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NAFTA
Here Today, Gone Tomorrow?

Will NAFTA end? This article examines issues that may be expected to arise in the event that the United States wishes to withdraw from NAFTA. These issues include legislative requirements in the United States, the potential resurrection of the Canada-United States Free Trade Agreement ("CUSTA"), and what may arise in the absence of any free trade arrangement.

In the most recent negotiating round for *NAFTA* 2.0, the United States finally enunciated its negotiating position with respect to particularly contentious issues, including dispute settlement proceedings, American automotive content under *NAFTA* and supply management. The negotiating position of the United States is being described as excessive and politically impossible for Canada and Mexico.

Press reports have been suggesting that the American position is simply a means of making renegotiations unpalatable, reflecting President Trump's intention to terminate *NAFTA*. It is certainly premature to write off *NAFTA*. One always expects negotiations to get more difficult as they move toward completion. Given the economic interests at stake in all three countries, the authors maintain hope that the talks will continue and ultimately succeed.

Can President Trump Tear Up NAFTA?

Even if it was the wish of the American administration to end *NAFTA*, it may prove to be a very difficult beast to kill.

As an opening proposition, no one country can tear up *NAFTA*. The United States can certainly withdraw from *NAFTA*, but the agreement would continue in force between Canada and Mexico unless either of those parties also chooses to withdraw.

Withdrawal from *NAFTA* requires six months notice before the rights and obligations under the agreement can be terminated. There is an interesting debate amongst US constitutional law scholars regarding President Trump's power to deliver such a notice without congressional approval and the legal consequences of such unilateral action. The *North American Free Trade Agreement Implementation Act* of the United States is 169 pages long and involves many amendments to American legislation including customs provisions, trade remedies, agriculture, and extensive amendments to a wide range of related statutes. Under American constitutional law, *NAFTA* only came into force when the legislation was approved by both houses of Congress and the President. To undo these extensive legislative changes in the United States would therefore require further legislation passed by Congress. Some have argued that even the delivery of a notice of withdrawal by President Trump without Congressional approval would be unconstitutional.

It has been reported that two thirds of American states have Canada as their major export market. This means that there may be a vested interested on the part of up to 66 Senators to protect jobs in their states by declining to implement the statutory measures required to remove *NAFTA* obligations from American legislation. Similarly, American southern states also have a significant interest in maintaining export markets in Mexico. Therefore, the prospect of sweeping legislative change may be challenging.

Nonetheless, there may be certain areas where changes to *NAFTA* rules *can* be made unilaterally by Presidential fiat.

First, as a matter of international law, a Presidential notice of withdrawal from NAFTA is likely to be deemed effective in putting an end to the international obligations of the United States even if there is a dispute about the constitutional validity of such action

under US law. Absent an obvious lack of authority, an international tribunal is unlikely to hold the United States to any legal obligations following delivery of required notice in accordance with NAFTA's express withdrawal provisions. If this notice occurs, certain provisions of NAFTA that were not implemented by US legislation, such as its investor-state dispute settlement provisions, will no longer be binding on the United States.

Second, the complex patchwork of US trade remedies legislation authorizes the executive branch to take certain unilateral actions against imports. The withdrawal of the US from NAFTA would lead to the loss of any international law constraints on such trade remedies enforceable through NAFTA (as opposed to other treaties, such as the WTO Agreements). Thus, Canada and Mexico may lose the ability to challenge certain US administrative actions before bi-national panels under NAFTA Chapter 19 or by state-to-state arbitration under NAFTA Chapter 20.

Potential Resurrection of the Canada-US Free Trade Agreement

The termination of *NAFTA* may not mean the termination of free trade arrangements between Canada and the United States. The *Canada-U.S. Free Trade Agreement* ("*CUSTA*"), concluded in 1989, was suspended as long as *NAFTA* applied to both Canada and the United States. An exchange of diplomatic letters in January 1993 indicated the intention of both parties that the suspension would "remain in effect for such time as the two Governments are Parties to the NAFTA". Termination of *NAFTA* could arguably mean that the provisions of *CUSTA* would go back into force, including tariff removal and the continuation of the automotive provisions that reflected a free trade arrangement with the United States that has been in existence since the 1965 Auto Pact. However, CUSTA did not include the investor-state dispute settlement provisions found in NAFTA. In addition, the equivalent to NAFTA Chapter 19 constraints on US trade remedy measures under CUSTA have now expired.

There are pundits in the United States who claim that the reversal of the suspension of CUSTA is not automatic, but would require legislative action to bring that agreement back into force. This view may be contrary to section 107 of the American NAFTA Implementation Act which makes clear that "[a]n agreement by the United States and Canada to suspend operation of [CUSTA] shall not be deemed to cause [CUSTA] to cease to be in force". One might reasonably argue that this provision automatically brings CUSTA back into operation without the need for further legislative action.

CUSTA has a termination provision similar to *NAFTA* in that it can also be ended upon six months notice; but arguably notice cannot be given until *NAFTA* has actually been terminated, since CUSTA is suspended until that time. Even then, the need for extensive legislative changes in the United States may further complicate any administration attempt to quickly terminate that agreement.

What Happens if there is no Trade Agreement between Canada and the United States?

1. General Impact

Even if these free trade arrangements were terminated between Canada and the United States, it is difficult to see how the United States might benefit since its most favoured nation (MFN) tariffs are generally very low.

It has been reported that average US MFN duty rates are in the range of 2.5%. For Canada the average duty rate is 3.5%. While customs duties are always an impediment to trade, these generally low rates will minimize the impact of the end of free trade agreements. Exporters to the US should confirm what the MFN duty rates will be on products they may wish to ship to the American market.

2. The Automotive Sector

The American MFN import duty rate on automobiles is currently 2.5% (though it does go up to 25% on pick-up trucks and

commercial vans). An additional complication for the American automotive industry is that 75% of all U.S. parts exports are to Canada or Mexico (as reported by the U.S. International Trade Administration in 2016). A further issue is the degree of rationalization in the North American automotive industry (and in particular between Canada and the United States). With parts routinely crossing the border six or seven times for further processing, existing supply chains would be severely disrupted in the event that the U.S. intended to impose local content requirements. The significance of these concerns is perhaps best expressed by American automotive producers who are opposed to the very proposals intended to benefit them.

3. Services

Loss of a free trade agreement would also inhibit the orderly movement of business travellers between *NAFTA* partners. Once again, this would likely act to the detriment of the United States as it currently maintains a substantial trade surplus in services with both Canada and Mexico. Without the protections available to American businesses under *NAFTA*, service exports could be severely impacted.

4. Dispute Settlement

Trade between existing NAFTA partners would continue to be subject to international trade discipline under the auspices of the World Trade Organization ("WTO") even in the absence of any free trade arrangements. The WTO includes a number of trade facilitation agreements, as well as a binding dispute resolution process to deal with protectionist policies imposed by Member states. These rights arose after NAFTA came into force. Canada has been successful in a number of WTO cases against the US where NAFTA was ineffective in resolving disputes.

Conclusion

NAFTA negotiations have reached a critical juncture with the more controversial American proposals now on the table. With over $1 trillion in three-way trade in goods and services, we believe it in

the interests of all three countries to continue to push forward and make whatever progress is possible. To the extent that there are threats, or reports of unilateral termination of *NAFTA*, these are unlikely to occur in the near future due to the limitations discussed above. In these circumstances, it is clearly a better road to seek accommodation with *NAFTA* partners, rather than to risk damage to the largest integrated market in the world today.

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a cautionary note