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TRADE AND INTERNATIONAL POLICY

## Countdown to the CUSMA Review – Pitfalls, Politics and Horse-trading Ahead

by Lawrence L. Herman

- The Canada-US-Mexico Trade Agreement (CUSMA) terminates on June 30, 2036. That's the definitive end-date, as spelled out in the Agreement. Every Canadian company doing business in or with the US (or Mexico) should have this date firmly in view.
- Before we get there, CUSMA requires a three-party review of its operations starting on June 30, 2026, six years after its entry into force. The purpose is to see if the three parties can agree to extend the agreement for another 16 years.
- However, in preparation, the three sides need to clear up uncertainties about the processes and procedures for the negotiations. Otherwise, things could go badly off the rails. Substantive issues will also be at stake. It is difficult to imagine an extension without major changes or additions to CUSMA satisfactory to all three countries, particularly the US.
- Absent an extension of the agreement, CUSMA will terminate in accordance with its terms. That possibility creates uncertainty overhanging North American trade and the attendant risks for trans-border business.

The review and termination provisions applying to CUSMA resulted from the 2017–2018 NAFTA re-negotiations, when the Trump administration actually wanted the new trade agreement to terminate in five or six years. Canada and Mexico refused, so the result was a bizarre compromise in CUSMA that gives maximum advantage to the US side.

Using this advantage, there are indications that the Americans will be putting things back on the table in the review that weren't settled earlier and that Canada – yet again – will be into horse-trading with the Americans on a range of matters.

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Thanks to the efforts of think tanks, the Canadian Chamber of Commerce, the Business Council of Canada, as well as industry groups like the automotive producers, the private sector is starting to pay closer attention to the implications this has for Canada-US business.<sup>1</sup> There are indications that the American business community has turned its attention to CUSMA (possibly more focused on Mexico). The Canadian business community should take heed.

Elements of uncertainty are compounded by the approaching US presidential election (November 5, 2024), by the fact that a new Mexican president will take office on October 1, 2024, and by the Canadian general election scheduled to occur on or before October 25, 2025. But whether Canada will be dealing with a Biden or Trump presidency in 2026, indications are that Canada and Mexico will be in for tough negotiations with the Americans.

This was expressed in a paper presented at a recent Brookings Institution event, stating, “President Biden is expected to face pressure in the election to take positions against some USMCA issues, including Mexico on labor, energy, and agriculture issues, and possibly Canada on dairy, digital tax, and other issues.” Further, the authors stated that should former president Trump be re-elected:

It seems unlikely that a Trump administration – that pushed so hard for a review clause, and with the leverage the U.S. has as the much larger economy among the three parties – would pass up the opportunity to use the review clause to negotiate better terms. (Meltzer and Verheul 2024.)

Former USTR Robert Lighthizer and Katherine Tai, his successor, have each made it clear that the process will allow the US to use maximum leverage over Canada and Mexico throughout CUSMA’s remaining term. At the Brookings Institution event just mentioned, Tai said the review shouldn’t be perfunctory and that the US, Mexico and Canada shouldn’t get “too comfortable” with their renegotiated tripartite trade pact:

[Y]ou do not want that review to happen in a way that all three parties come to the conversation too comfortable,” she said. “The whole point is to maintain a certain level of discomfort, which may involve a certain level of uncertainty, to keep the parties motivated to do the really hard thing, which is to continue to reevaluate our trade policies and our trade programs to ensure that they’re really responding to the changes that are happening around us. (Tai, cited in *World Trade Online* 2024.)

A well-known American expert has added the following point to Tai’s comment:

On the U.S. side, I think we will see some heavy lobbying by interest groups, and then that lobbying will get mixed in with the ideology of whoever is president at that point. What will come out is some U.S. demands, and no doubt some of these demands will make Canada and Mexico uncomfortable. (Lester 2024.)

## Clarifying the Process

Substantive issues are, of course, the key aspects. But before we get to those, there are procedural elements that require attention. These are set out in Article 34.7 of CUSMA which provides that the review is to be conducted by the Canada-US-Mexico Free Trade Commission (FTC) to determine if the Agreement will be extended for another 16 years. While on its face that seems pretty straightforward, there are aspects in need of clarification.

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1 The House of Commons Standing Committee on International Trade (CIIT) has been holding a series of hearings on the review. Minister Mary Ng, senior Global Affairs Canada officials and others have been testifying on the key issues for Canada, even at this stage. The CIIT has adjourned for the summer but more hearings are planned in the fall of 2024 (<https://www.ourcommons.ca/committees/en/CIIT/StudyActivity?studyActivityId=12563470>).

To begin with, it is not clear whether the possible 16-year extension is to run from CUSMA's formal end date in 2036 or from the time when and if the three governments agree to such extension – which could be at any time before 2036.

Next, the role of the Commission needs some clarification. It is not a stand-alone, independent body. It is comprised of the three governments represented by their trade ministers, as was the case of the equivalent body under NAFTA. The Commission is thus a fiction in some respects. The reality is that Canada, the US and Mexico will be exchanging positions among themselves under cover of the Commission.<sup>2</sup>

These exchanges are to take the form of “recommendations for action” from the three governments, to be sent in at least a month before the Commission starts the review. After getting those recommendations, the Commission deliberates and then decides on “appropriate actions” to be taken by the parties. This again is a fiction in that the Commission is the three governments themselves.

There is nothing in Article 34.7 that specifies what is meant by “appropriate actions.” In practical terms, it means changes, additions, recalibrations of CUSMA to either improve it or settle differences among the three governments. This is the part that seems likely to lead to an opening up of the Agreement and – again being realistic – that can lead to re-negotiation of major parts of the deal.

A further need for clarification is that nothing in Article 34.7 stipulates when the 2026 review is to be completed. What happens if the three governments can't reach agreement on any of the matters before the Commission? Under Article 30.3, the Commission decides “by consensus,” which in effect means unanimity (like at the WTO). Article 30.3 allows the parties to “decide otherwise” than by consensus, but it's impossible to envisage agreement to decide issues by majority vote.

It is highly desirable for the three governments to resolve these uncertainties now to help ensure the process doesn't get bogged down and become paralyzed as it enters these uncharted waters.

## Managing the Process

If, as seems likely, there is no agreement on CUSMA's extension for 16 years when the Commission meets in 2026, Article 34.7 then says that there have to be annual reviews of the Agreement by the Commission until the 2036 termination date. None of the details for these rolling reviews have been spelled out. Anything could happen. We are entering uncharted waters in this area as well.

To help ensure that it doesn't go off the rails, managing all of these processes will be important. Work should start now, while the clock is ticking and while there's time to get some of the procedural elements and guidelines in place to ensure that the process is well-orchestrated. Leaving things to chance in the hope that these will sort themselves out unnecessarily compounds the uncertainty.

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2 In fact, meetings of the FTC are largely set piece affairs, with the agenda and the outcome largely determined by the respective staffs of the Canadian trade minister, the US Trade Representative (USTR) and the Mexican Secretary of Economy. The Commission met last on May 23, 2024, in Phoenix, Arizona and agreed on a number of broad policy objectives. There was only passing reference to the 2026 review: <https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cusma-aceum/2024-05-23-joint-statement-declaration-commune.aspx?lang=eng>

Here are the most glaring elements of Article 34.7 in need of clarification,

- The role of the Commission in the review process needs to be made more precise, eliminating the fiction that it is somehow a stand-alone body that receives “recommendations for action” from governments. As already explained, the Commission is the three governments acting in that capacity and that needs to be made clear.
- It’s important to settle that we’re not talking about “recommendations” to be submitted by governments to themselves but a new set of proposals on a range of CUSMA provisions that are, in effect, the starting point for a round of ongoing negotiations. That, plus the methodology for the negotiations, needs to be spelled out.
- Similarly, the notion that the Commission deliberates on these recommendations and then decides on “appropriate actions” is a fantasy. The reality is that there will be a set of negotiations among the three parties. It means aspects of the negotiating process need to be specified. If, in fact, the “appropriate actions” will entail amendments or additions to CUSMA, this should be stated as well.
- Article 34.7 says nothing about the timeline for the 2026 review. This needs to be agreed upon. As well, under the scenario where there is no extension, the timelines and procedures for 10 years of annual reviews need to be settled. It would be damaging to have them running on indefinitely, as a kind of rolling exercise.

All of these procedural matters should be clarified through a protocol or addendum to CUSMA that sets out the above ingredients.<sup>3</sup> Talks should begin now on how to put this in place.

## Clarifying Substantive Items

Notwithstanding these administrative matters, the overriding element will be the substantive parts of the deal on the table starting in June 2026. The possibility of changes in government in the US and Canada clouds the picture, but whatever the political situation in each of the three parties at that point, the US position in the review will be dominant.

Clarification of US objectives will be provided under section 611 of the *United States-Mexico-Canada Agreement Implementation Act*, the US law that requires the USTR to report to Congress on the operation of CUSMA with areas that need updating by the end of 2025.<sup>4</sup> That report will not be available for another 18 months.

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<sup>3</sup> The rules under the *Vienna Convention on the Law of Treaties* allows parties to clarify and, where needed, to amend the terms of treaties by mutual consent. CUSMA Article 34.3 allows for amendments to be made and enter into force 60 days after ratification. Short of amendment, treaty law also allows parties to conclude a parallel agreement or understanding on how certain treaty terms are to be interpreted or applied.

<sup>4</sup> “The trade representative’s report shall include their assessment of CUSMA’s operation, as well as a recommendation on CUSMA extension. The trade representative is to report on prior efforts to resolve any concerns underlying the recommendation. The report will also set out the views of the 15 advisory committees . . .” Johnson, Jon, “CUSMA Joint Review May Not be a Smooth Ride”: *Intelligence Memo*, C.D. Howe Institute, 30 May 2024.

Without waiting for the USTR report, and without trying to list discrete items, there are actions the three governments could undertake even now in terms of preliminary scoping:

- i) One would be to agree on a defined list of subject areas or parts of CUSMA that can be opened up. This would be a means of keeping the process reasonably contained, maintaining the basic rules of the trading relationship intact.
- ii) At the other end of the spectrum would be an agreement not to foreclose any subject from being opened up, much like the 2017–2018 negotiations themselves. This has the advantage of allowing proposals for improvement, refinement and modernization across the full scope of CUSMA provisions. But it entails obvious disadvantages.

With some effort, it should be possible to categorize the kinds of issues that will be addressed: the first category would list contentious or difficult baskets of disagreement among or between the CUSMA parties; the second would classify parts of the Agreement that are not contentious and, hopefully, where there are shared objectives on modernizing and improving the Agreement.

As to the first basket, we have a pretty good sense of what some of the US demands directed to Canada will be, including the Digital Services Tax, the *Online Streaming Act*, toughening trade restrictions on Chinese imports and, of course, removing restrictions on dairy imports under Canada's supply management system. Even with agreement to somehow fence in the scope of the review, the American list is likely to be a long one.

Canada also has a list of concerns and grievances related to the preferential elements of President Biden's industrial policies in the *Inflation Reduction Act*, automotive rules of origin and a whole slew of American protectionist measures. Mexico will have its own list.

As to a shared modernizing and updating objective, this might cover things such as digital trade, environmental goods and services, decarbonization issues, supply chain facilitation, critical minerals, improved border and customs clearance procedures, human rights and forced labour and even matters of national security.

Going into the review with this kind of "positive" menu wouldn't prejudice tough bargaining, but at least there would be a set of less contentious areas that could bear fruit as post-2026 events unfold. A set of three-party initiatives aimed at modernizing trade rules in individual sectors could form the basis for an updated CUSMA down the road.

## Concluding Thoughts

The areas of uncertainty in the CUSMA review process, combined with the treaty's formal 2036 termination date, make it important for the three governments to resolve these matters before the 2026 review begins. It's vital to ensure that the process unfolds on a well-orchestrated basis and avoids adding uncertainty over the rules governing North American cross-border business.

At the end of the day, whatever emerges from the forthcoming review, a proper, stable treaty framework is needed to govern the three-country trading relationship. This should be the ultimate goal of the three governments as they prepare for the review process.

In the meantime, Canadian business needs to be prepared for some potentially tumultuous re-negotiations. The good news is that, thanks to the work of some of the business groups already noted, the private sector is waking from its relative complacency and looking at contingency planning. Much work lies ahead.



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