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# Indirect Tax Alert

News from EY Americas Tax

## Canada again begins Canada-US-Mexico Agreement (CUSMA) ratification

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On 29 January 2020, the Canadian Government tabled Bill C-4, *Canada-United States-Mexico Agreement Implementation Act*. The bill must now pass the required readings in both the House of Commons and the Senate and then receive Royal Assent.

### Background

Implementing legislation for the Canada-United States-Mexico Agreement (CUSMA) was first introduced during the previous Parliament as Bill C-100. However, the bill failed to pass through all the required reading stages before dissolution of Parliament prior to the October 2019 general federal election and therefore did not become law. With the resumption of parliamentary business after the Holiday adjournment, the minority Liberal government has made it a priority to restart and swiftly conclude the ratification process of CUSMA.

### Revised outcomes

The current version of CUSMA includes changes agreed to by the parties on 10 December 2019. Specifically, provisions relating to chapters covering state-to-state dispute settlement, labor, the environment, intellectual property, and rules of origin have been updated:

- ▶ **State-to-state dispute settlement:** The Free Trade Commission of Ministers will no longer be involved in the dispute settlement process; instead a panel will be automatically established upon request. Changes have also been made to ensure that a roster of potential panellists is created and to provide for additional clarity and transparency in the rules of procedure that provide guidance on the operation of panel hearings.
- ▶ **Facility-specific, rapid-response labor mechanism:** Canada has established a new bilateral mechanism with Mexico under the dispute settlement chapter regarding specific labor obligations on freedom of association and collective bargaining. This facility-specific, rapid-response mechanism will provide Canada with an enhanced process to ensure the effective implementation of specific labor obligations in covered facilities. The US has established an equivalent mechanism with Mexico.
- ▶ **Labor:** Parties have increased flexibility to pursue violations of CUSMA under the dispute settlement mechanism. The previous requirement that violations that relate to violence against workers must be committed through a sustained and recurring course of action or inaction in order to qualify as a violation has been removed. Failure to comply with an obligation in the chapter is now presumed to be “in a manner affecting trade or investment between the parties,” unless the defending party can demonstrate otherwise.
- ▶ **Environment:** Akin to the labor chapter, the burden of proof has been reversed in that failure to comply with an obligation in the environment chapter is now presumed to be “in a manner affecting trade or investment between the parties,” unless the defending party can demonstrate otherwise. A new article has been added to recognize the three parties’ existing commitments to implement certain multilateral environmental agreements to which they are a party.
- ▶ **Intellectual property:** The parties have agreed to remove the prior obligation on data protection for biologics. Canada will no longer need to amend its domestic regime to provide 10 years of data protection in this area. Additionally, the parties have agreed to:
  - Remove a provision on the availability of patents for new uses, new methods or new processes of using a known product, as well as a provision on data protection for “new indications” of existing drugs; and
  - Include additional language on an exception related to regulatory reviews, and new language on how parties may meet obligations dealing with patent-term restoration, patent linkage and data protection for small molecule drugs.
- ▶ **Rules of origin:** CUSMA rules of origin for automotive goods require that 70% of the steel purchased by vehicle assemblers qualify as originating in the CUSMA region. This requirement was updated to specify that, for purposes of meeting the 70% requirement, all steel manufacturing processes must be performed in one or more of the parties to CUSMA (i.e., Canada, the United States, Mexico) except for metallurgical processes involving the refinement of steel additives. This provision will come into effect seven years after CUSMA enters into force. The rules of origin for aluminum will also be reviewed 10 years after that time.

## Side letters

Alongside CUSMA, Canada and the US negotiated side letters on US Section 232 tariffs on autos and auto parts, future Section 232 measures, energy, wine, natural water resources, and research and development expenditures.

Given the increasing propensity of the US Administration to employ Section 232 tariff measures, the side letters on autos and auto parts and future Section 232 measures are a significant outcome for relevant Canadian industries. In the event the US applies Section 232 measures against imports of automobiles, Canada has secured a guaranteed annual exemption for 2.6 million Canadian-origin automobiles. Canadian light trucks are fully exempt from US Section 232 measures, and the US has also committed to provide a minimum 60-day exemption from any future Section 232 measures. This exemption will provide time for Canada and the US to agree on appropriate outcomes based on industry needs and historical trading patterns.

## Ratification process

As Canada is the last of the CUSMA member states to ratify the agreement, the pace of the Canadian ratification process will largely determine when CUSMA will enter into force. Per Section 2 of the *Protocol Replacing the North American Free Trade Agreement with the Agreement between Canada, the United States of America, and the United Mexican States*,

CUSMA enters into force on the first day of the third month following the last notification of ratification. Canada must complete the legislative process for Bill C-4 before notification can be executed under the relevant CUSMA provisions.

The current Liberal government has indicated that it will aim to ratify CUSMA as quickly as possible (i.e., the bill might receive royal assent before the end of February 2020). However, as the Liberal government is in a minority position,

the support of at least one opposition party will be required to successfully pass the legislation. Although opposition parties have indicated a desire to debate the bill in Parliament, which may delay the ratification process somewhat, there is growing pressure among several industry sectors and public institutions to fast-track ratification of Bill C-4.<sup>1</sup> If the bill is fast-tracked through the legislative process CUSMA could enter into force on 1 May 2020.

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## Endnote

1. *Trudeau, Freeland urge opposition parties to pass bill on new NAFTA swiftly*. CBC News, 27 January 2020. <https://www.cbc.ca/news/politics/freeland-north-american-trade-agreement-cusma-nafta-1.5441459>.

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