

Intelligence MEMOS



From: Jon Johnson

To: Superintendent Jeremy Rudin

Date: January 20, 2017

Re: **BACK TO THE DRAWING BOARD ON NAFTA'S RULES OF ORIGIN**

The Trump administration intends to put all aspects of the NAFTA on the (re)negotiation table. Recent reports indicate that it may put a particular focus on NAFTA rules of origins (ROOs).

ROOs are used for determining whether a good imported from one NAFTA country into another is eligible for duty free treatment. The rules generally require that materials from non-NAFTA countries be sufficiently transformed or have sufficient value added to them within Canada, the US, and/or Mexico, so that the resulting good can be considered as “originating” within NAFTA and therefore eligible for crossing borders between NAFTA countries without paying tariffs. These rules do not make distinctions of nationality between the three NAFTA countries. Therefore a qualifying part produced in Mexico or Canada or the US is simply considered as “originating,” as opposed to “Mexican,” “Canadian,” or “American”. ROOs are also good-specific and vary considerably from good to good.

Given Mr. Trump’s rhetoric respecting the auto sector, US demands in a renegotiation will most likely include requests for changes to automotive ROOs. Under NAFTA, ROOs for cars are exceedingly complex because, unlike other rules, they are based on a concept of tracing parts imported from non-NAFTA countries right back to the point of first importation. The rules for trucks are also based on a form of tracing. These rules are difficult to administer, both for automotive producers who must comply with them, and for customs officials who must administer them. The NAFTA automotive rules would be greatly improved through adopting a simpler system. Those agreed as part of the TPP were much simpler than NAFTA’s. US negotiators may start with the TPP rules as a template for assessing origin, notwithstanding Mr. Trump’s antagonism towards that agreement.

Regardless of the template for assessing origin, US demands will likely be for rules that result in an increase in American content. Therefore, increased content thresholds for vehicles (currently 62.5% North American content for cars and 60% for trucks) could be up for discussion. US negotiators may also request certain specific levels of US content in vehicles produced in NAFTA countries.

US negotiators will doubtless demand changes to other rules, and your departments should immediately begin opening lines of communication with all industries now to assess Canada’s position. During the NAFTA negotiations, the Canadian negotiators developed excellent relationships with representatives of industries affected by the ROOs. It is very important that similar relationships be developed with the negotiators in the forthcoming renegotiation. Negotiators cannot be expected to know the specific problems that may result from the adoption of a particular rule change unless industry players educate them. Negotiators must maintain open lines of communication with industry players so that they fully understand the ramifications of a particular demand and can develop convincing arguments for resisting it or at least modifying the demand to limit the damage that agreeing to it might cause.

Doing so will be particularly important since, unlike the NAFTA negotiations of a generation ago, where there was considerable good will on all sides, the Trump team’s approach appears to be much more adversarial.

Jon Johnson was a former advisor to the Canadian Government during NAFTA negotiations.