 3.5% of the anticipated domestic production for that year plus 1,000 MT.

For broiler hatching eggs and chicks, Canada will continue to provide the same global access as is provided for under a 1990 agreement between Canada and the United States. Canada's annual access will continue to be the greater volume of either 21.1% of that year's anticipated domestic production or Canada's WTO commitment volume.

Sugar and sugar-containing products

Upon CUSMA's entry into force, the United States will provide new Canada-specific duty-free TRQs for 9,600 MT of refined sugar and 9,600 MT of sugar-containing products. CUSMA will also carry forward Canada's existing sugar access into the United States for 10,300 MT of refined sugar and 59,250 MT of sugar-containing products secured in the Agreement from the 1997 Canada-U.S. bilateral understanding.

Margarine

Canada will eliminate its over-quota tariff on margarine imported from the United States over five years, while the United States will eliminate its over-quota tariff on edible mixtures similar to margarine over the same period. Compared to the NAFTA product-specific rule of origin, margarine produced with non-originating palm oil may now qualify for tariff preference between Canada and the United States.

Rules of origin

Rules of origin (ROO) are the criteria used to determine whether a good has undergone sufficient production in the FTA region to be eligible for preferential tariff treatment. They ensure that the benefits of the Agreement accrue primarily to producers located in FTA countries. In CUSMA, the NAFTA rules of origin have been modernized and, in some cases, strengthened. This is particularly true in the area of automobiles and auto parts.

Automotive rules of origin

Compared to NAFTA, the CUSMA rules of origin for automotive goods have been strengthened significantly and new origin requirements have been added for light vehicles and heavy trucks. The new automotive rules of origin regime also includes changes to the regional value content (RVC) calculation methodology.

Importantly, CUSMA includes significant changes to the criteria that automakers and parts producers must fulfil in order to qualify for duty-free treatment. These changes include the elimination of the NAFTA "tracing" requirement that obliges companies to track the value of certain non-originating materials used in production, regardless of how much production the materials undergo in North America. The tracing requirement placed a burden on automakers and parts producers to collect cost data from suppliers. Eliminating the tracing requirement means that automotive materials will be treated the same as materials used in the production of all other goods.

Innovative approaches are being taken to simplify compliance with the new CUSMA rules of origin for automotive goods. For example, the automakers will be permitted to certify compliance with the originating steel and aluminum requirements at the corporate level, thereby eliminating the need for traditional plant- or model-based record keeping and reporting for this requirement.

CUSMA also includes significantly higher RVC requirements than NAFTA, including a 75% threshold for vehicles and core parts (engines, transmissions, bodies, axles, steering systems, suspension systems and lithium-ion batteries), along with a 70% threshold for principal parts (e.g. starters, bumpers, brakes and seats) and 65% for complementary parts (batteries, wiring sets, and measuring instruments such as odometers).

CUSMA automotive rules of origin changes

For light vehicles, engines and transmissions used in the production of vehicles, NAFTA requires a 62.5% RVC. For heavy trucks, buses, tractors and specialty vehicles (e.g. ambulances, fire trucks), along with most other major auto parts, NAFTA requires a 60% RVC. Residual auto parts, including many electronic components (e.g. GPS, cameras), are subject to a 50% RVC.

CUSMA increases the threshold for light vehicles and their “core parts” (i.e. defined in CUSMA as engines, transmissions, bodies, axles, steering systems, suspension systems, and advanced batteries when used in vehicle propulsion) to a 75% RVC. All other major auto parts, most of which currently require a 60% RVC under NAFTA, will undergo increases to either a 65% RVC or a 70% RVC. These higher thresholds for vehicles and parts are being phased-in over a three-year period.

CUSMA increases the threshold for heavy trucks and their major parts, currently at a 60% RVC, to a 70% RVC, through a back-loaded phase-in over seven years. Importantly, diesel cars, buses, tractors, and specialty vehicles will continue to be governed by the current NAFTA thresholds (a 60% or 62.5% RVC, depending on the vehicle).

New CUSMA automotive rules of origin requirements

To qualify for preferential tariff treatment under NAFTA, light vehicles must meet a single requirement: a 62.5% RVC. Under CUSMA, light vehicles will have to meet five requirements:

- a 75% RVC for the vehicle;
- all core parts in the vehicle must qualify as originating (i.e. meet a 75% RVC);
- 70% of the steel purchased by an assembler for use in vehicle production must originate in the FTA territory;

- 70% of the aluminum purchased by an assembler for use in vehicle production must originate in the FTA territory;
- a labour value content (LVC) requirement whereby a proportion of a vehicle assembler's production activities must be undertaken by workers earning at least US$16/hour:
    - 40% LVC for passenger cars (phased in over three years); and
    - 45% LVC for light trucks (no phase-in period).

Heavy trucks will be subject to the following requirements: a 70% RVC threshold (phased in over seven years), 70% steel and aluminum requirements, and a 45% LVC requirement (no phase-in period).

Aluminum and steel

CUSMA includes new specific provisions that will have a positive impact on the Canadian aluminum and steel sectors. NAFTA did not include any provisions to incentivize the use of North American steel or aluminum. In order to qualify for duty-free treatment, the current NAFTA requires that light vehicles (i.e. passenger automobiles and light trucks) have 62.5% originating content. When CUSMA enters into force, automakers will be required to comply with a requirement that 70% of the aluminum and steel purchased for use in the production of light vehicles qualify as originating under the CUSMA product-specific rules of origin. This requirement will apply to aluminum and steel purchased by automakers for their own parts production, as well as to purchases that are directed to parts makers for fabrication into parts. Vehicles produced by automakers that are unable to satisfy this requirement will not be eligible for duty-free treatment under the new Agreement.

Many automakers have stamping and casting operations to produce parts such as body panels and engine blocks, and purchase aluminum and steel sheet materials, bars or ingots for use in these operations. For these operations, only aluminum and steel produced in Canada, the United States or Mexico will be counted toward meeting the 70% target. Aluminum and steel imported from outside of North America and purchased by an automaker will not count toward the 70% requirement. Notably, seven years after the Agreement enters into force, for purposes of the originating steel requirement applicable to passenger cars, light trucks and heavy trucks, the criteria for determining if steel is originating will be strengthened. As such, to qualify as originating in North America seven years after entry into force, all steel manufacturing processes must occur in one or more of the parties, except for metallurgical processes involving the refinement of steel additives. With respect to aluminum, the parties have committed to reviewing—10 years after CUSMA enters into force—the rules of origin applicable to the 70% originating aluminum requirement with a view to strengthening it. This commitment does not prevent the parties from reviewing the ROO applicable to aluminum at any time.

In addition to the aluminum and steel-specific ROO requirement, CUSMA includes other provisions that are expected to have a positive impact on the Canadian aluminum and steel sectors. Specifically, the Agreement includes strengthened regional content requirements for core parts (engines, transmissions, bodies, axles, steering and suspension systems) and principal parts (including aluminum and steel intensive parts such as brakes, bearings, radiators, bumpers and wheels). CUSMA requires 75% regional content for core parts and 70% for principal parts, compared to 60% to 62.5% in NAFTA. Higher regional content requirements will incentivize both automakers and parts producers to use originating North American aluminum and steel in the production of these parts to ensure they qualify for duty-free treatment under the new Agreement.

Separately from CUSMA, on May 17, 2019, Canada successfully negotiated with the United States the elimination of the Section 232 steel and aluminum tariffs of 10% and 25% imposed on Canadian aluminum and steel respectively. As part of the agreement on U.S. Section 232 tariffs, Canada and the United States agreed to implement effective measures to prevent the importation of aluminum and steel that is unfairly subsidized and/or sold at dumped prices and to prevent the trans-shipment of aluminum and steel made outside of Canada or the United States to the other country. As part of a similar outcome, Mexico undertook to implement the same measures.

Labour value content (LVC) expenditures

There are three types of expenditures that make up the LVC requirement: material and manufacturing, technology and assembly.

- **High-wage material and manufacturing expenditures** is the proportion of the production of a vehicle (i.e. net cost) undertaken in parts and assembly plants where workers' average wage rate (without benefits) is at least US$16/hour (minimum 25-30 percentage points of a producer's vehicles). This is the only expenditure directly related to the value of each individual vehicle.
- **High-wage technology expenditures** are the wages paid out annually by the vehicle producer to its research and development (R&D) and information technology (IT) employees, expressed as a percentage of total production wages paid out annually by the producer (maximum 10 percentage points that applies to a producer's vehicles). Wages are summed across a vehicle producer's operations in the three CUSMA parties' territories.
- **High-wage assembly expenditures** relate to a producer's engine assembly plant, transmission assembly plant, or advanced battery assembly plant where workers' average wage rate is at least US$16/hour (maximum 5 percentage points that applies to a producer's vehicles).

Vehicle producers will be ultimately responsible for certifying that their vehicles meet the overall LVC requirement.

Autos side letters

The U.S.-Canada autos side letters, which entered into force on November 30, 2018, ensure that Canadian exports of passenger vehicles and auto parts (subject to annual quantitative limitations) and light trucks (e.g. pickup trucks) will be exempt from any Section 232 measures the United States may impose on these goods in the future. Should the United States impose Section 232 measures, the side letter guarantees an annual exemption from such measures for 2.6 million Canadian passenger vehicles and US$32.4-billion-worth of Canadian auto parts. Light trucks are fully exempted from any Section 232 measure and do not count against the annual exemption on 2.6 million passenger vehicles. Notably, the annual volume limits for the exemptions exceed Canada's exports of passenger vehicles and auto parts to the United States by a considerable margin, leaving room for future growth.

Both originating and non-originating passenger vehicles, light trucks and auto parts exported from Canada to the United States are eligible for the exemption. However, non-originating goods would still be subject to customs duty applied by the United States, but these cannot exceed the MFN rate that was in effect on August 1, 2018. This means that for non-originating passenger vehicles, the United States cannot apply a customs duty higher than 2.5% for passenger vehicles and higher than 25% for light trucks.

Origin procedures

The origin procedures chapter (formerly referred to as customs procedures) is used by the customs administrations of each country to administer the rules of origin of goods in order to enable the trade community to take advantage of the preferential tariff treatment afforded under CUSMA. CUSMA's origin procedures contain obligations in areas such as certification of origin, record keeping, origin verifications, advance rulings, appeals, penalties and cooperation. Accordingly, the chapter prescribes the processes necessary for traders to take full advantage of CUSMA, while at the same time providing the customs administrations with an applicable methodology to ensure that only qualifying goods receive the benefits of the Agreement.

The origin procedures have been modernized to better support today's trade environment and limit the administration costs to traders by providing for electronic processes, increased trader participation in certification and verification, and a simpler means by which to certify the origin of the good. For instance, the CUSMA certification of origin has no prescribed format but rather is a set of minimum data requirements that may be completed and submitted electronically on any document. Furthermore, either the exporter, producer or importer may complete a certification of origin and consequently participate during an origin verification. CUSMA also promotes transparent and consistent application of the rules of origin through enhanced cooperation among the parties in the application of the rules of origin, specifically with respect to the verification of the origin of the good.

Textiles and apparel

CUSMA includes a new stand-alone chapter on rules of origin and origin procedures for textiles and apparel. This chapter will preserve Canadian market access to the U.S. and Mexican markets, including the tariff preference levels from which many Canadian producers benefit, while including new measures designed to encourage the use of North American sewing thread, narrow elastics and pocketing fabric. The outcome provides greater flexibility for producers that use small amounts of non-originating materials—a measure that will help such goods qualify for preferential treatment—and maintains the NAFTA yarn-forward rules of origin while relaxing the approach for niche, vegetable-based yarns and fabrics that are often sourced from outside the CUSMA region. The chapter also includes an element that expands on an existing NAFTA provision to provide a special, facilitative pathway to origin for Indigenous textile and apparel goods. The chapter includes unique enforcement provisions and enhanced cooperation among the parties to administer effectively the rules of origin specific to this industry. In addition, unlike NAFTA, tariff preference levels (TPLs) are now exempt from the U.S. merchandise processing fee.

Customs administration and trade facilitation

The new chapter on customs administration and trade facilitation builds on the WTO Agreement on Trade Facilitation and aims to reduce the transaction costs incurred by traders by simplifying, standardizing and modernizing trade-related customs procedures to facilitate the movement of goods within CUSMA territory. The new chapter includes commitments that will lead to greater predictability, consistency and transparency in customs matters. CUSMA parties have also agreed to continue to collaborate, exchange information and explore new and innovative ways to facilitate trade following the entry into force of CUSMA.

The chapter introduces new commitments and trade facilitative concepts such as:

- a commitment for Canada to maintain procedures that apply fewer customs formalities than those applied under formal entry procedures, to express shipments valued at less than $3,300;
- advance rulings on customs valuation criteria in accordance with the WTO Custom Valuation Agreement;
- measures that encourage consistency and predictability in the tariff classification and customs valuation of goods;
- a commitment to maintain a single window system that enables traders to submit import documentary requirements electronically, with limited exceptions, through a single portal;
- an obligation to inform importers when there is a delay in the release of their goods;

- provisions that allow for circumstances in which traders may correct errors without penalty; and
- provisions that encourage customs officials in all three countries to carry out their duties with professionalism and integrity.

The chapter also includes a commitment for parties to cooperate for the purposes of assisting each other in the enforcement of laws and regulations related to customs offences and to ensure the accuracy of claims for preferential duty rates under CUSMA. It provides for the parties to strengthen their enforcement efforts and to enhance cooperation in order to promote compliance within the CUSMA territory and assist the customs administrations to prevent fraudulent acts from going undetected.

All parties have committed to maintaining minimum *de minimis* thresholds for waiving customs duties and taxes on goods of a low value imported by courier from other CUSMA parties. Under current Canadian federal law, goods imported by courier with a value of $20 or less are relieved of the assessment of customs duties and the Goods and Services Tax/Harmonized Sales Tax that would otherwise be assessed at the border. Under CUSMA, Canada agreed to maintain a *de minimis* threshold for courier shipments of at least $150 for customs duties, and $40 for taxes, at the time or point of importation when imported from the United States or Mexico. Under this provision, parties are still permitted to apply informal entry procedures, including requiring the applicable supporting documents.

Sanitary and phytosanitary measures

The modernized sanitary and phytosanitary measures (SPS) chapter reinforces and builds on provisions contained in the original NAFTA and the WTO SPS Agreement. It also reflects the parties' extensive trade and regulatory relationship in food safety and animal and plant health. Importantly, the chapter maintains each party's sovereign right to take the SPS measures necessary to protect human, animal or plant life or health, while requiring that such measures be science-based, transparent and not applied in a manner that creates unnecessary barriers to trade. The chapter also includes many new obligations, including on science and risk analysis, compatibility of SPS measures, regionalization, equivalence, audits, import checks, certification, transparency and emergency measures. It modernizes and enhances the role of the SPS Committee created under NAFTA to facilitate implementation, strengthen cooperation, and manage and address issues. The chapter also provides for the establishment of technical working groups and creates a more structured technical consultations mechanism to resolve issues cooperatively.

Trade remedies and binational panel dispute settlement

The trade remedies chapter modernizes the NAFTA obligations and reaffirms the rights and obligations of the parties under three WTO agreements: the Agreement on

Safeguards, the Anti-Dumping Agreement, and the Agreement on Subsidies and Countervailing Measures. Most importantly, CUSMA preserves the binational panel dispute settlement mechanism from chapter 19 of the original NAFTA, which provides Canadian companies affected by trade remedy measures with the choice of a transparent, independent and expeditious dispute settlement system. This will continue to ensure that anti-dumping and countervailing duty measures are applied in accordance with each party's domestic laws.

The outcome also retains the existing exclusion of CUSMA parties from global safeguard action, adds new elements that strengthen cooperation on evasion of trade-remedy duties, and enhances transparency in trade remedy investigations.

Technical barriers to trade

The CUSMA technical barriers to trade (TBT) chapter improves upon the original NAFTA standards-related measures chapter and builds upon the commitments of the three parties in the existing WTO Agreement on Technical Barriers to Trade, namely in the area of transparency. The chapter also promotes the use of international standards, provides national treatment for conformity assessment bodies (e.g. laboratories, inspection or certification bodies), and allows persons of another party to participate in the development of technical regulations, standards and conformity assessment procedures by its central government bodies.

The TBT chapter complements the parties' other CUSMA commitments and helps to secure the market access gains made in other parts of the Agreement. It ensures that technical regulations and standards are applied equally to products and goods originating from one of the three countries, and where differences arise, the chapter seeks to promote convergence of the respective practices, where possible, while protecting each party's right to regulate in its own best interests.

Sectoral annexes

CUSMA incorporates sector-specific outcomes, including those concerning pharmaceutical products, medical devices, cosmetics products, chemical substances, information communication technology, energy efficiency, alcoholic beverages and proprietary food formulas. These sectoral outcomes build on and complement the obligations in the TBT and good regulatory practices chapters, which promote regulatory transparency and predictability, while preserving each party's right to regulate in the public interest to achieve legitimate public policy objectives, such as the protection and promotion of public health, safety and the environment. In these particular sectors of the North American economy, commitments in the sectoral annexes are designed to promote effective regulation that facilitates trade between the parties.

Government procurement

NAFTA included rules and market-access commitments that allowed Canadian businesses to access the procurement markets of the United States and Mexico. Canada and the United States subsequently improved upon these commitments in the revised WTO Agreement on Government Procurement (GPA), which entered into force in 2014. Going forward, Canada and the United States will maintain access to each other's procurement markets via the GPA in lieu of including bilateral government procurement commitments in CUSMA.

The GPA includes updated procedural rules that reflect more current procurement practices, such as conducting some of the procurement process online (e.g. electronic tendering) and expanded market-access commitments. For example, the GPA provides Canadian suppliers with access to state-level procurement opportunities in 37 U.S. states, including significant markets such as New York State.

While Mexico is not a party to the GPA, Canada and Mexico will rely on the CPTPP to provide Canadian and Mexican suppliers with access to procurement opportunities in each other's markets. These include updated procedural rules that reflect more current procurement practices, such as conducting some of the procurement process online (e.g. electronic tendering).

Given that there are no government procurement obligations for Canada under CUSMA, Canadian procuring entities will no longer be bound by NAFTA's relatively low procurement thresholds. Using the GPA rules for the United States and the CPTPP rules for Mexico, Canada will have greater ability to develop domestic procurement policies and practices.

Investment

The CUSMA investment chapter was modernized to bring it into line with the recent treaty practices of the three parties. The chapter contains a comprehensive and robust set of obligations similar to those found in other FTAs, including the CPTPP. CUSMA includes provisions such as national treatment, most-favoured nation treatment, minimum standard of treatment, expropriation and compensation, and transfers that provide investors with a predictable, stable, transparent and rules-based investment climate. The chapter also includes a corporate social responsibility (CSR) provision that reaffirms the importance of encouraging businesses to respect CSR standards, such as the OECD Guidelines for Multinational Enterprises. This CSR provision provides an illustrative list of CSR areas, including gender equality and the rights of Indigenous peoples.

The main difference between the CUSMA and NAFTA investment chapters is that CUSMA will not include trilateral investor-state dispute settlement (ISDS). Under CUSMA, there will be no ISDS mechanism between Canada and the United States.

Similarly, ISDS will not apply between Canada and Mexico, but Canadian investors will continue to have recourse to the CPTPP ISDS mechanism for their investments in Mexico. Bilaterally, the United States and Mexico agreed to a bilateral ISDS mechanism for a narrow set of disciplines and sectors.

With respect to the NAFTA ISDS, the parties agreed to a transitional period of three years, during which ISDS cases can still be brought forward under NAFTA for investments made prior to the entry into force of CUSMA. Apart from this transition period, U.S. investors will not be able to launch ISDS claims against Canada, and Canadian investors will not be able to launch ISDS claims against the United States. Aside from ISDS, investment disputes can continue to be addressed through the state-to-state dispute settlement mechanism (i.e. Chapter 31, Dispute Settlement). However, if successful, the state-to-state dispute settlement mechanism does not provide for the awarding of any damages to an investor.

Cross-border trade in services

The CUSMA cross-border trade in services (CBTS) chapter builds on previous free trade agreements, including the 1995 WTO General Agreement on Trade in Services (GATS) and NAFTA by including obligations and commitments that will provide enhanced transparency and predictability for service providers.

Key features of the chapter include obligations that maintain a level playing field by ensuring that Canadian service suppliers will be afforded the same treatment as that provided by other CUSMA countries to third parties and to domestic service suppliers. The chapter also enables parties to reach a balanced outcome by allowing them to list their respective non-conforming measures for sectors that are particularly sensitive and for which a party needs to preserve policy flexibility.

Temporary entry for business persons

The modernized temporary entry chapter maintains the market access commitments negotiated under NAFTA and the parties will continue to benefit from the same preferential treatment in place since 1994. Temporary entry commitments in the original NAFTA have supported North American economic growth and development through the facilitation of labour mobility for certain highly skilled business persons. Temporary entry commitments ensure that investors can see their investments first-hand and get a feel for the local environment. Similarly, these provisions enhance service suppliers' certainty that they will be able to enter the market to fulfill contracts on-site. Beyond market access, the chapter has been updated to provide greater certainty and clarity around the application of temporary entry provisions, and to refresh the mandate of the temporary entry-working group to include broader issues related to the temporary entry of business persons, such as the processing of electronic applications.

Financial services

The financial services chapter in CUSMA modernizes the NAFTA obligations and aligns them with Canada's more recent trade agreements, such as the CPTPP and the Canada-European Union Comprehensive Economic and Trade Agreement (CETA). The chapter includes comprehensive disciplines on national treatment, most-favoured nation treatment, transfers, and market access—all scheduled on an ambitious negative-list basis[9]—along with modernized commitments on regulatory transparency, cross-border supply of financial services, and data transfer and storage. The financial services outcome reflects Canada's non-discriminatory and transparent framework for foreign participation in its financial services sector and will provide a level playing field for Canadian financial institutions to compete in Mexico and the United States.

The most significant new aspect of the CUSMA financial services chapter is that each party agreed not to impose local data storage requirements for branches and subsidiaries of financial institutions of the other parties operating in its jurisdiction, subject to a variety of public policy safeguards. Currently, all federally regulated financial institutions in Canada are required to maintain copies of certain financial and corporate records at a location in Canada. CUSMA creates an exception to this requirement for branches and subsidiaries of foreign financial institutions domiciled in the United States, Mexico and countries to whom Canada owes an international obligation under the MFN provisions of an existing trade agreement. Under the Agreement, Canada has a one-year transition period to implement the obligation after entry into force.

No changes to Canada's privacy framework are required to implement commitments contained in the financial services chapter, including on data localization. Specifically, the *Personal Information Protection and Electronic Documents Act* (PIPEDA) would continue to apply to all data collected and held by all financial institutions that do business in Canada, regardless of whether the data is processed or stored in Canada or abroad.

Telecommunications

The CUSMA telecommunications chapter enhances regulatory certainty for telecommunications service suppliers by including disciplines to ensure reasonable and non-discriminatory access to and use of telecommunications services, and by requiring telecommunications regulators to act impartially, objectively and in a transparent manner. This chapter supports Canadian telecommunications service suppliers and investors by making the parties' regulatory environments more predictable and supportive of a competitive market. Specific commitments include:

[9] In a negative-list approach, all sectors of the economy are included unless otherwise specified in the list of non-conforming measures to specific disciplines of the trade agreement's relevant chapters (e.g. cross-border trade in services, financial services and investment).

- competitive safeguards;
- interconnection of telecommunications networks;
- unbundling of network elements;
- provision of private leased circuits;
- co-location of telecommunications equipment;
- cooperation between telecommunications regulatory bodies;
- number portability;
- allocation and use of scarce resources; and
- resolution of domestic telecommunications disputes.

Digital trade

CUSMA includes a new digital trade chapter that includes commitments that are aimed at facilitating economic growth and trade opportunities through the use of the Internet, as well as addressing potential barriers to digital trade, including with respect to the transfer and storage of information (data). Specific commitments include:

- protecting personal information of users of digital trade;
- permitting the cross-border transfer of information;
- minimizing requirements placed on where data can be stored and processed; and
- not applying customs duties to digital products transmitted electronically.

As with the outcomes on financial services, provisions on digital trade are consistent with Canadian privacy laws and policies, including PIPEDA.

Intellectual property

CUSMA contains a comprehensive intellectual property (IP) chapter that sets out a regional standard in almost all areas of IP rights protection and enforcement. The chapter builds on existing international IP agreements such as the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and certain treaties administered by the World Intellectual Property Organization (WIPO), and includes obligations on copyright and related rights, trademarks, geographical indications, industrial designs, patents, pharmaceutical IP, data protection for pharmaceutical and agricultural chemical products, trade secrets and IP rights enforcement. The new Agreement also includes provisions on Internet service provider (ISP) liability, which recognizes Canada's "notice-and-notice" ISP liability regime[10] as an effective approach to addressing online infringement. The chapter will provide creators and innovators with

[10] Canada's "notice-and-notice" regime requires ISPs to forward on notices from copyright owners to Internet subscribers, alerting them that their Internet accounts have been linked to alleged infringing activities.

a predictable and transparent framework of rules across the North American marketplace.

Competition policy

The competition policy chapter furthers the parties' goal of creating a fair, transparent, predictable and competitive business environment that ultimately benefits consumers. The chapter updates measures targeting anti-competitive business practices and includes new measures to protect consumers from fraudulent and deceptive commercial activities. It also introduces obligations for procedural fairness that ensure competition authorities maintain transparent procedures and respect the rights of defendants in competition-enforcement proceedings.

State-owned enterprises and designated monopolies

CUSMA seeks to ensure a level playing field between state-owned enterprises (SOEs) and designated monopolies and the private sector, while at the same time preserving the ability of Crown corporations to provide public services.

The modernized chapter on SOEs and designated monopolies expands upon the disciplines in the original NAFTA by obligating both SOEs and designated monopolies to operate in accordance with commercial considerations and non-discrimination. It also introduces new elements to the Agreement that build upon the CPTPP framework and establish rules on non-commercial assistance and the promotion of transparency. By promoting fair competition and preventing market distortion by governments, the SOE and designated monopolies chapter will help to ensure a level playing field in the North American market.

Labour

CUSMA includes a comprehensive labour chapter, subject to the dispute settlement provisions of the Agreement, that aims to improve labour standards and working conditions in all three countries by building on international labour principles and rights. The labour chapter includes new provisions to prohibit the importation of goods produced by forced labour; address violence against workers exercising their labour rights; and ensure that migrant workers are protected under labour laws. To address the main labour rights violations in Mexico (specifically, the use of "protection contracts" or employer-dominated union agreements), the chapter also includes an Annex on Worker Representation in Collective Bargaining in Mexico, under which Mexico commits to specific legislative actions to provide for the effective recognition of the right to collective bargaining.

To address labour violations related to collective bargaining and freedom of association in a timely manner, the Agreement includes an innovative rapid-response mechanism between Canada and Mexico, and between the United States and Mexico. This enforcement mechanism would allow for the rapid deployment of a three-member panel

of labour experts to a facility to examine whether the national labour law is being respected. A negative finding by the panel could result in the imposition of penalties, including the suspension of benefits or the blocking of shipments of goods from that facility.

Environment

The CUSMA outcome strengthens and modernizes environmental obligations by integrating them into an ambitious, comprehensive and enforceable environment chapter and subjecting them to dispute settlement. The chapter includes core obligations for the parties to maintain high levels of environmental protection and robust environmental governance, including commitments to enforce environmental laws, not derogate from these laws to encourage trade or investment, and promote transparency, accountability and public participation. The chapter includes a new article that identifies seven multilateral environmental agreements (MEAs) and commits the three parties to implement their respective obligations under the MEAs.

The outcome creates new commitments to address a range of global environmental challenges, including substantive obligations to combat illegal activities and trade, promote sustainable forestry and fisheries management, conserve species at risk, implement relevant MEAs, and take measures to protect the ozone layer and address marine pollution. The chapter recognizes the important role of Indigenous peoples in the long-term conservation of the environment, sustainable fisheries and forestry management, and biodiversity conservation. The environmental provisions take into account constitutionally protected rights related to the harvesting of natural resources.

As a part of the overall outcome, the parties also agreed to a parallel Environmental Cooperation Agreement (ECA). The ECA ensures that the unique institutions that have existed since 1994 under the North American Agreement on Environmental Cooperation are retained and modernized, including the Commission for Environmental Cooperation. Through the ECA, a modernized Commission for Environmental Cooperation will continue the legacy of effective trilateral cooperation between Canada, Mexico and the United States, including on global environmental issues of importance to Canada, such as climate change.

Small and medium-sized enterprises

CUSMA includes a new chapter on small and medium-sized enterprises (SMEs) designed to complement other commitments undertaken throughout the Agreement that support SME engagement in trade. Of note, the chapter fosters cooperation among the

parties to increase trade and investment opportunities for SMEs and ensures information is available to SMEs on the obligations and functioning of the Agreement.

Competitiveness

The new chapter on competitiveness recognizes North America's unique commercial ties, extensive trade flows and integrated production platform. This chapter focuses on strengthening regional economic growth, prosperity and competitiveness through the promotion of economic integration and the enhanced competitiveness of the region's exports. The chapter formalizes trilateral cooperation previously undertaken to coordinate policies and projects that advance North American competitiveness.

Anticorruption

The new chapter on anticorruption reflects Canada's commitment to fighting corruption, which builds on our domestic anticorruption framework as well as on our efforts under existing international conventions, including at the United Nations, the Organization of American States and the OECD.

Good regulatory practices

CUSMA includes a new chapter on good regulatory practices to further the goal of working together to ensure transparent, predictable and aligned regulatory systems that foster stronger trade relations and protect citizens. The chapter recognizes voluntary regulatory cooperation as an important good regulatory practice to facilitate trade and investment among CUSMA parties. The outcome preserves Canada's ability to adopt and apply its own laws and regulations that aim to regulate in the public interest to achieve legitimate public policy objectives, such as the protection and promotion of public health, safety and the environment.

Publication and administration

The modernized chapter on publication and administration includes provisions that set out strong standards for the regulatory systems of our North American partners, in line with transparency disciplines included in Canada's more recent free trade agreements. Such provisions will create a more transparent and fairer North American market for Canadian companies. The publication and administration chapter is divided into two sections. Section A addresses the publication and administration of laws, regulations, measures and administrative proceedings, ensuring that they are developed and applied in an open, transparent and consistent manner. Section B addresses the transparency and procedural fairness for pharmaceutical products and medical devices.

Administrative and institutional provisions

Institutional provisions set the ground rules for a free trade agreement by establishing its legal and institutional structure. These provisions are incorporated into a number of different chapters in CUSMA: the preamble, initial provisions and general definitions,

administrative and institutional provisions, and final provisions. More specifically, the institutional provisions establish the free trade area among the parties and address issues such as how the Agreement will enter into force, how it can be amended and how a party may withdraw. The institutional provisions also lay out the framework for the overall management of the Agreement, including the establishment of the Free Trade Commission (comprised of government ministers) and how this Commission operates with various other bodies established under the Agreement. Fundamentally, the institutional provisions contribute to the effective administration and operation of the Agreement and reflect additional obligations that the parties have undertaken in cross-cutting areas.

Dispute settlement

The CUSMA outcome improves upon NAFTA by ensuring that arbitral panels are created automatically upon request in order to address disputes with respect to the interpretation of and compliance with the Agreement. Specifically, the Free Trade Commission (of ministers) will no longer be involved in the dispute settlement process, meaning that a panel will be automatically established upon request. In addition, the parties made changes to ensure that a roster of potential panelists is created and updated. CUSMA also includes new requirements to provide for additional clarity and transparency on procedures regarding the operation of panel hearings. If an arbitral panel finds that a party has failed to implement its obligations under the Agreement, that party must remove the violation. If the violation is not remedied, the winning party is automatically entitled to suspend benefits of equivalent effect (such as increased import duties). Almost all of the obligations in the Agreement, including those related to labour and the environment, are subject to this dispute settlement system.

Exceptions and general provisions

The exceptions and general provisions chapter sets out commitments made between the parties to exclude certain areas from the Agreement or to set out obligations that apply more generally across the Agreement. Some of the exceptions are applicable to the entire Agreement while others only apply to certain chapters.

Generally, these exceptions are designed to ensure that CUSMA parties maintain the right to take action in the public interest, including with respect to health, the environment and national security. The chapter also sets out where parties may impose measures that would otherwise be inconsistent with obligations, including measures to pursue certain policy objectives or to protect confidential information. For Canada, the exceptions to the Agreement preserve key outcomes of the CUSFTA and NAFTA with respect to cultural industries—which preserve Canada's flexibility to adopt and maintain programs and policies that support the creation, distribution and development of Canadian artistic expression and content. In addition, for the first time in a free trade agreement, Canada has secured a general exception on Indigenous peoples' rights,

which clearly confirms that Canada's commitments under CUSMA do not impact its ability to adopt or maintain measures to fulfill its legal obligations to Indigenous peoples.

Macroeconomic policy and exchange rate matters

For the first time in a free trade agreement, CUSMA includes a chapter dedicated to macroeconomic policy and exchange rate issues. It demonstrates the parties' unified commitment to avoiding currency manipulation, and sets out a high standard for transparency and public reporting, creating a model that can be used for global adoption. Specifically, it commits the three parties to maintain market-determined exchange rates and refrain from competitive devaluation, and sets out enforceable rules for a high level of transparency and public reporting on exchange rates and other macroeconomic issues.

MODELLING FRAMEWORK AND ANALYSIS

The negotiations to modernize NAFTA took place in the context of the broader U.S. objective to rebalance the Agreement in favour of the United States or completely withdraw from the Agreement. In addition, as the negotiations progressed, Canada was facing a risk of continued U.S. Section 232 tariffs on steel and aluminum products from Canada, and threat of similar tariffs on automobiles and auto parts. Under these circumstances, Canada was presented with two choices: risk the consequences of a U.S. withdrawal from NAFTA or pursue a modernized Agreement. This report therefore presents the potential economic impact of CUSMA compared to the no-NAFTA reference point under which the United States withdraws from NAFTA and continues to impose Section 232 tariffs on steel and aluminum.

The modelling results represent the potential benefits of NAFTA preserved by CUSMA, the removal of Section 232 tariffs on the Canadian steel and aluminum industries, as well as the incremental impact of the implementation of the CUSMA outcomes.

Modelling framework

The economic impact assessment of CUSMA is based on simulations using a dynamic computable general equilibrium (CGE) model of global trade. This model follows the structure of the Global Trade Analysis Project (GTAP) model developed and supported by Purdue University.[11]

Baseline data development

The data used for this modelling exercise is based on the GTAP database version 10, which benchmarks all bilateral trade flows, trade protection and domestic support to 2014.[12] The model projects the economic activities in Canada and the rest of the world to 2020, when CUSMA policy changes would be introduced, and onward to 2025. The modelling results represent the benefits of NAFTA preserved under CUSMA in addition to the incremental changes under CUSMA. This long-term projection to 2025 is necessary to allow for structural adjustment in the economy during the implementation period. The underlying data are values in U.S. dollars at 2014 prices.

Since 2014, a number of bilateral FTAs have been concluded and implemented, notably CETA and CPTPP, as have certain unilateral liberalization initiatives undertaken by partner countries. To have a better representation of the policy environment as it is today, tariff data has been updated to include all these changes.

[11] Global Trade Analysis Project, Department of Agricultural Economics, Purdue University. https://www.gtap.agecon.purdue.edu/.

[12] Information for 2014 is the latest available.

For the purpose of this study, the global economy is disaggregated into 57 sectors, nine economies (Canada, the United States, Mexico, China, Japan, South Korea, Chile, Peru and India[13]) and an aggregate region comprising the rest of the world.

As a note of caution, the modelling results should be considered in the context of both the advantages and limitations of the CGE model being used. Specifically, the CGE model can reflect only the expansion of trade in products already traded in a given bilateral trading relationship (i.e. the intensive margin of trade); it cannot predict the creation of trade in new product areas (i.e. the extensive margin of trade). Further, the model only allows for analysis of gains from liberalization in goods and services trade and investment, and does not include gains from liberalization and enhanced economic cooperation in other areas. As a result, this assessment could be expected to underestimate the gains from liberalization.

Labour, gender and other effects

Given the importance of better understanding the impacts of FTAs on domestic markets, this analysis utilizes a labour market module building on the existing dynamic CGE model to assess the labour market effect of CUSMA, taking into account gender, age and the distribution of Canadian workers across different occupations.

This section provides a non-technical overview of the modelling methodology developed. A more detailed presentation of the data framework and the labour market module is set out in Annex 1. A more technical explanation of the labour market module is available upon request.

This newly developed labour market module expands the traditional modelling approach in fundamental ways as it addresses many shortfalls in the traditional modelling framework by incorporating unemployment, labour force participation, occupations, gender and youth into the model.

Labour market impacts

Traditional CGE models assume full employment and thus do not analyze potential unemployment that might be generated by labour market frictions as the economy adjusts to structural changes induced by trade agreements.

In reality, the labour market is never fully employed. There is always a high degree of job turnover in an economy: for example, workers may leave one job for another to take advantage of a better offer, or take a new job after being laid off from a previous one. Accordingly, there is a certain amount of observed “frictional” unemployment at all stages of the business cycle. The introduction of frictional unemployment into a quantitative framework for analysis enriches the understanding of the labour market and

[13] These countries represent the NAFTA countries’ major trading partners.

highlights the importance of frictional costs in job seeking, which could induce some workers to drop out of the labour force even in the presence of an overall rising economy.

Similarly, trade liberalization can generate both smooth job transitions and involuntary unemployment as some firms expand and create new higher-paying jobs, while others are forced to cut back output and reduce their workforce in response to loss of market share due to imports.

Further, trade liberalization is also likely to have an impact on labour force participation: higher real wages and associated job creation may encourage those who are not in the labour force to seek work.

Workers across occupations

Trade liberalization does not uniformly benefit all workers and all occupations, but instead results in job gains in some sectors and job losses in others. As a result, there has been increased emphasis on labour market adjustments that facilitate mobility across occupations, particularly given that trade liberalization could shift economic opportunity across firms and industries. Mobility across occupations is generally more difficult than mobility across industries within the same occupations. For instance, it is easier for a plumber in the construction industry to find a job as a plumber in the retail industry than for a plumber to change occupation and become an electrical engineer.

Under traditional economic modelling, differences in the professional composition of the labour force demanded by different sectors are not taken into account, and the potential consequences of a misalignment between skills available and skills in demand cannot be evaluated. Introducing a more detailed breakdown of occupations in the labour market is an important step to improving the ability to anticipate, and to respond to, the pressures on labour markets resulting from trade liberalization.

Gender

Providing equality of opportunity for women and men in the workplace is beneficial for productivity. The Government of Canada has made gender equality and women's economic empowerment a top priority. The lack of gender-disaggregated data in the traditional CGE framework has limited the ability to do an in-depth gender analysis. The introduction of a gender breakdown by occupation and sector thus greatly improves the ability to quantify potential impacts of a trade agreement from a gender perspective.

Youth

It is also important to consider the effects of trade on youth, a traditionally under-represented group in international trade and in Canada's economy more broadly. Youth engagement in trade as entrepreneurs, particularly in technology-enabled sectors, contributes to the ability of the economy to respond to new trade opportunities. Given

that young people are more likely to experience all types of unemployment (i.e. frictional and involuntary) particularly during periods of economic downturn, the creation of new economic opportunities through trade liberalization could be especially beneficial for young people integrating (or re-integrating) into the workforce. Introducing an age disaggregation into the quantitative analytical framework allows for analysis of the impact of trade agreements on the distribution of opportunities across ages, which in turn may inform domestic policy in terms of training programs and other support for young entrepreneurs.

A U.S. withdrawal from NAFTA

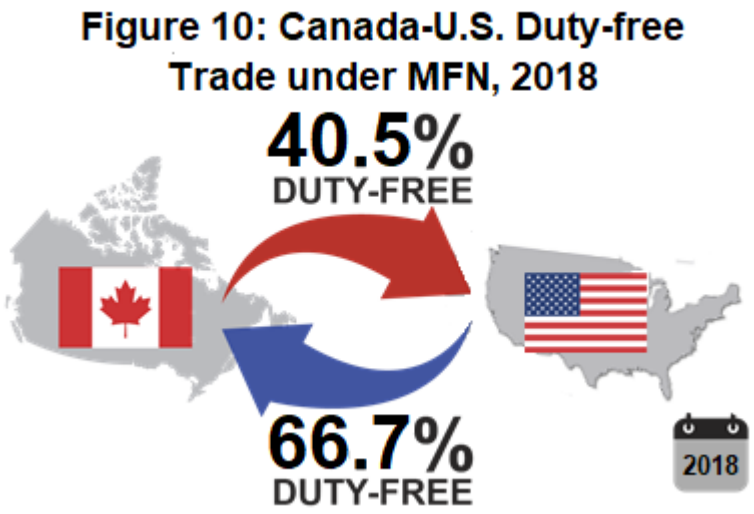
This section considers the potential consequences if the United States were to withdraw from NAFTA and continue its unilateral Section 232 tariffs on steel and aluminum from Canada. For the purposes of this assessment, it is assumed that Canada and the United States would not revert to trading under the Canada-United States Free Trade Agreement (CUSFTA). This is in part due to the fact that certain administrative and regulatory actions would have been required on the part of the United States to bring that earlier agreement back into force. As a result, trade between Canada and the United States would be governed by WTO rules and tariffs, whereas Canada and Mexico would continue to trade under NAFTA.

In the event of a U.S. withdrawal, the following key assumptions were made:

a) NAFTA preferential tariff treatment would cease. Trade between Canada and the United States would be governed by WTO rules and MFN tariffs would be applied according to each country's current applied MFN tariffs. Based on the average tariff by product, the trade-weighted MFN tariff is estimated at 1.7% for Canadian shipments to the United States and 2.5% for U.S. shipments to Canada.
b) Section 232 tariffs on steel (25%) and aluminum (10%) that started in May 2018 would remain in place.
c) Duty-free treatment currently provided for under WTO rules would continue, and the current original equipment manufacturer (OEM) tariff waiver for auto parts imported into Canada would remain in place. Higher tariffs would be applied only to a small proportion of products, such as trucks, footwear and apparel, for the United States. In 2018, about 40.5% of Canadian exports to the United States and 66.7% of U.S. exports to Canada were MFN duty-free. The share of duty-free trade between Canada and Mexico was even higher: about 75.1% of Canadian exports to Mexico and 57% of Mexican exports to Canada were duty-free in 2016 (see Figures 10 and 11).[14]

[14] 2016 information for Mexico's tariffs is the latest available.

d) For the purposes of this study, Canada's global TRQ access for chicken, turkey and egg products was assumed to be solely in accordance with its WTO commitments.



Source: Global Affairs Canada, Office of the Chief Economist

Source: Global Affairs Canada, Office of the Chief Economist

e) The chapter 19 binational panel review of anti-dumping and countervailing duty measures would cease to be available between the United States and Canada, and challenges to U.S. measures in this area would have to proceed in U.S. courts and/or at the WTO. Of note, the binational panel system can lead to the refund of duties collected, which is not available under WTO dispute settlement. The loss of this dispute settlement mechanism would therefore remove the potential for duty refunds in cases where the original calculation of duties was too high. The economic impact of such a change is difficult to assess and would involve significant speculation about future U.S. trade remedy actions and the potential judgements of U.S. courts. As such, we have not attempted to estimate this impact.
f) On government procurement, Canada would continue to access the U.S. procurement market via the GPA (as in the CUSMA outcome), while Mexico and Canada would continue to be bound by commitments on government procurement in NAFTA and CPTPP.[15]
g) For cross-border trade in services, Canada would rely on the GATS for the United States and existing FTA commitments in the case of Mexico (i.e. NAFTA and CPTPP). However, there are no comparable WTO obligations related to the temporary entry of business persons, meaning important NAFTA advantages in this area would cease to exist. Notably, Canada's commitments in services and government procurement under CPTPP and CETA would be maintained and there would be no rollback in commitments regardless of the U.S. withdrawal from NAFTA. These commitments have been integrated into the baseline of the economic modelling.
h) Canada's trade with Mexico would continue to be governed by NAFTA rules.

Importantly, in this study we have not made any assumptions regarding the potential implementation of U.S. Section 232 tariffs on automotive products.

Implementation of the CUSMA outcome

CUSMA preserves NAFTA's virtually tariff-free market access for Canadian exports, strengthens the integration of the North American automotive sector, reinforces Canada's relative position as a competitive investment destination for automobile and auto-parts production, and provides new market access opportunities into the U.S. market while at the same time preserving Canada's system of supply management. The new Agreement also modernizes provisions in line with Canada's more recent FTAs to

[15] Mexico's government procurement commitments under NAFTA are essentially the same as under the CPTPP.

help reduce red tape, facilitate trade and protect the Government's right to regulate in the public interest, including for health and safety.

On May 17, 2019, and as a condition for moving towards ratification, Canada secured the removal of U.S. Section 232 tariffs on approximately $17.2 billion worth of Canadian exports of steel and aluminum products to the United States. The removal of U.S. Section 232 tariffs on Canadian steel and aluminum products was a key element in clearing the path towards implementation and ratification of the Agreement. These unilateral tariffs threatened the high level of integration among Canadian and U.S. steel and aluminum producers and long-established cross-border value chains, and were contradictory to the long-standing Canada-U.S. security partnership.

Similarly, the imposition of Section 232 tariffs as high as 25% on Canadian automobiles and auto-part exports to the United States would have had a significant negative impact on Canada's auto industry and would have undermined decades of Canada-U.S. commercial cooperation. For this reason, it was imperative that Canada secure an exemption from any Section 232 measures on automobiles and auto parts as part of the CUSMA outcome. In a bilateral exchange of letters on November 30, 2018, Canada secured an exemption from any potential U.S. Section 232 tariffs on automobiles and auto parts for up to 2.6 million automobiles and US$32.4 billion in Canadian auto parts imported into the United States annually. Light trucks (e.g., pickup trucks) are fully exempt from any potential Section 232 tariffs. These levels are sufficiently high to provide both stability and room for growth for Canada's automotive industry in a scenario where Section 232 tariffs were imposed.

Quantitative interpretation of key CUSMA outcomes for economic impact assessment

CUSMA modernizes NAFTA and provides new rules to facilitate greater trade between parties. However, there are limitations on which new provisions in the Agreement can be modelled economically. Most importantly, data must be available and it must be analytically feasible to model the results. For new FTAs the focus of the economic impact assessment is usually placed on gains from tariff reductions; however, in the case of CUSMA, tariff elimination took place under NAFTA or in some cases its predecessor, the CUSFTA. As a result, the quantitative assessment of CUSMA focuses on the following new provisions in the Agreement:

- TRQs for agricultural products;
- automotive rules of origin;
- data localization commitments for financial services; and
- customs administration and trade facilitation, and origin procedures.

These provisions were selected based on the expected magnitude of their economy-wide impact, data availability and analytical feasibility.

Some provisions under CUSMA could also help reduce policy uncertainty in certain areas such as services, investment and digital trade, and result in a positive impact on businesses; however, modelling such gains is challenging and relies heavily on the assumptions made. Therefore, these types of benefits were not evaluated in this study. Furthermore, many of these obligations have already been implemented by Canada under CETA, and by Canada and Mexico under the CPTPP.

Quotas for sugar and sugar-containing products

Canada will continue to enjoy existing quota-based access into the U.S. market for Canadian refined sugar and sugar-containing products upon the implementation of CUSMA. In addition, the new Canadian quota access to the United States for refined sugar and sugar-containing products is estimated to be valued at US$20 million. For the purposes of this study, these quotas are assumed to be fully utilized.

Quotas for eggs, poultry and dairy

While Canada provided incremental market access to the United States on eggs and poultry, it is estimated that, due to the new calculation methodology, there will be a limited impact on the Canadian sector with regards to the imported volume of poultry and eggs into Canada, even though CUSMA specifically secures U.S. access to the Canadian chicken and egg market and could increase global access to the Canadian turkey market.

The U.S. quota access to the Canadian dairy market is estimated to be valued at US$ 300million. For the purposes of this study, the quota is assumed to be fully utilized. Furthermore, the study estimates that there would be no significant change in trade patterns with respect to Canadian dairy products being exported to the United States. While CUSMA provides Canada with new market access to the United States for certain dairy products, export gains from this access are expected to be limited primarily due to lower returns in the U.S. market and non-tariff measures that continue to limit Canadian exports to the U.S. market for dairy products.

Automotive rules of origin

To estimate the potential impact of strengthening rules of origin requirements for the automotive sector, the first step is to determine the share of vehicles that meets the new automotive rules of origin (ROOs) in each country using data from the *American Automobile Labeling Act*, trade and other production and price data.[16] The economic analysis focuses on the three new rules: regional value content, labour value content and the core parts requirement. Public data for the regional value content of steel and aluminum used in auto assembling is not currently available, but automotive

[16] National Traffic Highway Safety Administration, “Part 583, *American Automobile Labeling Act* Reports.” https://www.nhtsa.gov/part-583-american-automobile-labeling-act-reports.

stakeholders in Canada were consulted and did not express concerns with meeting this requirement. Vehicles that would meet all the new requirements were considered to continue to receive duty-free access under CUSMA. Vehicles that would not meet any one of the three requirements were considered to be subject to MFN tariffs in the CUSMA market—i.e. 2.5% for the U.S. market, 6.1% for the Canadian market and 20% for the Mexican market.

Based on our analysis, Canada has the highest percentage—about 65.7%—of vehicles in volume produced domestically that would currently meet the new CUSMA ROOs, followed by the United States and Mexico. With respect to vehicles assembled in Canada and exported to the United States, almost 70% would meet the new CUSMA rules of origin, which is also the highest of any pair of trading partners. Mexico has the largest share of vehicles exported to partner countries that would fail to meet the new origin requirements.

These figures are based on proportions of vehicle units produced. However, in value terms,[17] 74.4% of the value of Canada's vehicle exports to the United States and 67.8% of the value of Canada's vehicle exports to Mexico would currently meet the new ROOs.

Overall, if combining assembled vehicles and parts together, currently about 19.1% of Canadian automotive exports to the United States and 9.6% of Canadian automotive exports to Mexico would fail to meet the new CUSMA automotive ROOs, and would therefore be subject to MFN tariffs.

In this analysis, we assume that the vehicle manufacturers would adjust their sourcing of parts to comply with the new ROOs up to the point that the cost of doing so would be equivalent to MFN tariffs of 2.5% for products shipped to the United States and 6.1% for products exported to Canada. This would likely incentivize North American production and benefit Canadian automotive parts producers as well as Canada's steel and aluminum sectors. However, if the costs of sourcing adjustments were higher than the MFN tariffs, we have assumed that the manufacturers would simply choose to pay the non-preferential MFN duties on engines, transmissions, other parts and vehicles that are noncompliant. This assumption implies the application of MFN auto tariffs between CUSMA parties on all assembled vehicles that fail to meet the new rules of origin requirements. The application of MFN tariffs or adjustments to meet the new ROO could result in higher prices for consumers and overall higher costs of production due to increased sourcing of more expensive parts from within the region. This would likely affect competitiveness and, as a result, other automotive producing countries outside North America—such as Japan, South Korea, Germany and China—could benefit from

[17] The value is equal to the volume multiplied by the average manufacturer's suggested retail prices (MSRP).

this change. Overall, these changes would have a negative impact on automotive production in Canada, the United States and Mexico.

Financial services

Canada agreed to provisions on local data storage requirements for branches and subsidiaries of foreign financial institutions, subject to a variety of public policy safeguards. Currently, all federally regulated financial institutions in Canada are required to maintain copies of certain financial and corporate records at a location in Canada. Under the Agreement, Canada has a one-year transition period to implement the new obligation after entry into force.

As a result of this commitment, Canada's investment environment for both banking and insurance would improve. This improvement can be assessed through use of the OECD's Services Trade Restrictiveness Index (STRI). As part of the study, Canada's STRI scores for banking and insurance have been updated to account for the changes under CUSMA (see Table 1). For future investment in insurance services, Canada's STRI score improves from 0.2084 before CUSMA to 0.2018 after CUSMA. Similarly, the STRI score for investment in banking services improves from 0.1783 to 0.1663. The technical explanation of economic modelling of the effect of legislative amendments is presented in Annex 2.

Table 1 – Change in Canada's STRI Score for Financial Services

Sector	STRI Score		
	Before CUSMA	**After CUSMA**	**Change**
Insurance	0.2084	0.2018	-0.0065
Banking	0.1783	0.1663	-0.0120

Source: Global Affairs Canada, Office of the Chief Economist.

The United States and Mexico already comply with CUSMA commitments in financial services; therefore, no change would be expected in their STRI score following entry into force.

Customs administration, trade facilitation and origin procedures

CUSMA improves on NAFTA outcomes in the areas of customs administration, trade facilitation and origin procedures. The modernized chapter on customs administration and trade facilitation would reduce administrative and financial burdens on traders, as well as enhance border efficiency and reliability. The origin procedures have also been modernized to minimize the burden on traders by providing for electronic processes, increased trader participation in certification and verification, and a simpler means by which to certify the origin of the good.

To quantity the effect of improvements in the areas of customs administration, trade facilitation, and origin procedures, the OECD Trade Facilitation Index (TFI) is used to measure the improvement in each OECD TFI subcomponent (see Annex 3 for more details). For the component related to origin procedures, the benefits would apply to dutiable imports of industrial products only among three countries; for customs administration and trade facilitation, benefits would apply to imports of all industrial products.

Canada and the United States score very highly in many subcomponents of the OECD's TFI. Therefore, the scope for improvement as a result of CUSMA would be limited.

Canada's TFI score improves to 19.238 after CUSMA from 18.875 before CUSMA, a net change of 0.363 (see Table 2). The improvement would be most significant for Mexico, from 16.350 before CUSMA to 16.852 after CUSMA. For the United States, the net improvement is 0.321. The estimated net change in TFI for each country is used in the economic model to assess the potential gains from improvements in customs administration, trade facilitation and origin procedures.

Table 2 – Change in OECD Trade Facilitation Index

	Before CUSMA	After CUSMA	Change
Canada	18.875	19.238	0.363
United States	20.060	20.381	0.321
Mexico	16.350	16.852	0.502

Qualitative assessment of key CUSMA outcomes

From a qualitative perspective, the assessment also considered certain new provisions in CUSMA that are not quantifiable but expected to have a net positive GDP impact by facilitating trade between the three countries and strengthening the North American competitiveness globally. In particular, this includes updated provisions on agricultural biotechnology, rules of origin for crude oil and textiles and apparel, non-tariff barriers, cross-border trade in services, financial services, investment, intellectual property, digital trade, labour and environment, and dispute settlement.

Agriculture

In addition to the market access outcomes identified in the qualitative section above, the agriculture chapter includes, among other provisions, forward-looking provisions for agricultural biotechnology that increase transparency and establish practical, trade-facilitative approaches to getting safe products to market. This will help increase innovation, transparency and predictability in the North American agricultural and agri-food market; however, it is difficult to quantify the benefits economically.

Diluent and the rule of origin change for crude oil

In the CUSMA outcome, the parties updated the rule of origin for crude oil to ensure that Canadian crude oil exports to the United States and Mexico qualify as originating under the Agreement. In recent years, producers of crude oil have occasionally used non-originating diluent. The diluent is removed from the crude at its point of destination and recycled through the North American pipeline grid. As a result, non-originating diluent has been mixed with originating diluent. This has made it very difficult for exporters to determine whether the diluent used to enable exports of crude oil is originating or not. As a result, many have opted to not claim NAFTA preference when exporting and instead pay the applicable U.S. MFN tariffs and the U.S. Merchandise Processing Fee (MPF). While it is not possible to model the benefits of this particular change (as the MPF applies on the value of individual shipments for which data is not available), Canadian industry has estimated that these duties and MPF charges amount to approximately $60 million a year. The change to the rules of origin for crude oil in CUSMA will allow for the use of non-originating diluent, thus making it possible for Canadian crude exporters to claim CUSMA preferential tariff treatment and remove the need to pay the U.S. tariffs and MPF.

Tariff preference levels for textile and apparel goods and the U.S. MPF

Under the CUSMA outcome, trade under the tariff preference levels for textile and apparel goods will no longer be subject to the U.S. MPF. The MPF is applied on a per shipment basis and is set at 0.3464% of the value of a shipment, with a minimum of US$25 and a maximum of US$508.70 per shipment. Removing the MPF will alleviate financial and paperwork burdens for Canadian exporters. However, given that per shipment information is not available, we could not quantify the savings that would result from the waiving of the MPF on the $763 million in Canadian tariff preference level exports to the United States in 2019.

De minimis

There is insufficient data, both pertaining to coverage and the behavioural response of consumers, to accurately quantify the revenue impacts of changes in the *de minimis* waiver of customs duties and taxes. However, the anticipated impacts can be qualitatively assessed.

Overall, given the narrow nature of the changes, the provision would have a negligible impact on the overall Canadian economy. Canada already provides streamlined customs clearance procedures, including streamlined documentation and other entry procedures in separate frameworks. Further, Canada has already separated customs release from the payment of applicable customs duties and taxes. For security reasons, all importations into Canada remain subject to examination, and importations of any value are subject to verification to ensure compliance with Canada’s import requirements.

Despite being negligible at the macroeconomic level, the changes could give rise to discernible effects on some individual retailers and producers in Canada, as well as employment and wages at the affected firms.

Some domestic consumers could be expected to benefit from limited price savings on their purchases from U.S. and Mexican retailers, resulting from the non-application of duties and taxes associated with the increased *de minimis* thresholds. That said, in many cases the shipping costs associated with low-value imports could offset the relative competitive advantage of the items being relieved of duties and taxes. While this measure may be positive for some consumers, as noted above, some workers could be impacted as a result of possible reduced business activity in affected domestic sectors, principally in retail.

The business sector in Canada could experience some small negative impacts. Any potential impacts would be most likely in the domestic retail sector, including both “bricks and mortar” stores and e-commerce retailers in Canada, which could face increased competition and lower demand as more consumers may import more low-value goods directly from foreign U.S. and Mexican retailers. The economic impact of reduced business activity would be greatest where goods purchased by Canadians from foreign U.S. and Mexican retailers are displacing purchases of goods sold in Canada, particularly those with high Canadian content. In addition, secondary effects could be experienced by manufacturers and wholesalers in Canada. That said, any negative business impacts could be mitigated by consumers spending their price savings in the domestic economy.

Government revenues could be lower, with reductions in customs duties, business income tax and sales tax revenues, relative to what they otherwise would have been.

Few gains for Canadian exports would be anticipated, owing in large part to geographic restrictions often included in Canadian retailers’ purchase contracts for international brands that prevent them from selling to purchasers located outside of Canada.

Finally, there could be an increase in imports from the United States and Mexico owing to the increased competitive advantage that U.S. and Mexican retailers would gain over domestic retailers and retailers outside the CUSMA region, stemming from lower customs duties and taxes. There also could be some decline in imports from retailers based in non-CUSMA countries.

Non-tariff barriers to trade

The CUSMA outcome will enhance regulatory transparency and predictability, which will provide added assurance for exporters that their goods will make it to market and not be delayed by unjustified or unclear measures at the border, and that companies have sufficient time to adjust to new regulations and other requirements. The outcome will also ensure that Canada’s agricultural and processed food exports can rely on sanitary

and phytosanitary measures that are risk-based and that increase predictability of market access, so that products make it to market in a reasonable amount of time. Given the nature of these changes, it is difficult to quantitatively model the potential impacts of these improvements.

Cross-border trade in services (CBTS)

Canada will benefit from the modernized CBTS chapter in CUSMA, which will provide continued secure and predictable access to markets in the United States and Mexico. As the outcomes relate largely to security of existing access, the benefits are qualitative in nature and thus would not necessarily be captured by quantitative economic modelling.

Qualitative improvements are found with regard to the market access obligation that is now captured under CUSMA. This obligation is based on NAFTA's provisions and Annex on Quantitative Restrictions, and was further developed in numerous bilateral FTAs (including CPTPP). Under this obligation, parties agreed to list improved commitments from the baseline of GATS 1995, which reflect the domestic regime that parties were willing to bind to in 2005 under GATS during the WTO Doha Round negotiations (this was also the CPTPP result).[18] In this regard, Mexico has provided commitments commensurate with its CPTPP commitments and the United States has taken on commitments commensurate with those included in the Trans-Pacific Partnership negotiations. Overall, these commitments provide for certainty and predictability in market access, but do not account for a significant quantitative market access gain.

As part of the CUSMA CBTS outcome, Canada agreed to rescind the decision of the Canadian Radio-television and Telecommunications Commission (CRTC) to prohibit simultaneous substitution of U.S. advertising during the broadcast of the Super Bowl. The CRTC decision was quashed by the Supreme Court in Canada on December 19, 2019. The rescission of the decision will not induce a significant economic impact from the NAFTA benchmark, given that simultaneous substitution of advertising was permitted until February 2017 and became permitted again in December 2019 following the court decision referenced above. Canada also agreed to provide U.S.-based programming services specializing in home shopping access to the Canadian market by authorizing them to negotiate affiliation agreements with Canadian distributors. While this may increase competition in the Canadian teleshopping market, the change will not induce a significant economic impact from the NAFTA benchmark.

Financial services

Similar to the outcome in the chapters on cross-border trade in services and investment, the economic benefits of financial services in CUSMA are moderated by the relatively ambitious level of existing Canadian and U.S. commitments under the 1995 GATS. In

[18] This assessment on the market access obligation also applies to commitments relating to the supply of a service in the territory of a party by a covered investment (i.e. mode 3).

particular, both Canada and the United States made significant market access and national treatment commitments at the time, which reflected their relatively open and liberal financial service sectors. Both countries also scheduled their commitments according to the GATS Understanding on Commitments in Financial Services, which includes an expanded range of provisions, such as obligations on commercial presence, the transfer and processing of information, and cross-border trade in financial services.

Mexico's commitments under GATS, in contrast, were more limited. In particular, Mexico reserved the right to maintain limitations (that have since been liberalized) on foreign ownership of financial institutions and it did not schedule commitments under the GATS Understanding on Commitments in Financial Services. While Mexico's CUSMA commitments represent a significant improvement when compared to GATS, they are consistent with the updated market access offer that Canada secured from Mexico under CPTPP. As such, the additional benefits of CUSMA are modest for Canadian financial service providers seeking to access or operate in the Mexican market.

On the aggregate, the economic benefits of the changes in financial services in CUSMA are therefore largely limited to provisions under CUSMA that reduce policy uncertainty, in particular with respect to the U.S. market. These include provisions that lock in market access and other commitments enjoyed by Canadian financial institutions and in many areas capture future liberalization undertaken by the parties. In addition, CUSMA provides additional investment protections such as compensation for expropriation, and minimum standard of treatment.

The financial services chapter does, however, contain two important new commitments. First, the parties agreed to revise a government's ability to impose data localization requirements on branches and subsidiaries of foreign financial institutions, subject to a variety of public policy safeguards (see the Financial services section, above). Second, the parties committed to an expanded range of listed financial services, such as portfolio management and electronic payment card services, that are permitted to be provided on a cross-border basis. Although these commitments only bind services that are permitted under each CUSMA country's current policy framework—and are not likely to result in new economic benefits—they should nonetheless support business confidence and the long-term growth of cross-border financial services trade.

The United States and Mexico must also provide reciprocal treatment for Canadian financial institutions operating in those markets. However, the data localization commitment does not require a change in either of those countries' financial sector regulatory regimes. Therefore, the benefits to Canadian financial institutions operating in these markets are largely of a qualitative nature (business confidence).

In line with the outcome in the investment chapter, investor-state dispute settlement will not apply to Canada for financial services in CUSMA. A further discussion of the

potential economic impact of the ISDS outcome on inbound FDI, which equally applies to the financial services sector, is discussed in the Investment section, below.

Investment

Considering Canada's strong legal system and respect for the rule of law, we do not anticipate that the removal of the ISDS mechanism would have a significant impact on U.S. investors' decisions to invest in Canada. Similarly, we do not foresee that Canadian investments in the United States would be significantly impacted.

Once CUSMA enters into force, it is possible that the number of U.S. investors bringing claims against Canada could increase before the three-year transition period expires. This would require resources to defend these cases and to pay damages if Canada were found to be in breach of its NAFTA investment obligations. This potential impact has not been incorporated into the economic impact assessment, given that it would require speculation on potential future investor actions and future decisions of an arbitral panel.

Following the expiry of the three-year transition period for the NAFTA ISDS mechanism, it is possible that an increased number of companies could seek government intervention to resolve investment disputes with the United States, including by initiating a state-to-state dispute under CUSMA. On the other hand, Canada will not be subject to the payment of any future damages under ISDS with the United States. Between 1994 and 2019, Canada paid approximately $275 million in penalties and legal fees related to ISDS cases.

Compared to the scenario where the United States withdraws from NAFTA, the CUSMA outcome would represent a gain with respect to transparency and predictability with the United States, even without an ISDS mechanism, given that the only multilateral agreements relating to investment, the WTO Agreement on Trade-Related Investment Measures and the GATS are not comparable to a comprehensive investment chapter. There would be no impact with Mexico as it is a party to the CPTPP, which contains ISDS provisions.

Data transfer and storage (digital trade)

In practice, the provisions in the CUSMA digital trade chapter are expected to result in gains of a more qualitative nature. Any quantitative gains directly resulting from the digital trade chapter are expected to be limited as the market access commitments across other chapters in NAFTA apply to goods and services traded both digitally and physically. Furthermore, the chapter does not include any provisions that require Canada, Mexico or the United States to change any domestic laws or regulations. Instead, the Agreement's obligations provide for enhanced predictability and certainty for consumers and businesses engaging in trade over the Internet by entrenching existing practices in the form of trade commitments.

Intellectual property

CUSMA contains a comprehensive intellectual property (IP) chapter, which sets out a regional standard in almost all areas of IP rights protection and enforcement (e.g. copyright and related rights, patents, trademarks, geographical indications, industrial designs, pharmaceutical and agricultural chemical data, as well as border, criminal and civil enforcement of IP rights, including the enforcement of trade secrets). The CUSMA IP chapter will provide creators and innovators with a predictable and transparent framework of rules across the North American marketplace.

In most areas, Canada's domestic law and policy is already consistent with the CUSMA outcome on IP. However, Canada will be required to make certain changes to its IP regime upon the Agreement's entry into force in the areas of copyright (criminal remedies in respect of rights management information, or RMI; increases in certain specific copyright terms of protection, such as 75 years for published sound recordings from the date of publication, up from Canada's current term of 70 years from publication); and IP rights enforcement (ex officio border authority to detain suspected counterfeit trademark and pirated copyright goods in transit; and new criminal offenses for the unauthorized and willful misappropriation of a trade secret). Canada will also be required to provide full national treatment in respect of copyright and related rights, which could have associated costs for businesses when making certain uses of sound recordings whose makers were U.S. nationals at the time of first fixation of the sound recordings. This potential cost is difficult to quantify because it would depend on the royalty rates established by the Copyright Board of Canada or negotiated between businesses and relevant U.S. rightsholders.

Canada also has transition periods for certain IP commitments, which begin upon the entry into force of the Agreement. Canada has a four-year transition period to complete its accession to the *Brussels Convention Relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite*. Canada has a 4.5-year transition period to provide patent term adjustment (PTA) to compensate patent applicants for unreasonable patent office delays. Under this commitment, patent applications would be eligible for PTA if they are filed after the entry into force of the Agreement or two years after signing of the Agreement (December 1, 2020), whichever of the two dates is later, but only if there were "unreasonable" delays in the granting of the patent. Canada also has a 2.5-year transition period to provide a general copyright term of protection of "life of the author" plus 70 years for works of authorship (up from Canada's current term of "life plus 50").

Following the expiration of Canada's transition periods, these latter commitments could be expected to have an impact on the cost of IP-protected goods and services in Canada. For instance, on copyright, under a term of "life plus 70," a copyright-protected work that has been on the market for 50 years after an author's death would not enter

the “public domain” for an additional 20 years. This means that users would continue to need to seek authorization from, or make payment to, the copyright owner in order to use the work during the additional period. With respect to PTA, the market exclusivity on patented technologies or products could be extended in the event of an unreasonable patent office delay, which can be expected to either delay or create barriers to the market entry of competitors. This could thereby delay the availability of less expensive versions of these technologies or products for consumers.

In view of Canada’s transition periods, and given that these commitments will take effect after CUSMA’s entry into force and will be applied at the end of the period of IP protection, it is difficult to establish a quantitative assessment of their potential economic impacts for Canada. For instance, with respect to the term of protection for copyrighted works of authorship, any future costs arising from Canada’s commitment in this area would depend on the relative cost of works that would otherwise fall into the public domain in a given year, which could vary year to year. Any change to any of these variables would have an impact on the estimated cost implications for Canada. In respect of PTA, the potential cost of a longer patent term due to unreasonable delays in the issuance of a patent will depend on a range of factors, including the nature of a given patent and the framework established upon implementation of Canada’s PTA commitment.

Government procurement

Given that there is no government procurement outcome under the Agreement that applies to Canada, Canada and the United States will retain access to each other’s procurement markets through their obligations under the GPA. Importantly, the GPA includes higher procurement thresholds and updated procedural rules that reflect more current procurement practices, such as conducting some of the procurement process online (e.g. electronic tendering). The GPA also includes expanded market-access commitments between Canada and the United States, in particular with respect to sub-federal procurement opportunities in 37 U.S. states. Government procurement obligations between Mexico and Canada will be maintained under the CPTPP.

Labour and environment

The CUSMA outcome will help ensure that all parties maintain high levels of labour and environmental protection and that domestic laws are not deviated from as a means to attract trade or investment. This outcome will help level the playing field for Canadian businesses and workers, but is difficult to quantify economically.

Facility-specific rapid-response labour mechanism

The establishment of a new bilateral mechanism with Mexico with respect to specific labour obligations on freedom of association and collective bargaining will provide Canada with an enhanced process to ensure the effective implementation of specific

labour obligations in covered facilities. The United States has also established an equivalent mechanism with Mexico. While it is difficult to estimate the potential impacts of this new mechanism, it is expected that it will contribute to the overall implementation of labour reforms in Mexico and help level the playing field within North America.

Dispute settlement

Under CUSMA, and in addition to continued access to the NAFTA chapter 19 mechanism for trade remedies, Canadian stakeholders will benefit from Canada's enhanced ability to enforce the Agreement. In particular, the state-to-state dispute settlement mechanism has been improved to ensure that panels will be established automatically upon request and that a roster of potential panelists is created and maintained.

POTENTIAL ECONOMIC IMPACT OF THE IMPLEMENTATION OF THE CUSMA OUTCOME

The effect of the implementation of the CUSMA outcome would secure GDP gains of $6.8 billion (US$5.1 billion), or 0.249%. This preservation of NAFTA benefits takes into account the new rules of origin for automotive products, incremental access into Canada's supply managed sectors, new provisions for customs administration and trade facilitation, origin procedures, and data localization commitments for financial services.

The majority of the GDP gains would come from household consumption, which would increase by 0.244%, followed by an investment increase of 0.119% (see Table 3). Total Canadian exports would increase by 0.505%, while imports would expand by 0.641%.

Importantly, CUSMA would secure jobs that would otherwise be lost, representing a preservation of employment of 0.160%. Real wages would also appreciate by 0.504%.

While we have not quantified in this study the impact of avoiding the potential imposition of U.S. Section 232 tariffs on autos and auto parts, it is important to note that the importance of implementing the CUSMA outcome increases significantly when compared to the scenario where the U.S. withdraws from NAFTA and maintains or implements Section 232 tariffs on steel, aluminum and automotive products.

Table 3: Macroeconomic Impacts of CUSMA Outcomes Compared to No-NAFTA in 2025

Major macroeconomic indicators	% change
Real GDP	0.249
Terms of trade	0.211
GDP by expenditure category (weighted)	
Consumption	0.244
Investment	0.119
Government expenditure	0.029
Total exports of goods & services	0.505
Total imports of goods & services	0.641
Factor markets	
Capital stock	0.247
Real wages	0.504
Jobs	0.160

Source: Simulations by Global Affairs Canada, Office of the Chief Economist.

Sectoral effects for Canada–United States trade

The sectoral impacts reported in Table 4 represent Canada's trade with the United States that would otherwise be lost without the Agreement, plus the new commitments in

CUSMA, such as automotive rules of origin and new market access for dairy and sugar products.

Table 4: Sectoral Impacts of CUSMA Outcomes for Canada-U.S. Trade Compared to No-NAFTA, US$ million, 2025

Sector	Canadian Exports to United States		Canadian Imports from United States	
	Value	%	Value	%
Cereals	73.0	3.9	3.2	0.5
Vegetables, fruit, nuts	134.5	8.6	58.6	1.3
Crops	467.3	29.1	48.7	5.9
Bovine cattle, sheep and goats, horses	36.3	1.8	-2.0	-2.6
Animal products	6.9	0.7	5.5	0.9
Forestry	0.6	0.7	1.6	0.4
Fishing	6.0	0.5	3.2	0.5
Coal	-0.1	-0.1	1.5	0.3
Oil & gas	-38.2	0.0	53.2	0.9
Minerals	-30.8	-1.7	91.3	3.5
Bovine meat products	109.1	9.6	625.9	69.4
Meat products	155.9	9.5	112.5	5.3
Vegetable oils and fats	567.8	17.6	164.1	16.4
Dairy products	60.4	48.1	347.5	100.2
Sugar & other food products	446.4	4.2	1,429.6	13.0
Beverages & tobacco	33.7	3.8	246.0	12.4
Textiles	416.6	37.1	569.5	26.5
Wearing apparel	357.4	62.0	325.3	46.6
Leather products	69.8	70.1	91.6	31.3
Wood products	152.5	1.7	198.6	10.2
Paper products, publishing	-66.7	-0.6	46.0	0.5
Petroleum, coal products	-4.3	0.0	186.5	1.2
Chemical, rubber, plastic products	4,074.7	12.1	3,713.0	8.8
Mineral products	106.6	5.9	248.4	6.5
Ferrous metals	1,918.6	25.6	514.4	6.2
Metals	2,491.3	13.6	356.5	5.4
Metal products	457.9	10.1	1,077.3	13.5
Motor vehicles & parts	4,066.6	6.2	6,585.3	10.5
Transport equipment	9.1	0.1	712.6	7.2
Electronic equipment	-52.8	-1.1	200.4	1.6
Machinery & equipment	1,040.0	6.1	1,413.5	3.7

Sector	Canadian Exports to United States		Canadian Imports from United States	
	Value	%	Value	%
Other manufactures	62.0	1.7	707.8	10.4
Services	-271.8	-1.1	234.2	0.7
Total	**16,856.6**	**5.0**	**20,371.1**	**6.8**

Source: Simulations by Global Affairs Canada, Office of the Chief Economist

The figures reported in Table 4 suggest that CUSMA would help preserve US$16.9 billion of Canada's exports to the United States, or 5% relative to the reference point of No-NAFTA, while securing US$20.4 billion of imports from the United States, or 6.8%.

For the automotive sector, U.S. tariffs on Canadian automotive products under NAFTA are zero. In the event of a U.S. withdrawal from NAFTA, however, Canadian automotive products would face an average trade-weighted U.S. MFN tariff of 2.7%. In this case, Canada's automotive exports to the United States would decrease by US$5.6 billion, or 8.4%. Similarly, imports of U.S. automotive products to Canada would drop by US$7.7 billion, or 12.3%. The rest of the world would increase their exports to North American markets by US$1.3 billion as they would not be affected by tariff changes and would gain a competitive advantage against North American automotive producers. The loss of NAFTA benefits and increased imports from the rest of the world would cause Canadian automobile production to decrease by 5.5%. Under CUSMA, however, these losses would largely be avoided.

The new automotive rules of origin under CUSMA would likely increase auto-part production in North America but could also lead to higher production costs. At the same time, non-North American automotive producers would not need to undertake any adjustments to their production methods. As a result, the economic model projects that Canada's exports of motor vehicles to the United States would decline by US$1.5 billion relative to the current trade regime under NAFTA, and imports from the United States would decrease by US$1.2 billion. At the same time, automotive imports from non-North American countries could increase, resulting in a decline of the Canadian automobile production of 1.7%.

The effect of preserving NAFTA benefits and the tightening of automotive rules of origin would safeguard Canadian automobile production of 3.8% relative to the no-NAFTA reference point. The effect on Canadian automotive exports to the United States would be US$4.1 billion and on Canadian automotive imports from the United States would be US$6.6 billion.

For agricultural products, it is assumed that Canada's new tariff rate quota access to the United States in refined sugar and sugar-containing products would be fully utilized. As a

result, Canadian exports of sugar and sugar-containing products to the United States would increase by US$20 million. It is also estimated that, while CUSMA secures access to the Canadian chicken and egg market specifically for the United States, and could increase global access to the Canadian turkey market, overall there will be a limited impact on the Canadian sector with regards to the imported volume of poultry and eggs into Canada arising from the implementation of CUSMA.

It is assumed that the new U.S. quota access to the Canadian dairy market would be fully utilized. As a result, it is estimated that Canadian dairy imports from the United States would increase by nearly US$300 million. The effect on Canadian dairy imports from the United States would be US$347.5 million, reflecting the combination of both the new quota access for the United States and the preservation of existing trade under NAFTA that could be lost in the event of no-NAFTA.

The effect on Canadian dairy exports to the United States would be US$60.4 million, reflecting entirely the preservation of existing trade under NAFTA. Under CUSMA, it is estimated that there would be no significant change in trade patterns with respect to Canadian dairy products exported to the United States. While CUSMA provides Canada with new market access into the United States for certain dairy products, export gains from this access are expected to be limited primarily due to lower returns in the U.S. market and non-tariff measures that continue to limit Canadian exports into the U.S. market for dairy products.

Sectoral effects for Canada-Mexico trade

In the event of a U.S. withdrawal from NAFTA, bilateral trade between Canada and Mexico would continue to be governed by NAFTA rules. Existing economic ties between Canada and the United States, and Mexico and the United States would be loosened. This, in turn, would generate alternative opportunities for the expansion of Canada-Mexico trade. As a result, Canada-Mexico trade is expected to expand significantly to replace the losses of Canada-U.S. and Mexico-U.S. trade.

CUSMA would preserve Canada's and Mexico's trade with the United States. As a result, the theoretical projection of the expansion of bilateral trade between Canada and Mexico under a U.S. withdrawal from NAFTA would not take place. It is in this context that the modelling results in Table 5 project a decline in Canada's exports to Mexico of US$1.5 billion, as well as a decline in imports from Mexico of US$4.0 billion.

Table 5: Sectoral Impacts of CUSMA Outcomes for Canada-Mexico Trade Compared to No-NAFTA, $US million, 2025

Sector	Canada's Exports to Mexico		Canada's Imports from Mexico	
	$	%	$	%
Cereals	-27.8	-6.3	0.0	-1.3
Vegetables, fruit, nuts	-30.2	-63.2	-59.5	-5.2
Crops	-86.4	-10.2	-3.6	-7.9
Bovine cattle, sheep and goats, horses	-0.4	-8.2	0.0	-4.0
Animal products	-0.1	-1.4	0.0	0.0
Forestry	0.0	-8.3	0.0	-9.7
Fishing	0.0	1.0	-0.4	-4.2
Coal	1.0	3.6	0.0	-7.6
Oil & gas	0.1	0.9	-7.4	-0.9
Minerals	0.5	0.7	4.0	1.4
Bovine meat products	-205.8	-105.5	-2.8	-37.3
Meat products	-635.2	-191.3	-0.2	-9.1
Vegetable oils and fats	-7.7	-10.8	-0.3	-2.3
Dairy products	0.5	3.6	-0.9	-37.2
Sugar & other food products	-32.0	-12.7	-54.1	-13.7
Beverages & tobacco	-0.5	-0.8	-7.2	-4.6
Textiles	-23.5	-15.4	-17.4	-17.1
Wearing apparel	-0.1	-1.8	-50.1	-15.6
Leather products	-0.2	-8.5	-1.0	-2.2
Wood products	-0.3	-0.4	-4.2	-14.6
Paper products, publishing	-9.9	-2.9	-6.5	-4.2
Petroleum, coal products	0.2	1.8	-2.5	-0.9
Chemical, rubber, plastic products	-76.9	-3.9	-110.1	-11.2
Mineral products	0.3	0.8	-16.5	-9.0
Ferrous metals	-44.8	-5.7	-27.5	-7.0
Metals	-45.5	-12.4	0.7	0.2
Metal products	-42.1	-5.2	-46.5	-12.4
Motor vehicles & parts	-217.8	-8.3	-2,481.6	-21.0
Transport equipment	5.9	3.0	-84.1	-15.1
Electronic equipment	-14.7	-2.0	-326.9	-5.2
Machinery & equipment	-25.4	-2.3	-508.3	-8.6
Other manufactures	-16.3	-5.6	-159.2	-10.5
Services	4.7	3.0	-3.9	-4.1

Sector	Canada's Exports to Mexico		Canada's Imports from Mexico	
	$	%	$	%
Total	**-1,530.1**	**-12.7**	**-3,978.1**	**-12.3**

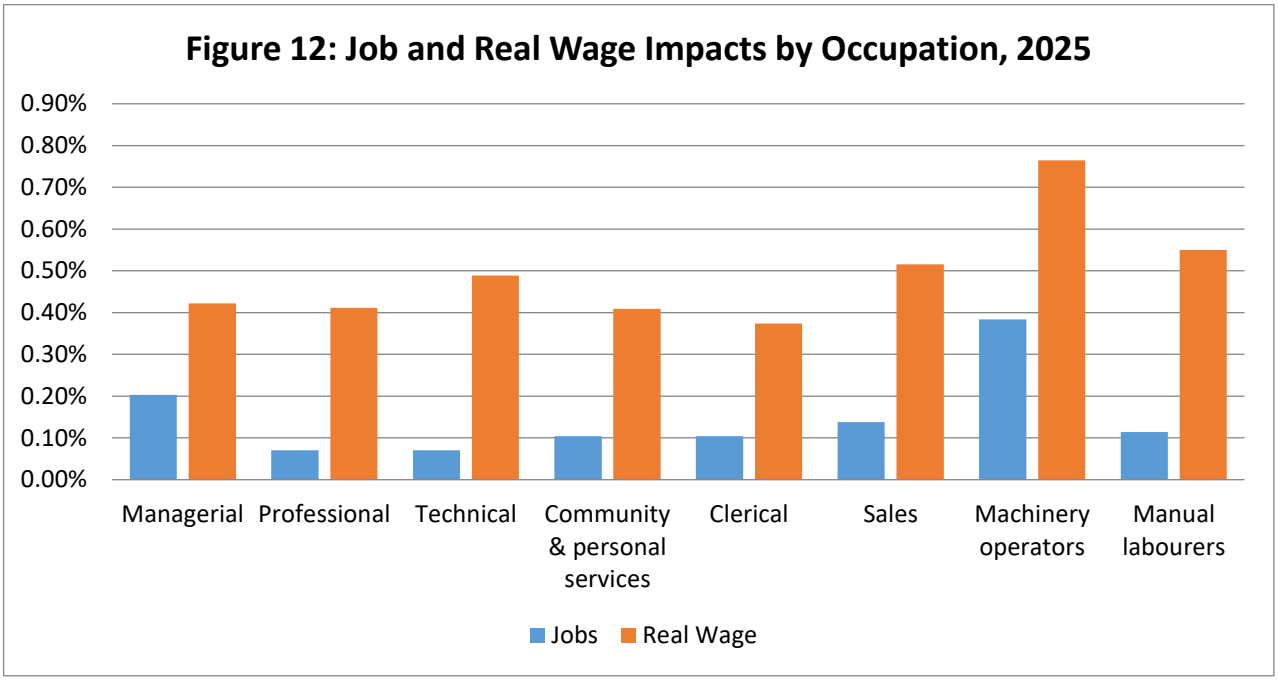
Source: Simulations by Global Affairs Canada, Office of the Chief Economist

Impact of CUSMA on the labour market

Overall, the impact of CUSMA on the Canadian labour market is expected to be positive.

CUSMA compared to a no-NAFTA reference point would secure GDP gains (0.249%), preserve jobs (0.160%) and result in real wage gains (0.504%), which in turn would lead to higher levels of consumption (0.244%). These gains would be lost if CUSMA was not implemented. The wage gains of 0.504% are particularly important as it indicates that trade liberalization achieves higher income for workers, farmers and businesses.

CUSMA would serve to protect jobs and secure well-balanced real wage gains across occupations (see Figure 12). Machinery operators, manual labourers and sales workers would experience the strongest real wage gains under CUSMA, as these occupations would be most affected in the event of a U.S. withdrawal from NAFTA. The real wage gains for machinery operators, manual labourers and sales workers could potentially improve income inequality in Canada, as these gains would outpace those in generally higher-paid managerial, professional and technical occupations. Overall, this represents a positive development for middle-class jobs and an improvement in income inequality across Canada, and supports a broader sharing of the benefits and opportunities of the Agreement across Canadian society.



Source: Simulations by Global Affairs Canada, Office of the Chief Economist

A total of nearly 38,000 jobs would be protected and secured under CUSMA, with most of them in the industrial sectors.

Impact on gender

With respect to gender balance, the occupations that would be most affected by no-NAFTA, and therefore projected to preserve the most jobs under CUSMA, would be concentrated in sectors employing more men than women, such as the motor vehicles and parts sector (e.g. machinery operators). At the same time, the income gains protected by CUSMA could be spent on consumption, retail purchases and other services, where more jobs are traditionally held by women. These jobs would be lost in an event of no-NAFTA, but they would be protected by CUSMA. Overall, the Agreement would secure 18,708 jobs for men and 18,853 jobs for women. This would have the effect of promoting more balanced employment configurations (see Table 6).

Table 6: Potential Job Impacts by Profession and Gender

Occupation/Gender	Male	Female	Total
Managerial	2,902	2,798	5,699
Professional	-72	2,810	2,739
Technical	274	1,233	1,507
Community & personal services	302	816	1,118
Clerical	29	2,564	2,593
Sales	2,455	6,303	8,758
Machinery operators	12,021	1,967	13,988
Manual labourers	797	362	1,159
Total	18,708	18,853	37,561

Source: Simulations by Global Affairs Canada, Office of the Chief Economist

Impact on youth

There would be about 6,000 more secure employment opportunities among younger age groups under CUSMA compared to the outcome of no-NAFTA. Implicitly, young people are making a choice between work and school. With the opportunities in the job market protected, more youth would have the opportunity to pursue either employment or education.

ANNEX 1: LABOUR MARKET MODULE

The CGE model with the labour market module improves the existing modelling framework and addresses some existing concerns. In particular, it introduces greater differentiation of labour occupations and adds the age and gender profiles of the labour force. This allows us to capture the movement of workers within sectors across occupations, and into and out of the labour force in response to changing incentives for leisure versus labour. As such, it improves the ability of public policy to anticipate and to respond to the pressures on labour markets resulting from trade liberalization.

Base data development

Labour market data used in the labour market module is sourced from Statistics Canada's Survey of Labour and Income Dynamics, Annual Demographic Estimates, and the Census.

Table 7 describes data points used in the labour module. There are 10 possible categories: eight occupation categories, one unemployment category, and one category for people not in the labour force. The population is assigned at the start of a given year to one of these 10 categories. New entrants are distributed across the eight possible professional categories or into unemployment.

Table 7: Labour Market Categories for the Labour Market Module

Indicator	Categories
Labour market status	1. Managerial 2. Professional 3. Technical 4. Community and personal services 5. Clerical 6. Sales 7. Machinery operators and drivers 8. Manual labourers 9. Unemployed 10. Not in the labour force
Gender	Male and female
Age	1. 15-24 2. 25-34 3. 35-44 4. 45-54 5. 55-64 6. 65+

The working age population as defined by Statistics Canada includes all individuals who are 15 years and older, and reside in Canada. Table 8 shows the distribution of the Canadian working age population across occupations by gender.

Table 8: Distribution of Canadian Working Age Population by Occupation and Gender, 2015

Occupation/Gender	Male	Female	Total
Managerial	1,331,106	916,383	2,247,489
Professional	1,259,547	1,749,759	3,009,306
Technical	761,992	875,889	1,637,881
Community and personal services	249,564	588,405	837,968
Clerical	353,717	1,566,868	1,920,584
Sales	2,052,953	2,579,401	4,632,353
Machinery operators & drivers	2,516,037	284,104	2,800,141
Manual labourers	592,686	189,302	781,987
Unemployed	757,113	570,049	1,327,162
New entrants	286,821	282,887	569,708
Not in the labour force	4,115,391	5,596,395	9,711,785
Total	14,521,663	14,954,703	29,476,366

Source: Statistics Canada, 2016 Canadian Census

Labour market adjustment to a policy shock

A policy shock affects the existing profile of employment by changing the demand and supply for labour by occupation.

When trade is liberalized, a trade policy shock would result in a demand for additional labour, raising the after-tax wage rate for labour and creating an incentive for labour participation. Labour market participation by age and gender is determined by the trade-off that workers face between labour and leisure: higher wages tend to increase labour force participation. New entrants are determined exogenously based on the population's demographic profile.

The allocation of labour supply across occupations takes into account worker preferences. Each category of worker supplies labour to occupations that are compatible with that category's gender, age and occupational characteristics, yet responds to differential wages and labour demand across occupations. Thus, workers in a given category would switch their offer towards another activity if the wage rate for that other activity rises relative to the average of the wage rates across all activities.

The modelling framework assumes that there is always competition for jobs—that is, the number of people who plan to participate in employment activity is greater than or equal to the number of job vacancies. Since there is the possibility of transitioning into unemployment or exiting from the labour force, the modelling framework allows for the markets to include unemployment. Consequently, the model specifies which offers of

employment are accepted and what activities are undertaken by those whose offers for employment are not accepted.

ANNEX 2: FINANCIAL SERVICES MODELLING

Barriers to trade and investment in services often take the form of regulatory measures that do not necessarily generate direct revenues like tariffs, but do require the use of real resources to meet regulatory requirements. Many of these regulatory requirements are necessary for safety and public benefits, but the complexity of these regulations could increase the costs of trade and investment. Trade agreements attempt to address these issues, not necessarily by removing or reducing these barriers, but rather by imposing binding commitments to increase transparency and predictability of regulatory rules with a view to creating an environment conducive to trade and investment growth. In some cases, however, actual changes to regulatory rules are required to implement services and investment commitments.

The difficulty of quantifying services and investment commitments is that impediments to trade and investment in services are not directly observable. The recently developed OECD Services Trade Restrictiveness Index (STRI) offers a promising approach. The OECD STRI provides comprehensive and comparable information on services restrictions for 44 countries across 22 major services sectors. The STRI measures existing domestic regulatory regimes for services and investment, and thus it uses qualitative information (laws and regulations) to estimate indices that range from “0” to “1,” where 0 represents a fully open regime and 1 represents a completely closed regime in a services sector. The STRI includes five policy areas:

1) restrictions on foreign entry
2) restrictions to movement of people
3) other discriminatory measures
4) barriers to competition
5) regulatory transparency

Area 1 applies to commercial presence (mode 3 under the GATS), and areas 2 to 5 apply to cross-border trade in services (modes 1, 2 and 4 under the GATS).

For financial services under CUSMA, the parties agreed to revise a government’s ability to impose local data storage requirements on branches and subsidiaries of foreign financial institutions, subject to a safeguard ensuring that financial regulators have ongoing and unrestricted access to the financial information they need in order to fulfil properly their mandates.

Currently, all federally regulated financial institutions are required to maintain copies of certain financial and corporate records at a location in Canada. To comply with the data storage commitments, legislative amendments are required to create an exception to this requirement for branches and subsidiaries of foreign financial institutions domiciled in the United States or Mexico. Under federal financial statutes, Canadian banks and insurers would continue to be subject to requirements to maintain copies of their records in

Canada. These financial institutions, including foreign financial institutions, would be able to continue transferring financial information abroad for processing.

The required legislative changes are included in the modelling approach for investment, but not cross-border trade in services given that current requirements only apply on a GATS Mode 3 basis. Following the STRI methodology, we estimated Canada's STRI banking and insurance scores to account for the changes under CUSMA. Because of the new legislative amendments, Canada's STRI score for future investment in insurance services drops from 0.2084 before CUSMA to 0.2018 after CUSMA, representing an improvement in the investment environment in Canada in the area of insurance services. Similarly, the STRI score for investment in banking services improves from 0.1783 to 0.1663. This is incorporated into the economic model to account for the effect of the legislative amendments on the Canadian economy.

The change in STRI scores is interpreted as a reduction in a phantom tax in the dynamic GTAP model—a tax that has the effect of changing business behaviour but does not result in the collection of revenues. The reduction of the phantom tax is expected to give rise to an increase in foreign capital formation in Canada. The final capital formation in the sector after policy change would be driven by two factors: change in the rate of return from capital investment resulting from policy change under CUSMA and a change in the composition of capital between foreign-owned and domestic-owned capital.

The United States and Mexico must also provide reciprocal treatment for Canadian financial institutions operating in those markets. However, the data storage commitment does not require a change in either of those countries' financial sector legislative frameworks, which is reflected in the modelling approach.

ANNEX 3: CUSTOMS ADMINISTRATION, TRADE FACILITATION AND ORIGIN PROCEDURES MODELLING

The Trade Facilitation Index (TFI) was developed by OECD to benchmark the condition of the existing border procedures used by 160 economies across the globe. It is updated every two years and is intended to show each economy which area of the border procedure may require improvement. The Index is formed by summing up eleven TFI indicators/subcomponents[19] that cover different areas of border procedures. Each question addresses specific measures used in each area of border procedure and their answers are coded in scores of 0, 1 and 2. A value of 2 represents the best performance level that can be achieved.

In order to calculate the possible improvement in trade facilitation under CUSMA, each commitment on origin procedures and customs and trade facilitation is mapped to the questions in the questionnaire. If there is an improvement as a result of CUSMA, the answer will be adjusted to a higher level. For example, the current answer to question C36 (concerning the maximum time by which the advance ruling will be issued) for Canada is coded 0. Under CUSMA, the time needed for the issuance of an advanced ruling would be reduced and therefore the answer is adjusted to a code of 1. However, if the current performance is already at the best level, no adjustment is applied. By taking into account all new commitments in the areas of custom administration and trade facilitation, and origin procedures, a set of new TFI scores is generated for each country that could be compared to existing rules and procedures. The differences between the new and existing TFI scores quantify the net improvement and are used in the model to assess the impact of improvement on trade and economy in general.

[19] The eleven indicators cover areas of information availability, involvement of trade community, advance rulings, appeal procedures, fees and charges, formalities-documents, formalities-automation, formalities-procedures, internal border agency cooperation, external border agency cooperation, and governance and impartiality.