



Canada-U.S. Relations

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Summary

Relations between the United States and Canada, though generally close, have undergone changes in tenor over the past three decades. During the 1980s, the two countries generally enjoyed very good relations. The early 1990s brought new governments to Ottawa and Washington, and although Canada's Liberal Party emphasized its determination to act independently of the United States when necessary, relations continued to be cordial. In early 2006, a minority Conservative government assumed power in Ottawa. It was regarded as being more philosophically in tune with the George W. Bush Administration than the Liberals had been; some observers believe that this compatibility helped facilitate bilateral cooperation. This cooperation has continued with the election of President Obama in November 2008, despite the differences in the two leaders' governing philosophies.

The two North American countries continue to cooperate widely in international security and political issues, both bilaterally and through numerous international organizations. Canada's foreign and defense policies are usually in harmony with those of the United States. Areas of contention have been relatively few, but sometimes sharp, as was the case in policy toward Iraq. Since September 11, the United States and Canada have cooperated extensively on efforts to strengthen border security and to combat terrorism, particularly in Afghanistan. Both countries were also active participants in the U.N.-sanctioned NATO mission in Libya.

The United States and Canada maintain the world's largest bilateral trading relationship, one that has been strengthened over the past two decades by the approval of two major free trade agreements. Although commercial disputes may not be quite as prominent now as they have been in the past, the two countries in recent years have engaged in difficult negotiations over items in several trade sectors, including natural resources, agricultural commodities, and intellectual property rights. The most recent clash centered around the Buy America provision of the 2009 economic stimulus law. However, these disputes affect but a small percentage of the total goods and services exchanged. In recent years, energy has increasingly emerged as a key component of the trade relationship. In addition, the United States and Canada work together closely on environmental matters, including monitoring air quality and solid waste transfers, and protecting and maintaining the quality of border waterways.

Many Members of Congress follow U.S.-Canada environmental, trade, and trans-border issues that affect their states and districts. In addition, because the countries are similar in many ways, lawmakers in both countries study solutions proposed across the border to such issues as federal fiscal policy and federal-provincial power sharing.

This report begins with a short overview of Canada's political scene, economic conditions, security and foreign policy, and environmental initiatives, focusing particularly on issues that may be relevant to U.S. policymakers. This country survey is followed by several summaries of current bilateral issues in the political, international security, trade, and environmental arenas. The questions following each summary are designed as potential inquiries to Canadian officials to promote thought and discussion among policymakers.

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Overview¹

Relations between the United States and Canada, though generally cordial, have undergone several changes in tenor over the past three decades. The 1980s and early 1990s were marked by an increasingly close partnership, whose milestones included the mid-1980s “Shamrock Summits” (named after the Irish heritage shared by the two countries’ leaders, Brian Mulroney and Ronald Reagan), the 1989 U.S.-Canada Free Trade Agreement, and the 1994 North American Free Trade Agreement. To many Canadians, however, Ottawa seemed at times to have drawn a bit *too* close to Washington, DC, with Canada casting itself too willingly in a secondary role.

In 1994, one Canada watcher observed that in the foreign policy arena, Canada “politely distances itself from the United States” in certain ways. In an interview that year, the newly elected Liberal Prime Minister Jean Chrétien summed up his view of the bilateral relationship: “We like each other. I just don’t want Canada to be perceived as being the 51st state of America.” Many believe, however, that this initial show of mild reserve was intended for domestic consumption, and that Canada and the United States in fact continued to enjoy excellent relations. Chrétien and President Bill Clinton are said to have had congenial meetings; they focused on areas where the two countries were able to reach agreement, including environmental issues, cooperation on border measures, and technology projects.²

In February 2001, President George W. Bush met with Chrétien. The two leaders discussed energy, missile defense, and trade. After September 11, however, economic and environmental issues often took a back seat to joint efforts to improve security, both at home and abroad. Canada became involved in the crisis at the outset, and has cooperated closely with the United States in efforts to combat international terrorism.

Nevertheless, Chrétien did not establish with President Bush the same rapport that he had enjoyed with Clinton. Differences over a number of issues tended to strain relations. The Bush Administration inherited some long-standing trade disputes, most notably over wheat and softwood lumber, and Canada and the United States were on different sides of several international issues, including the U.S. withdrawal from the ABM treaty and the International Criminal Court. But it was over security-related matters, particularly defense spending, Iraq, and missile defense, that the two governments had their sharpest differences. Despite these controversies, Canada and the United States continued to work together on a number of fronts to thwart terrorism, including strengthening border security, sharing intelligence and expanding law enforcement cooperation. The Canadian government passed a new anti-terrorism act, and Canada has contributed significant military assets to the NATO-led coalition in Afghanistan.

Paul Martin, who became prime minister in December 2003, met several times with President Bush. At the January 2004 Summit of the Americas, the two leaders discussed several topics and came to agreement on Canadian eligibility to bid on reconstruction contracts in Iraq and on the ground rules for U.S. deportation of Canadian citizens. In April 2004 in Washington, DC, Martin and Bush met once more and talked about a variety of issues, from terrorism to the “mad cow”

¹ Prepared by Carl Ek, Specialist in International Relations; and Ian F. Fergusson, Specialist in International Trade and Finance, Foreign Affairs, Defense, and Trade Division.

² “Canada Narrows Its Foreign Policy Goals to Focus on Trade.” By Charles Trueheart. *Washington Post*. November 17, 1994. p. A44. “Don’t Take Canada For Granted.” By Tad Szulc. *Parade Magazine*. February 20, 1994.

crisis. In November 2004, during President Bush's first official visit to Canada, missile defense, border security, and global "hot spots" were on the agenda. Although bilateral tensions heated up in 2005 over the issues of missile defense and softwood lumber, Canada's government and private citizens responded promptly and generously to assist the United States after Hurricane Katrina.³

In February 2006, after a come-from-behind election victory, the Conservative Party assumed power as a minority government, and Stephen Harper became Canada's 22nd Prime Minister—the first Conservative to lead the country in 12 years. Observers believed that Harper's government was somewhat more politically compatible with the Bush Administration in many areas. However, although the policy orientation of Harper's Conservatives may be similar to that of the Republicans in Washington, differences still arose on certain issues, particularly those that touched upon matters of perceived sovereignty. For example, on January 26, 2006, days before his inauguration, Harper sharply took exception to comments made earlier by the U.S. Ambassador to Canada and asserted Canada's sovereignty over the so-called Northwest Passage, the frozen arctic region that global warming may turn into a waterway linking Asia and Europe.⁴

The election of Barack Obama in November 2008 signaled a new chapter in U.S.-Canada relations. Unlike President Bush, Obama has been quite popular in Canada—a January 2009 public opinion poll put the new American president's approval rating in Canada at 86%; Obama has enjoyed continued popularity among Canadians—an October 2011 survey showed that 51% of Canadians believed Obama had done at least a "good" job, while another 30% said his performance had been "fair."⁵ Some believe that this favorable view may be facilitating the Harper government's cooperative efforts with the United States. In addition, although Harper has a more conservative orientation than Obama, many observers believe both leaders are pragmatic in their approach to solving public policy problems, and that the bilateral relationship will continue to be collaborative and productive. On February 19, 2009, renewing a tradition broken in 2001 by President Bush, President Obama made Canada his first official foreign visit. He and Harper focused on trade, climate change, and Afghanistan, among other issues; in September 2009, Harper met with Obama at the White House. Harper traveled to Washington to meet with Obama again in February and December 2011; the two leaders agreed to the establishment and implementation of a U.S.-Canada Regulatory Cooperation Council and issued a Declaration on a Shared Vision for Perimeter Security and Economic Competitiveness. Prime Minister Harper was in Washington again in April 2012 to attend a North American summit meeting with President Obama and Mexican President Felipe Calderon.⁶

³ "Bush Launches Bid To Repair US-Canada Ties." *Agence France-Presse*. November 30, 2004.

⁴ "Harper Tells U.S. To Butt Out On Plans For Defending Canada's Arctic." *Canadian Press*. January 26, 2006.

⁵ If Things Don't Work Out Next Year, Obama Could Always Come North: Poll. *Canadian Press*. October 18, 2011.

⁶ "Obama Makes Overtures to Canada Prime Minister." *New York Times*. February 20, 2009. "Obama's Popularity Higher Than Ever In Canada: Poll." *National Post*. September 20, 2009. "Obama May Be Slapped By U.S. Electorate, but Canada Still Claps: Poll." *The Canadian Press*. November 4, 2010. "PM and U.S. President Obama Announce Shared Vision For Perimeter Security and Economic Competitiveness Between Canada and the United States." Web site of the Canadian Prime Minister's Office. February 4, 2011.

<http://www.pm.gc.ca/eng/media.asp?category=1&featureId=6&pageId=26&id=3931>

Canada's Domestic Scene

Background and Current Political Situation

The Liberal Party, which took power from the Conservatives in 1993, was by 2003 being commonly referred to as “Canada’s natural ruling party.”⁷ Maintaining a Liberal majority appeared to be a safe bet at that time, but in early 2004 the “sponsorship scandal” erupted. Canada’s Auditor General issued a report stating that, under a program intended to build support for Canadian unity, the Chrétien government had funneled C\$100 million in public funds for dubious contracts to Québec advertising firms associated with the Liberal party.⁸

The Liberals’ standing in the polls plummeted, and the opposition parties strengthened. To the right of the Liberals, two conservative parties had merged under a new leader, Albertan Stephen Harper. And to the left, the New Democratic Party (NDP) likewise had recently elected a dynamic party chief, Jack Layton.

In June 2004 elections, the Liberals, despite losing seats in the House of Commons, won a plurality and formed a minority government. In November 2005, the Liberals lost a confidence vote, and snap elections were held on January 23, 2006. This time, the Conservatives won a plurality, and governed until May 2011 as a minority. Some analysts cautioned that the Tory victory did not necessarily represent a “paradigm shift” to the right in Canadian politics; they noted that the Conservative party won only 37% of the popular vote. Because past minority governments have been relatively short-lived, Harper kept one eye on the next elections. In addition, Harper relied upon the *ad hoc* support of the other three parties to ensure passage of the various items on his legislative agenda. Many believe that is why he advocated fairly centrist policies.⁹

However, Harper has been willing to challenge public opinion over Afghanistan, where the Liberal government deployed troops in 2002. In 2006, he won a narrow vote in parliament to keep Canadian troops in Afghanistan for two additional years. Harper initially characterized the mission as humanitarian in nature and also asserted that it was in Canada’s national interest to demonstrate its ability to play a leadership role internationally. But as Canadian operations shifted from peacekeeping to counter-insurgency and casualties mounted, public support diminished. Canadian troops ended their combat role there in July 2011.

Canada’s October 2008 elections did little to change the makeup of parliament. The Conservatives, who reportedly anticipated a weakening in future support, called the elections in hopes of capturing a majority. However, the Tories emerged only with a somewhat stronger plurality.

In November 2008, a budget bill put forward by the Conservatives precipitated a political crisis; the spending plan proposed, among other things, the elimination of federal funding for political

⁷ “Welcome To Their Nightmare: Finally, a Reason To Start Paying Attention To Politics Once Again.” *Globe and Mail*. December 8, 2003.

⁸ “Canada: Martin on the Ropes in Funding Scandal.” *Oxford Analytica*. February 25, 2004. February 23, 2004. “Canada’s Premier Acts to Counter Scandal.” By DeNeen L. Brown. *Washington Post*. February 17, 2004.

⁹ “Interview: Stephen Harper.” *Maclean’s*. March 6, 2006. “Conservatives To Govern From Political Center.” *Oxford Analytica*. January 24, 2006. “Harper’s Five Easy Pieces.” *Economist*. April 8, 2006.

parties. The opposition parties, which would have been severely affected by the plan, rebelled and were poised to vote down the government—ostensibly because Harper had failed to put forward a stimulus package that would respond to the economic downturn. Harper withdrew his proposals and, to avoid the no-confidence motion, prorogued (suspended or recessed) the session of parliament until January 2009; the shutdown was sharply criticized by many.¹⁰

During this time, the Liberal party named public intellectual Michael Ignatieff as their new leader. Some believed that when Parliament returned in January, he would seek to bring down the government and force new elections. However, he declined to do so, reportedly choosing instead to support the government's stimulus program (see below) and to consolidate the party's strength rather than challenge the Conservatives immediately.¹¹

In the fall of 2009, many believed the Harper government might face a no-confidence vote, particularly when public criticism was touched off by questions over how forthcoming the government had been during inquiries over official knowledge about the turnover by the Canadian military to Afghan authorities of prisoners who were subsequently abused and reportedly tortured. On December 30, 2009, Harper prorogued parliament until early March. Harper's spokesperson explained the move as one necessary to give the government the time to "recalibrate" and "consult" over its budgetary policies. However, other observers argued that Harper sent the legislature home in order to avoid confrontation over the detainee controversy. The second prorogation in roughly a year's time prompted harsh criticism by the opposition parties, as well as scattered protests around the country.¹²

However, an uptick in the economy helped Harper, whose party also benefited from a "bounce" from the success of the Vancouver Winter Olympics. In addition, the government's handling of aid to Haiti in the wake of the January 2010 earthquake earned praise. On the negative side of the ledger, Harper was faulted for two seemingly unnecessary prorogations, and also for not carrying out the institutional changes (including reform of the Senate and of the electoral process) that he promised during his late 2005 campaign and early in his tenure.

Some analysts in 2010 believed that the political stalemate might permit the Harper government to serve until the next general federal elections, set for October 2012. However, on March 25, 2011, the Conservatives lost a no-confidence vote presumably over a contempt of parliament ruling that the government had underestimated the costs of prison construction and of military fighter aircraft procurement; however, some observers maintain that the budget was the main point of contention.¹³

Canada's most recent elections were held on May 2, 2011; it was the fourth time Canadians had gone to the polls in seven years. But unlike the last three elections, which returned minority governments, this one resulted in significant changes for all of the national parties: first of all, the Conservatives managed to capture a comfortable majority of 166 seats in the 308-seat

¹⁰ "Canadian Leader Shuts Parliament To Avoid No-Confidence Vote, Angering Many." *New York Times*. December 6, 2008.

¹¹ "The Liberals Try a New Leader," *The Economist*, December 13, 2008.

¹² "Harper Goes Prorogue." *The Economist*. January 9, 2010. "Improved Poll Numbers Not Enough To Entice Ignatieff Into Spring Election." *Canadian Press*. January 28, 2010. "Conservatives Secure 10-Point Lead: Poll." *National Post*. April 12, 2010. "Stalled Institutional Reform Hurts Harper." *Oxford Analytica*. March 9, 2010. "Stimulus Has Boosted Growth, Harper." *Oxford Analytica*. April 14, 2010.

¹³ "Canada: Country Report." *Economist Intelligence Unit*. April, 2011. p. 11.

parliament—and a majority of seats in Québec—up from 144. In second place was the NDP, which wound up with 103 seats, almost triple the 36 they had held before. The Liberals won just 34 seats, down from 77, making them the third-largest party for the first time in the nation’s history. The separatist BQ was reduced from 48 down to just 4 seats—causing it to fall below the threshold for official party status. Finally, the Green Party managed to win a seat—another first.¹⁴

In explaining the results, observers note that many Canadians reportedly had become comfortable with Harper’s personality and leadership style. In addition, Harper has generally avoided divisive social issues and has instead succeeded in positioning his party more toward the center—a technique that had been used by the Liberals between 1993 and 2006. Harper’s trump card, however, was the economy (see below). Since the mid-1990s, both Liberal and Conservative governments had run budgetary surpluses, leaving the government in a good position to introduce limited stimulus measures during the global economic crisis, from which Canada emerged in better shape than most other developed countries.

Harper struck a conciliatory note on election night, saying “[w]e are intensely aware that we are and must be the government of all Canadians, including those that did not vote for us.” After 5 years of running a minority government, conservatives now have greater latitude to pass the kind of legislation they want to. But observers note that they still need to steer somewhat toward the middle—with an eye toward maintaining control of parliament after the next elections, which may be held no later than May 2016.

The Conservatives have already launched several proposals through parliament, including bills that would repeal the long gun registry, eliminate the Canadian Wheat Board, strengthen the criminal code, and scrap election subsidies for political parties. Harper has also proposed certain changes in the structure of the parliament, including increasing the number of members in the House of Commons—in order to reflect population changes—and reform of the by-appointment Senate. Harper has indicated that he will address other issues, including immigration reform, public pensions, and bilateral trade liberalization agreements with several countries. His government will also continue to assert its sovereignty in the Arctic, and to promote the production and export (mainly to the United States) of Alberta’s oil sands petroleum.¹⁵

The Liberals are reportedly attempting to rebuild their campaign coffers and are preparing for the next leadership race (Ignatieff resigned shortly after the elections). The NDP is a work-in-progress—many of the incoming class of MPs are young and/or relatively inexperienced, and, more importantly, the party lost its charismatic leader, Jack Layton, to cancer in August 2011. In March 2012, the NDP elected as their new leader Thomas Mulcair, a former Layton deputy. Mulcair is from Québec, and has been described as a “firebrand center-leaning” pragmatist.¹⁶

In recent weeks, Ottawa has been preoccupied with the so-called “Robocall” controversy. In February 2012—9 months after the elections—two journalists alleged that campaign operatives

¹⁴ Data from Canadian Parliament’s website, updated August 2011: <http://www.parl.gc.ca/Parlinfo/Files/Parliament.aspx?Item=1924d334-6bd0-4cb3-8793-cee640025ff6&Language=E&MenuID=Lists.Parliament.aspx>

¹⁵ “Harper Finally Wins Majority As NDP Surges Into Opposition.” *Globe and Mail*. May 2, 2011. “A Conversation With the Prime Minister.” *Policy Options*. June-July, 2011. p. 6.

¹⁶ “Canada Opposition Chooses New Leader.” *Agence France Presse*. March 24, 2012. “A Principled Pragmatist Who’s Always Up For a Fight.” *Globe and Mail*. March 26, 2012. NDP Opts For a Power Broker Over a Protest Leader. *Globe and Mail*. March 25, 2012.

for the Conservatives had computer-generated recorded telephone messages to registered opposition voters, directing them to incorrect polling stations. Elections Canada (the Canadian equivalent of the Federal Election Commission) is investigating the claims. The controversy, along with other factors, has caused the Conservatives to slump in the polls recently.¹⁷

National Unity

For more than four decades, an emotional debate has waxed and waned over the status of French-speaking Québec, Canada's second-largest province geographically and home to about one-quarter of its population. Many Québécois are concerned that their language and culture will be overwhelmed by the rest of English-speaking Canada. Some believe that their society may only be preserved if Québec separates from the rest of Canada and forms an independent country. A 1980 provincial referendum on "sovereignty-association" for Québec was defeated 60%-40%.

In October 1994 elections, after the provincial Liberals had governed Québec for several years, the province once more elected the separatist Parti Québécois (PQ). The victorious PQ held a referendum on sovereignty on October 30, 1995. Québeckers essentially voted on whether they wished to continue to remain a part of Canada, or strike off on their own. The vote went 50.6% to 49.4% in favor of keeping the country whole. The wafer-thin margin shocked federalists and separatists alike. Nearly two decades later, the country is still affected by the impact of what has been called a "near-death experience."

In 2003, Québec voters turned out the PQ and replaced them with the Liberals, led by Jean Charest. A former leader of the Progressive Conservatives at the national level, Charest is a committed federalist, which rules out another sovereignty referendum during his tenure. In the early part of his first term, Charest lost some support when he attempted to reduce the economic role of the provincial government; those efforts prompted strong protests from the powerful public service unions. Some Québec-watchers assert that Charest learned from this experience and changed his tactics. In elections held in 2007 and 2008, the Liberals won a plurality, and a majority, respectively; Charest retained his spot as premier. The next provincial election must be held by November 2013. In recent months, Charest's popularity has plummeted, in part due to corruption allegations associated with the construction industry. A recent poll showed the Liberals being trounced by the PQ.¹⁸

Since the debate began in the 1960s, the United States government has assiduously sought to remain officially neutral on the issue of Québec, continually repeating the three-point "mantra" that the United States enjoys excellent relations with a strong and united Canada; that the Québec question is an internal issue that is for Canadians to decide; and that the United States does not wish to interfere with Canada's domestic matters. However, some analysts detected a slight "tilt" on the part of Clinton Administration toward the federalists during the 1995 referendum campaign. If, at some future date, Québec eventually *does* leave the confederation, the U.S. government will be faced with difficult political and economic questions.

¹⁷ "Delayed Reaction." *The Economist*. March 3, 2012. "Tories Accused of Minimizing Robo-calls Controversy." *Globe and Mail*. March 30, 2012. "Numbers Add Up To Trouble For Tories." *National Post*. March 23, 2012.

¹⁸ "'The Nationalists Are on the Rise': Pollster; Forum Research Survey; PQ Would Romp To Landslide Victory If Provincial Election Were Held Today" *Montreal Gazette*. March 27, 2012.

Foreign and Security Policy Issues

The Canadian Ministry of Foreign Affairs and International Trade lists five policy priorities for the period 2011-2012:

- implementation of the Global Commerce Strategy, with a special focus on emerging markets (including China, India, and Brazil) and on negotiating a trade agreement with the European Union;
- further strengthening of ties with the United States through cooperation in the areas of border management, trade, investment, energy (particularly with regard to oil sands), and the environment;
- contributing to effective international governance, security, and stability;
- enhancing security cooperation in the Americas, particularly with Mexico, Central America, and Haiti; and
- exercising sovereignty in the Arctic.¹⁹

As a middle power, Canada has exercised a somewhat disproportionate influence in world affairs, chiefly through its active participation in international organizations, including the G-8, G-20, and the Asia-Pacific Economic Cooperation forum. From 1998 to 2006, Canadian diplomat Louise Frechette served as Deputy Secretary General of the United Nations, and from 1996 to 2006 Canadian Donald Johnston was Secretary General of the Organization for Economic Cooperation and Development. The president of the International Criminal Court from 2003 to 2009 was Judge Philippe Kirsch from Canada. The first head of the U.N. War Crimes Tribunal was Canadian Louise Arbour.

Canadian military officers have also been tapped for leadership positions in international organizations and coalitions. In June 2005, Air Force General Ray Henault was named head of NATO's military committee, a post he held until 2008. And in 2011, Lieutenant-General Charles Bouchard was head of the allied military operations in Libya.²⁰

Canadians are proud of the active role played by their military as international peacekeepers. Since the United Nations first dispatched an armed peacekeeping contingent to help defuse the Suez Crisis in 1956, Canada has participated in numerous U.N. peacekeeping operations, from Cyprus and the Sinai, to Bosnia, Rwanda, Somalia, and Afghanistan. As of March 2012, more than 1200 Canadian Forces personnel were participating in international operations in Afghanistan, the Caribbean, the Middle East, and Africa. An autumn 2010 survey showed that 52% of Canadians "believe traditional peacekeeping is the proper role for our men and women in uniform."²¹

¹⁹ Priorities For 2011-2012. Foreign Affairs and International Trade Canada. Modified March 8, 2012. http://www.international.gc.ca/about-a_propos/priorities-priorites.aspx?view=d

²⁰ "Canada Moving Into Role As Leader Overseas." *Vancouver Sun*. March 28, 2011.

²¹ *Canada and International Peacekeeping*. By Joseph T. Jockel. Center for Strategic and International Studies/Canadian Institute of Strategic Studies. Washington, DC, 1994. Canadian Forces Operations. Canadian National Defence web site. Updated March 23, 2012. <http://www.forces.gc.ca/site/operations/index-eng.asp> "Canada Must Stand On Guard." *Winnipeg Free Press*. October 27, 2010.

As with other countries in the 1990s, Canada's military was subject to dual pressures. In Ottawa's view, the collapse of the Soviet Union and the Warsaw Pact reduced the military threat, making it more difficult for the government to justify sustaining historic spending levels on defense. Leaders believed that the country's large debt early in the decade necessitated funding cutbacks in most areas of government, including defense. However, relative to its NATO allies, Canada had devoted only a modest share, about 2% of GDP, of its budget to defense spending during the 1980s and 1990s. That percentage declined even further, from 2.01% in 1990 to 1.1% in 2005; among the 26 NATO members, only Luxembourg and Iceland (which has no armed forces) spent a lower percentage. Canada's meager military budget irked some within the alliance, particularly the United States.²²

After the round of cutbacks in the 1990s, the number of active personnel in Canada's armed forces tumbled from 87,000 in 1989 to 52,000 in 2004, the 56th largest in the world. The Canadian forces also were strapped for resources to replace aging equipment. This trend disturbed many, and there were numerous warnings published. In March 2002, a Canadian Senate committee called for increased defense spending to counter the threat of international terrorism; it also recommended that personnel levels be increased and that more resources be provided to the Canadian Security Intelligence Service. A November 2002 Senate report recommended boosting troop levels to 75,000 and restructuring the armed forces. A brace of studies in the fall of 2003 likewise called for changes in force restructure and procurement practices and for increases in manpower and budgets. A news report characterized one of the studies as concluding that "Canadian Forces are teetering on the edge of irrelevance." In September 2005 the Senate published yet another report, which called for a doubling of spending on defense.²³

Recent Canadian governments appear to have heeded these messages. As of March 2011, there were approximately 66,000 regular force members and 34,000 reserves. In addition, Canada's defense spending has been trending upward. The budget tabled in February 2005 contained the largest military spending increase in two decades: C\$12.8 billion—roughly equal to the entire 2005 military budget—spread over five years. The Harper government's first budget added C\$5.4 billion in military spending over the next four years. The 2007 budget confirmed the previous year's spending increase, and the 2008 budget sought to ensure continuity through the Canada First Defence Strategy, which is set to provide for yearly increases of 2% beginning in 2011-2012. The government budget for the armed forces in 2008-2012 will average around C\$20 billion annually; due to budget retrenchment, the rate of growth of military spending is expected to slow. In addition, Canada unilaterally halted its contribution to two NATO air surveillance programs, and may cancel, delay, or reduce its planned purchase of F-35 fighter aircraft (see below).²⁴

U.S.-Canada Foreign and Security Policy Issues

For a variety of practical and historical reasons, Canada's relations with the United States have always been a key priority. The two countries share a 5,500 mile border, a common language, cultural similarities, as well as vital interests in the international realm. Trade between the two

²² "Spend More On Military, U.S. Envoy Urges Ottawa." *Toronto Star*. February 25, 2004.

²³ "Armed Forces Hobbled, Report Says." By Daniel LeBlanc. *Globe and Mail*. December 3, 2003. "Senators Sounding Alarm On Defence." *The Gazette*. October 3, 2005.

²⁴ *The Military Balance, 2011*. International Institute for Strategic Studies. Defence and Budget 2005—Highlights. DND website. http://www.forces.gc.ca/site/reports/budget05/summ05_e.asp.

countries exceeds \$1 billion per day; however, Canada's dependence on exports to the United States has prompted several governments to attempt to expand and diversify its international commerce.

According to the U.S. State Department, "U.S. defense arrangements with Canada are more extensive than with any other country." Former Canadian Ambassador to the United States Michael Kergin referred to the defense relationship as being "intermestic" in nature.²⁵

Over the past century, U.S.-Canadian defense cooperation has been close. In 1940, President Franklin D. Roosevelt and Prime Minister McKenzie King established the Permanent Joint Board on Defense, which formalized bilateral consultation on military matters and is still in operation. In 1949, the two countries were founding members of NATO. During peacetime, military cooperation has occurred chiefly in the context of bi- and multinational organizations.

NORAD

In 1958, Canada and the United States signed the North American Aerospace Defense Command (NORAD) agreement. The continental air defense pact monitors U.S. and Canadian airspace and encourages joint efforts in aerospace technologies. In the wake of the September 11 terrorist attacks, there were discussions of deepening military cooperation along the NORAD model, in the context of the newly created U.S. Northern Command, to include land and sea forces. But some Canadians were concerned that such a move might impinge upon Canada's sovereignty, and in August 2002, the Canadian government announced that its land and sea forces would not be participating in the command. In December 2002, however, the two countries signed a new accord creating a binational planning group (BPG) based at NORAD to coordinate responses to terrorist attacks and other crises. The BPG issued its final report in March 2006; the panel put forward numerous recommendations, including that the two countries develop a common security vision and improve interoperability through joint military planning, training, exercises, and information sharing. In August 2004, Canada and the United States amended NORAD to permit it to share information on incoming ballistic missiles. Ottawa and Washington also agreed to expand the scope of the agreement to encompass nautical surveillance.

In February 2008, the commanding generals of U.S. Northern Command and of its Canadian counterpart, Canada Command, signed a binational Civil Assistance Plan. Under the plan, the armed forces of each country, after appropriate consultation with civilian authorities on both sides of the border, may come to the support of the other country's military in the event of civil emergencies such as floods, earthquakes, or the effects of a terrorist attack. In May 2011, NORAD leaders noted that changes in the Arctic—specifically, ice melt and commercial development—would likely lead to a need for increased activity in the high north.²⁶

²⁵ United States Department of State. Bureau of Western Hemisphere Affairs. *Background Note: Canada*. December 22, 2011. "Remarks to the Center for Strategic and International Studies." February 28, 2005.

²⁶ "Continental Divides." By Sydney J. Freedberg, Jr. *National Journal*. March 23, 2002. "Leading academics Examine Risks Inherent In Closer Military Co-operation With the United States." *Canada NewsWire*. April 26, 2002. "Canada Won't Join Norad-Like Land-Sea Force. By Rick Mofina." *Ottawa Citizen*. August 15, 2002. September 12, 2005. Binational Planning Group. Final Report. March 13, 2006. <http://www.canadianally.com/BPGFinalReport.pdf> U.S. Northern Command website: <http://www.northcom.mil/news/2008/021408.html> "NORAD Commanders Say Melting Ice and Energy Development Will Make Arctic Busier." *Canadian Press*. May 7, 2011.

Missile Defense

Ottawa long debated whether it should participate in the U.S. ballistic missile defense (BMD) system. Some analysts expressed reservations over the plan, in the belief that it might spark a new arms race, while others reportedly preferred to keep Canada's options open. Parliament held hearings on the issue, but no official policy was enunciated. Finally, in May 2003, Canada said that it would enter into discussions with the United States; a Canadian military affairs journalist described Canada's likely negotiating goals: "Canada wants the anti-missile shield run by NORAD—in effect, giving Canada equal status in protecting North America and a finger on the trigger. Ottawa wants a share of the industrial benefits and access to secret technologies, all while paying little or nothing. And it continues to insist that space not be weaponized."²⁷

On February 24, 2005, the Canadian government said that it would not participate in BMD. However, Canada's ambassador to the United States had pointed out earlier that the two countries had already agreed to allow NORAD to share information with U.S. BMD commands. U.S. officials expressed puzzlement and disappointment with the announcement, noting that Canada had sent signals that it would likely sign on. Polls showed that a majority of Canadians, particularly Québeckers, opposed BMD, leading some analysts to suggest that domestic political pressures may have guided the decision. In late February 2006, Canada's Defense Minister said that the Harper government likely would review the missile defense issue if asked to do so by Washington. Any final decision on participation, he added, would be subject to a parliamentary vote. In April 2008, U.S. Air Force General Gene Renuart, head of NORAD, was quoted as having said that all incoming intelligence concerning missile threats was shared with Canada.²⁸

Joint Strike Fighter

In February 2002, Canada agreed to participate in the further development of the U.S.-led multinational Joint Strike Fighter (JSF, or F-35) program, contributing \$150 million over a 10-year period. In December 2006, it was announced that the Canadian government had committed an additional C\$500 million for the development of the aircraft. Canada has reportedly agreed to consider purchasing the new fighters to replace its own fleet of CF-18 planes when they are retired in 2017, and has earmarked nearly C\$4 billion for the new planes. In June 2007, the Department of National Defense announced plans to form a new office to evaluate Canada's future air defense requirements. Canada appeared to reap rewards from its participation; as of June 2007, Canadian firms had won 150 JSF contracts worth about \$160 million. In addition, Canadian defense companies stand to benefit from the Pentagon's plans to purchase additional F-35s. In July 2010, Defense Minister MacKay confirmed that the government planned to spend C\$9 billion on the acquisition of 65 F-35 aircraft. The opposition Liberals criticized the decision, arguing that it should have been reviewed by parliament first, while the New Democrats maintained that the radar-evading F-35 may be more airplane than Canada needs. The media have also faulted the purchase, pointing to large cost overruns. During a January 2011 visit to Canada, former U.S. Defense Secretary Robert Gates urged Canada to proceed with its planned procurement of the aircraft. However, in early 2012, it was reported that the government was

²⁷ "Shoot Down Defence Dreamers." By Paul Koring. *Globe and Mail*. June 25, 2003.

²⁸ "Canada and the U.S. Missile Defense System." Dwight M. Mason. *CSIS Hemisphere Focus*. January 9, 2004. "Martin and the Politics of Missile Defense." *Globe and Mail*. May 1, 2004. "Martin's Move Irritates U.S." By Sean Gordon. *Toronto Star*. February 24, 2005. "Minister Backs U.S. Missile Plan." *Toronto Star*. February 24, 2006. "Canada Kept In Loop At NORAD About All Missile Threats." *Ottawa Citizen*. April 10, 2008.

contemplating delay or cancellation of the purchase. Associate Defense Minister Julian Fantino told a parliamentary defense committee that “we have not as yet discounted the possibility, of course, [of] backing out of the program.” He later clarified that the government might purchase fewer than 65, and that “this government will adapt our plans as necessary to maintain this acquisition within the existing budget.”²⁹

NATO

Canada has been engaged in the debate over NATO’s future. It supported the 1999 and 2004 rounds of enlargement and announced that it would participate in the NATO Response Force, which the alliance agreed to at its November 2002 Prague summit. At the April 2008 Bucharest summit, Canada endorsed the addition of Croatia, Albania, and Macedonia; in addition it supported the proposal to offer Membership Action Plans to Georgia and Ukraine. Finally, as noted above, Ottawa has maintained troops in Afghanistan since 2002, and its military leaders have served in a command capacity. In April 2003, then Foreign Minister Graham, along with the Dutch and German governments, requested that NATO take over command of ISAF.³⁰ In a 2009 speech in the UK, Canadian Defense Minister Peter MacKay cautioned that NATO was being tested in the crucible of Afghanistan, and urged more equitable burden sharing.³¹

Although it has no troops stationed in NATO territory in Europe, Canada in recent years contributed several hundred troops to the NATO-led Stabilization Force (SFOR) in the Balkans. Canada also supplied 200 troops to NATO’s mission in Macedonia. Canada cooperated “wing-to-wing” with the United States in *Operation Allied Force*, the NATO campaign of air strikes against targets in Serbia and Kosovo, contributing 18 CF-18 fighter aircraft and providing two rotations of approximately 1,500 troops each to KFOR. In addition Canada has supported non-NATO peacekeeping operations; it has provided 600 to the initial U.N. peacekeeping mission in East Timor and has also sent 500 troops to maintain stability in Haiti. In 2011, former Secretary of Defense Robert Gates lauded Canada for its contributions to the alliance missions in Afghanistan and Libya.³²

In March 2012, however, it was reported that, as a part of its wide-ranging budget retrenchment efforts, the Canadian government had notified the alliance that it would halt its participation in the NATO Airborne Warning and Control System (AWACS) and the Alliance Ground Surveillance (AGS) program; the government estimates savings at C\$90 million.³³

²⁹ “Canadian Firms Big Winners In U.S. Jet Project.” *National Post*. April 21, 2006. “Canada Commits Up To \$500 Million to the Development of CF-18 Replacement.” *The Canadian Press*. December 13, 2006. “New Office To Assess Canada’s Fighter Needs.” *Defense News*. June 18, 2007. Forces Tag \$3.8B To Buy Advanced Jets. *Ottawa Citizen*. June 27, 2007. “Canada’s Defense Chief Rejects Criticism of F-35 Jet,” *New York Times*. July 17, 2010. “Costs Rocket for Canada’s Jet Fighter,” *Toronto Star*. May 20, 2011. “Canada’s F-35s: Engines Not Included” *Ottawa Citizen*. April 17, 2011. “U.S. Calls On Canada to Stick With F-35,” *Globe and Mail*. January 27, 2011. “Ottawa Having Second Thoughts on F-35 Jets.” *Globe and Mail*. March 14, 2012. “Tories Say F-35 Jets Will Come, Eventually.” *Toronto Star*. March 17, 2012.

³⁰ “NATO Umbrella Sought.” By Allan Thompson. *Toronto Star*. April 4, 2003. “NATO Sees Key Role For Canada In Afghan Security.” *Reuters*. May 6, 2003. CRS interview of Canadian government official, May 7, 2008.

³¹ NATO’s Future At Stake In Afghanistan: MacKay. *Ottawa Citizen*. February 16, 2009.

³² Current Operations. Canadian Expeditionary Force Command website. Updated April, 2009. <http://www.comfec-ccfcom.forces.gc.ca/pa-ap/ops/index-eng.asp> “Canada Punches Above Its Weight In NATO: U.S. Defence Secretary,” *Montreal Gazette*. June 11, 2011.

³³ “Canada Bails Out of NATO Surveillance Programs.” *National Post*. March 19, 2012.

Afghanistan

Canada was one of the first countries to join the military operation in Afghanistan; its participation dates back to October 2001. Along with British, Dutch, Danish, and U.S. troops, Canadian forces have been serving on the front line in the combat operations to counter attacks by al Qaeda and Taliban fighters. Much of the time, Canada maintained approximately 2,800 troops in the country. A total of 157 Canadians, including one diplomat, have died in Afghanistan. In 2005, Canada launched a Provincial Reconstruction Team mission in Kandahar. Ottawa also has provided humanitarian and reconstruction assistance to Afghanistan. Canada is among the top five donors to the country, and has pledged C\$1.9 billion through 2011 in reconstruction and development assistance.³⁴ As noted above, Canada ended its combat role there in July 2011, however, Canadian troops (510 as of January 2012) will remain until 2014 to help train Afghan national security forces.

Libya

In March 2011, the Harper government committed approximately 650 troops, including air, sea, and land forces, to assisting the U.N.-sanctioned NATO mission to protect the civilian population in Libya. Canadian CF-18 fighters patrolled the no-fly zone and conducted a disproportionately large number of air strikes, and the frigate *HMCS Charlottetown* came under fire from Qadhafi loyalists, but suffered neither damage nor casualties. In late March, a Canadian general was appointed commander of NATO military operations in Libya. Some analysts argued that Canada took part in the mission in order to demonstrate its continuing commitment to the North Atlantic alliance, and to reinforce Canada's traditional leadership role in U.N. peacekeeping missions. According to public opinion polls, there was strong public support for Canada's participation.³⁵

Haiti

Canada and the United States have worked closely together over the past 17 years with the U.N. mission in Haiti, where a contingent of the Canadian armed forces, along with members of the Royal Canadian Mounted Police, took the reins from departing U.S. forces who had helped restore the democratically elected government in Haiti in 1994. In 2004, after the Aristide government stepped down in the face of armed rebellion, Canada joined the United States and France in providing peacekeepers to the U.N.-authorized Multinational Interim Force sent to the troubled island; Canada dispatched helicopters and nearly 500 troops. In February 2008, then-Canadian Foreign Minister Bernier traveled to Haiti, where he announced that Ottawa's total multiyear aid package would be raised to C\$555 million. In the wake of the turmoil over food shortages, he called for international donors to harmonize their assistance during an April 2008 donor conference. Haiti is the second-largest recipient (after Afghanistan) of Canadian development assistance. Canada's former Governor General, Michaëlle Jean, who was born in

³⁴ DND website: http://www.forces.gc.ca/site/newsroom/view_news_e.asp?id=1703. "Canadian Development Assistance In Afghanistan: Current Projects." Government of Canada website. January 31, 2008. http://www.canada-afghanistan.gc.ca/cip-pic/afghanistan/library/afgh_security-en.asp "Canada's War in Afghanistan Is Over." *National Post*. August 8, 2011.

³⁵ "Dispatch: Canadian Support For the Libya Intervention." Stratfor. March 28, 2011. "Libya: New Development." Foreign Affairs and International Trade Canada web site. September 1, 2011. "Canada: Country Report." *Economist Intelligence Unit*. April, 2011. "Canada Contributed a Disproportionate Amount To Libya Air Strikes: Sources." *National Post*. August 25, 2011.

Haiti, traveled to the island in January 2009; she visited several development projects, and met with government and civil society leaders. Jean returned to visit following the January 12, 2010, earthquake that devastated the country. At an international donor conference held at the United Nations, Canada made a two-year pledge of C\$400 million in humanitarian and reconstruction assistance, making it the largest per capita provider of aid to Haiti. Canada employs a “whole-of-government” approach in supporting Haiti, involving the Defense and Foreign Affairs Departments, the Canadian Border Services Agency, the Royal Canadian Mounted Police, and Correctional Services Canada.³⁶

Iraq

Canada was disinclined to expand the so-called war on terrorism beyond Afghanistan to Iraq. In September 2002, during a meeting in Detroit with President Bush, Chrétien reaffirmed Canada’s preference for a U.N. mandate, a stance that strongly reflected Canadian public opinion. Washington later requested of Ottawa specific military commitments in the event of a conflict with Iraq, but no definitive answer was given. Over the following months, the government’s statements on Iraq were characterized by the media as imprecise and at times contradictory, an apparent attempt to keep options open. But in the House of Commons on March 18, 2003, Chrétien stated unequivocally that “Canada will not participate.” The Bush Administration expressed disappointment with the decision.³⁷

Washington subsequently requested that Canada assist in the reconstruction of Iraq by sending troops or military police. Ottawa responded by offering 150 members of its Disaster Assistance Response Team, a non-traditional military unit consisting of security, engineering, and medical personnel. Canada also provided funding in a number of areas, including humanitarian and reconstruction aid, support for elections, and police training. The Canadian International Development Agency pledged C\$300 million (2003-2010) in assistance to Iraq. In January 2004, Canada announced that it would cancel Iraq’s \$564 million debt.³⁸

Cuba

Cuba has been another issue where the two countries have not always seen eye-to-eye. For decades, Canada has maintained normal diplomatic relations with Cuba, and has maintained relatively extensive business links: Canada is Cuba’s third-largest trading partner and its number one source of tourists. Because of this ongoing commercial relationship, Canadian government officials publicly criticized a U.S. law (the Cuban Liberty and Democratic Solidarity Act, P.L. 104-114) that seeks to apply indirect pressure on the Castro regime by permitting Cuban

³⁶ “Canada Pledges \$555 Million In Aid To Haiti.” *Reuters*. February 24, 2008. Canada Participates In Harmonization Efforts In Haiti. News Release. Foreign Affairs and International Trade Canada. April 23, 2008. ‘I Can Feel the Strength of the People,’ Jean Says. *National Post*. March 30, 2010. Canada Pledges \$400 million To Haiti. *Ottawa Citizen*. April 1, 2010. Canada’s Role In Haiti. *Globe and Mail*. April 3, 2010. Government of Canada web site, last modified January 1, 2011. http://www.canadainternational.gc.ca/haiti/engagement/whole_of_government-pangouvernementale.aspx?view=d

³⁷ “Well, Maybe ...” *Economist*. September 28, 2002. “PM Scolds McCallum On Canada’s Role In Iraq.” By Shawn McCarthy and Daniel Leblanc. *Globe and Mail*. January 16, 2003. “Bravos Greet Chrétien.” By Tim Harper. *Toronto Star*. March 18, 2003.

³⁸ “Iraq: Canada’s Commitment.” Canadian International Development Agency web page: <http://www.acdi-cida.gc.ca/iraq#1> Updated May 24, 2007.

Americans to file lawsuits against foreign firms that use Cuban property that was expropriated by the Castro regime. U.S. supporters of the Cuba embargo have been critical of Canadian mining companies and hotel chains that do business with the island nation. Canadians, who are sensitive to being perceived as America's "junior partner," object that the law amounts to the United States forcing its foreign and commercial policies upon other countries. In 2003, after the Castro government handed down draconian prison terms to 75 political dissidents, Ottawa expressed official disapproval. The transfer of Cuba's presidency from Fidel to Raul (temporary in 2006, permanent in 2008) prompted vigorous debate in the Canadian press over what policy Ottawa should adopt toward Cuba.³⁹ In April 2009, the Obama Administration announced that it would ease restrictions on family travel and remittances to Cuba and allow greater telecommunications links with Cuba. The decision was welcomed by Ottawa; Peter Kent, Minister of State of Foreign Affairs for the Americas, commented that "the election of the Obama Administration has given real momentum to the sort of change that Canada has been encouraging for a long time." A planned trip by Kent to Havana in May 2009 was cancelled, reportedly because Kent had said that he planned to address the human rights issue during his trip, and because Prime Minister Harper had referred to himself as an "anti-communist conservative." The trip was re-scheduled, and Kent traveled to Cuba later in the year. In mid-2010, relations were strained over the case of a teenaged Canadian traveler detained for three months in Cuba. The 19-year-old, who suffered injuries when the vehicle he was driving was sideswiped by a pickup truck, was held by Cuban authorities under threat of a jail sentence. He was allowed to return in early August.⁴⁰

China

Relations between Canada and China were somewhat cool during the early years of the Harper government, when Ottawa criticized Beijing's human rights practices and conferred honorary citizenship on the Dalai Lama.⁴¹ Observers argue that a turning point occurred in late 2009, when Prime Minister Harper, reportedly responding to the Canadian business community, made his first trip to China; Premier Wen Jiabao publicly chided the Canadian Premier for not having visited sooner. Today, the Canadian Government's web site characterizes bilateral cooperation as "strong," noting that several ministries "have productive cooperation programs and memoranda of understanding with their Chinese counterparts, and hold regular exchanges" During a July 2011 visit to Beijing, Foreign Minister John Baird declared that relations between the two countries had "entered a new era," and described China as a "friend" and "ally." Prime Minister Harper traveled to China a second time in February 2012. During the visit, he signed 20 commercial deals worth C\$3 billion, as well as a declaration of intent on a long-pending investment protection agreement.⁴²

³⁹ See, for example: "Castro's Resignation Unlikely To Change Canadian-Cuban Relations, Experts Say." *The Canadian Press*. February 19, 2008. "Don't Support Castro's Island Prison." *National Post*. February 19, 2008. "With Fidel Castro Gone, U.S. Hawks Will Look North." *Toronto Star*. February 20, 2008. "The Autumn Of the Patriarch." *Ottawa Citizen*. February 23, 2008.

⁴⁰ "Unreformed Tyranny." *Globe and Mail*. November 23, 2009. "Cuba To Give Canada Expanded Air Access With Island To Boost Tourism." *Canadian Press*. January 15, 2010. "Cuba's Tainted Image." *Toronto Star*. August 4, 2010.

⁴¹ Canada: Country Report. *Economist Intelligence Unit*. August, 2011. p. 11. Canada/China: Harper Trip Raises Hoes For Relations. *Oxford Analytica*. December 2, 2009.

⁴² Canada—China. Government of Canada web site: http://www.canadainternational.gc.ca/china-chine/bilateral_relations_bilaterales/china_canada_chine.aspx?lang=eng&view=d 'New Era' For Canada and China, Baird Says. *National Post*. July 21, 2011. Baird Embraces China As 'Friend.' *Globe and Mail*. July 19, 2011. "Harper's China Visit Ends with Panda Pact." CBC News. February 11, 2012. <http://www.cbc.ca/news/world/story/2012/02/11/harper-china-saturday.html>

International Criminal Court

The International Criminal Court (ICC) is another issue on which the two countries differ. Canada has long been a leading advocate of the U.N.-sponsored tribunal, while some U.S. policymakers have opposed U.S. participation on the grounds that it might make U.S. military personnel vulnerable to politically motivated prosecution by hostile regimes. In May 2002, the Bush Administration declared that the United States would not support the ICC; the same day, then-Canadian Foreign Minister Bill Graham declared that he was “extremely disappointed” with the U.S. decision. In a U.N. speech four months later, Graham faulted the United States “for its ‘ad hoc and unilateral pursuit’ of the prosecution of crimes against humanity.”⁴³

Border Security

In the wake of the attacks on New York and Washington, U.S.-Canadian relations came to the fore. In particular, the issue of U.S.-Canada border security was brought into sharp focus. The issue first became a matter of urgent concern in December 1999, when U.S. border officials, acting on a tip from Canadian authorities, stopped Ahmed Ressam at the U.S.-Canadian border as he was attempting to smuggle explosives into the United States; it was later discovered that Ressam had planned to bomb the Los Angeles airport, and that he had received terrorist training from Al-Qaeda in Afghanistan.

Despite the fact that none of the 19 September 11 hijackers entered from Canada, the attacks sparked renewed debate over Canadian laws regarding the treatment of immigrants seeking refugee status or political asylum.⁴⁴ By February 2002, Ottawa had already made “steps to tighten immigration and refugee policies, including more rigorous screening of people who claim refugee status and stepped up detentions and deportations of claimants suspected of being security risks.”⁴⁵

Some American policymakers pointed to the Ressam case as proof that the United States must tighten its borders with Canada. Skeptics, however, note that such measures might seriously impede commerce by creating long delays at border crossings, and that determined terrorists and criminals would at best be inconvenienced, not stopped, in traversing the two countries’ 5,500-mile border. About 80% of U.S.-Canada merchandise trade crosses the border by truck; many of these shipments are “just-in-time” deliveries; their delay at border crossings can seriously disrupt manufacturing in the United States and Canada.⁴⁶ Both sides have strong incentives to strengthen security but keep goods flowing.

Since the September 11, 2001, attacks, Ottawa and Washington have taken numerous steps, separately and jointly, to improve border control. In December 2001, they signed the Smart

⁴³ “Canada Raps U.S. Rejection Of World Criminal Court.” By David Ljunggren. *Reuters*. May 6, 2002. “U.S. Rift With Allies On World Court Widens.” By Julia Preston. *New York Times*. September 10, 2002.

⁴⁴ In April 2009, U.S. Department of Homeland Security Secretary Janet Napolitano raised concerns when she averred that some of the 9/11 terrorists had crossed over from Canada. “Napolitano’s Comments About Canada’s Border Spark Diplomatic Kerfuffle.” *The Canadian Press*. April 21, 2009.

⁴⁵ “Al-Qaida In Canada?” CBSNEWS.com. April 25, 2002. “Canada Alters Security Policy To Ease Concerns of U.S.” By Clifford Krauss. *New York Times*. February 18, 2002.

⁴⁶ Canadian Government Fact Sheet: A Unique and Vital Relationship, modified, June 2, 2011, <http://www.canadainternational.gc.ca/can-am/offices-bureaux/welcome-bienvenue.aspx?lang=eng&view=d>

Border declaration that aims at improving security and efficiency at border crossings; the agreement lays out a 30-point (since increased to 32-point) list of areas of joint activity, ranging from pre-clearance of goods (the FAST program) and people (NEXUS), to biometric identifiers, to infrastructure improvements. The cooperation covers crossings by air, land, and sea traffic. In December 2002, the two nations signed the Safe Third Country agreement, intended to permit coordination of refugee and asylum policy.

The two countries also cooperate extensively on law-enforcement activities around the border. Since 2002, U.S. Immigration and Customs Enforcement (ICE) and Royal Canadian Mounted Police (RCMP), along with partner agencies in each country, have established 15 Integrated Border Enforcement Teams (IBETs) operating at 24 locations at and between U.S.-Canadian ports of entry. The IBETs are binational, multi-agency, intelligence-led enforcement teams focused on identifying, investigating, and interdicting common national security threats and criminal activity. Between 2005 and 2010, RCMP and U.S. Coast Guard agents also participated in the Shiprider pilot program, allowing fully cross-trained and cross-designated agents from each country to conduct joint enforcement exercises along international waterways. The countries signed an agreement to expand and extend Operation Shiprider in 2009, but the agreement has yet to be approved by the Canadian Parliament.

In February 2011, President Obama and Prime Minister Harper signed the Beyond the Border declaration, which described their shared visions for a common approach to perimeter security and economic competitiveness. The 2011 agreement focuses on information sharing and joint threat assessments to develop a common and early understanding of the threat environment; infrastructure investment to accommodate continued growth in legal commercial and passenger traffic; integrated cross-border law enforcement operations; and integrated steps to strengthen shared cyber-infrastructure.

This vision was fleshed out by the Beyond the Border Action Plan, released during a meeting of the two leaders on December 7, 2011. It set out goals and progress metrics related to:

- harmonized cargo screening under the “cleared-once, accepted twice” principle,
- joint inventories and gap analysis related to travel and trade threat assessments and border surveillance,
- automated biographic and biometric data sharing,
- an integrated entry-exit system,
- enhanced pre-clearance of goods and travelers, and
- expansion of interoperability among law enforcement and deployment of cross-designated personnel.⁴⁷

The Western Hemisphere Travel Initiative (WHTI), a provision of a 2004 U.S. law requiring travelers passing between the two countries to present a passport, a NEXUS card, or an equivalent secure, approved document, at the border came into effect on June 1, 2009. The Department of Homeland Security (DHS) has worked with the Canadian government to develop an alternative document that is secure, inexpensive, and would be carried anyway—for example,

⁴⁷ United States-Canada Beyond the Border Action Plan, December 2011, available at: <http://www.dhs.gov/xlibrary/assets/wh/us-canada-btb-action-plan.pdf>

a driver's license containing enhanced biometric information. Currently, such enhanced licenses are being issued by the provinces of British Columbia, Manitoba, Ontario, and Québec, and by the states of Michigan, New York, Vermont, and Washington. In March 2011, GAO reported a greater than 95% compliance rate with WHTI requirements in FY2010.⁴⁸

Canada's custom service stepped up the purchase of high-tech X-ray equipment, and U.S. and Canadian customs agents are working together, inspecting containers at several Canadian and U.S. seaports. Border security personnel levels have also been beefed up, and Integrated Border Enforcement Teams have been established in high-priority regions. Canada also has set up an Air Transport Security Authority, which, among other activities, is responsible for pre-board screening.

In 2004, the Canadian government created a Department of Public Safety and Emergency Preparedness, a counterpart to the U.S. DHS, and a Border Services Agency. Recent Canadian federal budgets have contained new monies for security-related priorities such as intelligence, maritime and cyber security, threat assessment, and emergency response.

Canada has taken other actions beyond the realm of border security, including freezing terrorists' assets, broadening the scope of terrorist activities punishable by law, extending police investigative powers, introducing legislation that would put restraints on fund-raising activities by extremist organizations, expanding cooperation between the FBI and the RCMP, and increasing outlays for countering nuclear, biological, and chemical weapons attacks.⁴⁹

In early June 2006, Canadian police conducted a series of raids in the Toronto area, arresting 18 individuals. The arrests were made in accordance with the Anti-Terrorism Act passed late in 2001. The group reportedly had discussed attacking several possible targets, including power plants, a Canadian military base, the Toronto Stock Exchange, and other prominent sites. The plan involved having some members of the group detonate truck bombs while another group reportedly would storm the parliament and capture hostages. Prime Minister Harper was said to have been a key target. Most of the suspects were in their teens or early 20s. All were either Canadian-born or had immigrated to the country at an early age. They had a variety of backgrounds; some were students, some held jobs, and some were unemployed. Many were from middle class backgrounds, and few of them had criminal records. Of the Toronto 18, seven admitted guilt and four were convicted. Charges against the other seven were stayed or dropped.⁵⁰

U.S. officials claimed that the arrests proved that Canada's law enforcement and intelligence services were doing an excellent job of ensuring security. An FBI spokesperson said there was "no imminent threat" to the United States stemming from the Toronto operation. However, some U.S. Members of Congress claimed that Canada maintains lax immigration and asylum policies, and that the arrests demonstrated that stricter controls over the U.S.-Canada border are in order. The incident prompted close consultations between U.S. and Canadian policymakers and law

⁴⁸ U.S. Government Accountability Office, *Border Security: DHS Progress and Challenges in securing the US Southwest and Northern Borders*, GAO-11-508T, March 30, 2011, p. 6, <http://www.gao.gov/new.items/d11508t.pdf>.

⁴⁹ For another brief overview of efforts to secure the U.S.-Canada border, see Joint Counter-Terrorism Initiatives. By Melissa Radford. Border Facilitation: Products and People. By June Dewetering. Both in *Canada and the United States: Shared Interests and Concerns*. Canadian Library of Parliament. January, 2009. http://www.parl.gc.ca/information/library/PRBpubs/prb0834_00-e.htm

⁵⁰ "Recent Terrorism-related Cases in Canada," January 24, 2011, <http://www.cbc.ca/news/canada/story/2011/01/21/f-terror-cases-quickfacts.html>

enforcement officials. The operation has not arisen as a domestic political issue in Canada, but it has renewed debate about Canada's immigration practices, its commitment to a multicultural environment, its security measures, and the presence of its troops in Afghanistan.⁵¹

In a late August 2010 sting operation known as Project Samosa, the RCMP and the Canadian Security and Intelligence Service (CSIS) seized bomb-making materials and arrested six men suspected of conspiring to commit acts of terrorism and to transfer funds to insurgents in Afghanistan. Authorities stated that the detainees, who were said to be mainly educated professionals, are believed to have received training in Afghanistan or Pakistan. One of the detainees was a contestant on the "Canadian Idol" television show in 2008.⁵² Three of the men were charged with conspiracy and other offenses; two of them have been released on bail.⁵³

Economic and Trade Issues

The Canadian economy experienced a shallower recession and has recovered faster than the United States. Canada officially exited the recession in the 1st quarter of 2010. After dropping by 2.8% in 2009, Canadian gross domestic product (GDP) grew by 3.2% in 2010, 2.5% in 2011 and the *Economist Intelligence Unit* and *IHS Global Insight* expect the economy to expand by 1.9% and 2.0%, respectively, in 2012.

In contrast to the United States, the Bank of Canada has raised interest rates three times—to a 1% target rate—to constrain demand. This interest rate, along with sustained commodity prices, led to the Canadian dollar flirting with parity with the U.S. dollar for much of 2010, and remaining above parity through the first eight months of 2011, dropping to a yearly low of \$0.94 on October 4, 2011 and gradually rising back towards parity in the first three months of 2012. The unemployment rate, which hit a generational low of 5.8% in January 2008, peaked at 8.7% in August 2009, and gradually fell back to 7.5% by the end of 2011.⁵⁴ Canada recorded its first current account (CA) deficit in nine years in the fourth quarter of 2008, and the collapse in trade due to the great recession led to a CA deficit of \$36 billion for 2009 as a whole. While the volume of trade recovered in 2010, the CA deficit remained at about \$40 billion, around 2.8% of GDP in 2011.

Budget Policy

While Canada is heavily dependent on the world economy, and thus easily affected by it, some Canadian policymakers believed that the country was in a relatively better position to ride out the economic downturn. After all, Canada had profited handsomely from the resources boom that only began to wind down in the summer of 2008. Also, Canadians were reassured by its

⁵¹ "Canada's Terror Sweep Grabs Spotlight in U.S." *Canadian Press*. June 3, 2006. "U.S. Praises Canada On Terror Arrests But Critics Blast Immigration Laws." *Canadian Press*. June 4, 2006. "Terrorists In Toronto: Is Canada Safe? Are We?" By Tanya Primiani and Christopher Sands. *CSIS Commentary*. Center for Strategic and International Studies. June 20, 2006. "The Toronto Terror Plot." *Economist*. June 10, 2006.

⁵² "Third Terror Suspect was Canadian Idol Contestant," *Toronto Star*, August 26, 2010; August 27, 2010. "Canada Arrests Show Affluence Is No Bar To Militancy," *Oxford Analytica*. August 27, 2010. "Few Details Given As 4 Canadians Are Held In Terrorist Plot," *New York Times*. August 28, 2010.

⁵³ "Recent Terrorism-related Cases in Canada," January 24, 2011, <http://www.cbc.ca/news/canada/story/2011/01/21/f-terror-cases-quickfacts.html>

⁵⁴ Economic data are from Economist Intelligence Unit, wire service reports, and Statistics Canada.

comparatively more regulated banking system, which was able to avoid the worst excesses of the U.S. financial meltdown. However, Canada could not long avoid the effects of the collapse of the U.S. housing market, the woes of the U.S. automotive sector, and the seizing up of credit markets worldwide. Canada entered into recession in the first quarter of 2009 and would not emerge from recession until a year later.

Canada's Stimulus Program

Following the reconvening of parliament in January 2009, the government introduced a C\$258.6 billion budget, which called for C\$40 billion in stimulus spending and tax cuts for FY2009-FY2011. The stimulus consisted of a package of income tax cuts, employment insurance (EI) benefit extensions, job retraining, 'hard' infrastructure spending, tax credits for home renovation, retrofits for social housing, and investments in First Nation's health programs.⁵⁵ In all, the C\$40 billion represents a stimulus of about 1.5% of GDP in the first year and 1.1% in the second year. Increased spending represents approximately 72% of this package and tax cuts contribute the remaining 28%. The March 2010 budget allocated the remaining C\$19 billion in stimulus.

The 2009 budget also marked a return to deficit spending for Canada after 12 successive budgets in balance or surplus. The 2009 budget contemplated a deficit of C\$34 billion the first year, and predicted a total of C\$81 billion in borrowing over five years before the budget was expected to return to surplus in 2013. The March 2010 budget revised upward the 2009 deficit to C\$53.8 billion, proposed a C\$49.2 billion deficit in 2010, and envisaged the budget returning to balance in 2015 with a total C\$158.4 billion increase in the national debt.

The return to deficit spending, while acknowledged as necessary by most of the political spectrum to combat the severe economic recession, was not undertaken lightly. Prior to the "austerity" budget of 1995, Canada had racked up 27 straight years of deficit spending. At its peak in 1996, Canada's public debt represented 101.6% of GDP, and government sector spending reached 53.6% of GDP in 1993. Realizing this course was unsustainable, the Liberal government of then Prime Minister Jean Chrétien and his Finance Minister Paul Martin embarked on a financial austerity plan using such politically risky measures as cutting federal funding for health and education transfers, applying a means test to those eligible for Seniors Benefits, and cuts in defense. A nationwide goods and services tax was introduced to help close the gap. Under this budget discipline, the government submitted a balanced budget in 1998 and a political consensus emerged not to resort to deficit spending, at least until 2009.

The March 2012 budget confirmed that the government's program of fiscal consolidation is underway. The budget intends to save approximately C\$5.2 billion on an annualized basis by 2014-2015 through:

- elimination of 19,200 public service positions (about 4.8% of the federal government),
- a 10% cut to the Canadian Broadcasting Corporation (CBC),
- increasing the eligibility of Old Age Security (OAS) from 65-67 to be phased in from 2023-2029,

⁵⁵ "Tories to Aggressively Implement Budget Spending Measures," *The Hill Times*, February 2, 2009.

- cuts to health care and public safety (RCMP and corrections), and
- elimination of the penny, among other initiatives.

The 2012 budget contemplates a C\$21.1 billion deficit for the current 2012-13 period with the deficit narrowing to C\$1.3 billion in 2014-15 and a return to surplus in 2015-16.⁵⁶

Energy

Canada is the United States' largest supplier of energy—including oil, uranium, natural gas, and electricity—and the energy relationship has been growing.⁵⁷ Canada is the world's fifth-largest petroleum producer, and its reserves are believed to be the third largest in the world only after those of Saudi Arabia and Venezuela; Canada's sources of oil include traditional and offshore wells and, increasingly, Alberta's oil sands.⁵⁸ In 2010, the value of U.S. petroleum and natural gas imports from Canada reached \$82.2 billion from \$63.7 billion in 2009. Canada provides 22% of U.S. crude oil imports and supplies 85% of U.S. natural gas imports.⁵⁹ Canada is particularly valued because it is considered a reliable source of energy, as it is not a member of OPEC. The two countries are also working on the development of pipeline construction projects. China has shown interest in Canada's oil sector, and has recently bought stakes in the Alberta's oil sands projects. Canada also a net exporter of electricity to the United States, and the North American electricity grid is closely interconnected.

Bilateral Trade Issues

The United States and Canada enjoy the largest bilateral commercial relationship in the world; total two-way cross-border trade amounted to over \$1.3 billion per day in 2010. Over the past twenty years, U.S.-Canada trade relations have been governed first by the 1989 U.S.-Canada Free Trade Agreement and, subsequently, by the 1994 North American Free Trade Agreement. These agreements, along with the conclusion of the Uruguay Round of multilateral trade negotiations and the creation of the World Trade Organization, contained mutual concessions on commercial trade barriers, and, more importantly perhaps, established binding dispute settlement mechanisms. While these agreements have resolved some of the sharp differences from the past, questions regarding the effectiveness of dispute resolution mechanism remain.

Meanwhile, several trade issues—some old, some new—have yet to be completely resolved. Many of these disputes involve long-running battles over agricultural commodities or natural resources, including softwood lumber and farm goods. Some analysts attribute the longevity of these conflicts to the inherent incompatibility of the two countries' different natural resource and agricultural programs, others to the political sensitivity of the commodities under negotiation.

⁵⁶ See Budget 2012 site, <http://www.budget.gc.ca/2012/home-accueil-eng.html>

⁵⁷ See CRS Report R41875, *The U.S.-Canada Energy Relationship: Joined at the Well*, by Paul W. Parfomak and Michael Ratner.

⁵⁸ U.S. Energy Information Administration (EIA), Country Analysis Brief: Canada, April 2011, <http://www.eia.gov/countries/cab.cfm?fips=CA>

⁵⁹ 2009 statistics from U.S. International Trade Commission <http://dataweb.usitc.gov>

Softwood Lumber

A 1996 agreement restricting Canadian lumber exports to the United States expired in March 2001. Shortly thereafter, the U.S. Commerce Department launched countervailing duty and anti-dumping investigations; in May 2002, the International Trade Commission (ITC) found that Canadian imports threatened to injure U.S. industry, and Commerce applied 27% (later reduced) duties on Canadian softwood. Canada challenged the agency decisions under NAFTA and in the WTO.

After several years of inconclusive and sometimes conflicting litigation, the two sides announced that they had struck a seven-year agreement on softwood on April 26, 2006 (the SLA). As part of a complicated formula, the United States will allow unlimited imports of Canadian timber when market prices remain above a specified level; when prices fall below that level, Canada will impose export taxes and/or quotas. In addition, the United States will return to Canada a large majority of the duties it had collected.⁶⁰

The implementation of the softwood lumber agreement has not been without controversy. As the depressed housing market has reduced demand for softwood lumber, the market price has been under the level (\$355 thousand board feet) in which export taxes must be charged. The United States and Canada resorted to arbitration over the use of adjustment mechanisms to calculate the quotas used for eastern Canadian lumber. The arbitral panel sided with the United States, and after Canada did not implement the panel's recommendation, the United States levied a 10% tariff on the affected lumber to recoup the compensation awarded by the arbitral panel in April 2009.

In January 2008, the United States also requested arbitration over six provincial forest sector assistance programs in Québec and Ontario, programs that the United States believes contravene the anti-circumvention provision of the SLA. In January 2011, the LCIA found certain of these programs breached the SLA, and Canada began imposing additional charges on lumber from Quebec and Ontario for the duration of the agreement.

The Obama Administration has also sought arbitration under the SLA over timber grading practices in British Columbia. They claim that the BC government has changed its classification procedures for timber and has been grading an increasing amount of its cut as salvage Grade 4 lumber. For its part, Canada attributes this increase to an infestation of mountain pine beetles and rejects the assertion that this policy represents a subsidy for Canadian producers. A panel was established in January 2011, although no determination has been made in this dispute.

Country of Origin Labeling

The 2002 Farm Bill required retailers to provide country-of-origin labeling (COOL) for fresh produce, red meats, seafood, and peanuts. The requirements for seafood were implemented on September 30, 2004, but COOL requirements for other products were delayed until September 30, 2008. The 2008 Farm Bill, The Food, Conservation, and Energy Act of 2008 (P.L. 110-246), reaffirmed this timetable and added goat meat, chicken, ginseng, pecans, and macadamia nuts as covered commodities. A final rule was issued on January 15, 2009, effective March 16, 2009. A

⁶⁰ "U.S. Gets a Lift In Lumber Fight With Canada." By Ian Austen and Clifford Krauss. *New York Times*. August 31, 2005. "Conservative Government Wins Softwood Truce." *Globe and Mail*. April 28, 2006.

WTO dispute settlement panel found that COOL violated the WTO's Technical Barriers to Trade Agreement in November 2011. The United States appealed that ruling on March 23, 2012.

Buy American Stimulus Provisions

The Buy American provision of the American Recovery and Reinvestment Act of 2009 (ARRA, §1605, P.L. 111-5) states that no funds shall be appropriated for building projects or public works projects unless all the iron, steel, and manufactured goods are made in the United States. This provision was subject to three discrete waivers: (1) applying this policy would not be in the public interest; (2) the iron, steel, or manufactured products are not produced in sufficient quantities or of a satisfactory quantity in the United States; or (3) the inclusion of the applicable U.S. products would increase the cost of the overall project by more than 25%. The Senate added language to ensure that the provisions are applied in a manner consistent with U.S. trade obligations.

With regard to Canada, the United States has undertaken government procurement obligations under the World Trade Organization's (WTO) Agreement on Government Procurement (AGP) and under the North American Free Trade Agreement (NAFTA). The AGP is a plurilateral agreement that only binds those WTO members that agreed to undertake obligations under it. Furthermore, the AGP only applies to the sectors and the procurement agencies that the national government (and sub-national government agencies) includes in its schedule of national commitments. NAFTA contains similar commitments on the national level, but excluded sub-national entities.

Both the United States and Canada have undertaken extensive obligations to open their government procurements at the national level under both agreements. However, because Canadian provinces never signed up to the AGP, as had 37 U.S. states, regulations implementing the ARRA excluded Canadian firms from bidding on ARRA-financed contracts that are tendered by the U.S. states.⁶¹ In February 2010, the United States agreed to permit Canadian firms to bid on sub-federal ARRA contracts in return for a Canadian commitment to sign its provinces up to the AGP, which it did by notice to the WTO on March 19, 2010. In addition, both parties committed themselves to begin negotiations reciprocally to expand commitments for market access in procurement between the two countries.⁶²

Intellectual Property Rights

In 2011, the U.S. Trade Representative again listed Canada on its Special 301 report on intellectual property rights protections to the priority watch list for intellectual property rights protections.⁶³ The priority watch list indicates that the listed trading partner has problems with respect to IPR protection, enforcement, or market access for persons relying on intellectual property and that these problems merit "increased bilateral attention." In this designation, Canada joins such notorious IPR violators as China and Russia. The United States again urged Canada to implement the World Intellectual Property Organization's Copyright treaty, which has been

⁶¹ Office of Management and Budget, "Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009, April 3, 2009. pp. 160-166.

⁶² "U.S.-Canada Announce Buy American Deal, Provinces to Sign GPA," *Inside U.S. Trade*, February 12, 2010.

⁶³ United States Trade Representative, 2011 Special 301 Report, p. 27. Available at http://www.ustr.gov/webfm_send/2841.

signed but not ratified by Canada.⁶⁴ The United States also expressed concern about trade in pirated and counterfeit goods in Canada, and urged greater enforcement and “deterrent-level” penalties for IPR infringement. The United States urged Canada to adopt tougher border security measures to crack down on this trade, including allowing for the seizure of pirated and counterfeit goods by customs agents without a court order. The government re-introduced the Copyright Modernization Act (C-11) in September 2011, and is pending debate in the House of Commons. This legislation was intended to bring Canadian copyright law into conformance with the WIPO Internet treaties and allow for some format shifting and fair-dealing (fair-use) exceptions, but would prohibit the circumvention of digital protection measures. It also would have clarified the rights and responsibilities of internet service providers for infringement of their subscribers.⁶⁵

Environmental Issues

The United States and Canada, which share a common border that stretches 5,500 miles, cooperate extensively on environmental matters. Since they signed the Boundary Waters Treaty in 1909, the two countries have, through the International Joint Commission, worked together on protecting and maintaining border waterways, especially the Great Lakes. In 1978, the two signed the Great Lakes Water Quality Agreement.

In 2002, Canada ratified the Kyoto Agreement; in 2006, however, the government announced that emission targets had been exceeded. The Harper government has established a goal of cutting greenhouse gas emissions 20% by 2020, mainly by increasing reliance on hydro- and nuclear power, and by increasing carbon abatement in the oil sands, but it has also declared that it would coordinate its greenhouse emission strategy with the United States. In December 2011, Canada announced that it was withdrawing from the Kyoto Protocol, after having declined to take on a second phase commitment in June 2011.

The long feud over Pacific salmon—one of the more prominent bilateral disputes in recent years—had both environmental and commercial aspects. Canada contended that American fishermen were taking more than their equitable share of the migratory fish; the United States, on the other hand, maintained that its fishing was in accordance with the 1985 Pacific Salmon Treaty (PST) and with sound conservation practices. After a pause, talks resumed in 1997, and the two sides finally reached an accord in 1999; both countries are monitoring implementation of the agreement.⁶⁶ The so-called Annex IV fisheries regimes of the PST were renegotiated in 2008.

One area of contention concerns the diversion of the naturally overflowing waters of Devils Lake, in North Dakota. For flood-control purposes, the state has constructed a channel that diverts excess water ultimately to the Red River, which flows northward. Manitobans have objected to this solution, arguing that the lake water contains toxic chemicals from agricultural runoff; they are also concerned that the introduction of alien species of aquatic life may disturb the ecological balance and endanger recreational fishing in Lake Winnipeg, into which the Red River empties. The Canadian government has requested that the case be referred to the International Joint Commission. In April 2006, after meetings between senior environmental officials of the two

⁶⁴ The WIPO Copyright treaty updates existing copyright protections for Internet and other electronic media.

⁶⁵ “Bill Would Update Canadian Copyright Act To Respect Needs of Digital Age, Official Says,” *International Trade Reporter*, June 10, 2010.

⁶⁶ CRS Report RL30234, *The Pacific Salmon Treaty: The 1999 Agreement and Renegotiated Annex IV*, by Eugene H. Buck.

governments, the United States agreed to install a permanent filtration system at the Devils Lake outlet. However, this filtration system, estimated to cost \$15 million, has not been installed. In February 2008, the North Dakota Supreme Court found that the state had acted improperly in changing certain environmental standards for the water released from the lake's outlet. At this time, the channel operates intermittently, subject to North Dakota health regulations. Meanwhile, Manitoba has offered to address the issue of a 30-mile border road that acts as a dike, trapping water in northeastern North Dakota, if North Dakota installs the filtration system at the Devils Lake Channel. North Dakota's governor demurred, maintaining that the two issues are unrelated.⁶⁷

Other environmental problems the two countries have dealt with in recent years include secondary wastewater treatment, control of predator fish and other invasive species introduced into the Great Lakes by ocean-going vessels, and sustainability of the St. Lawrence Seaway. In addition, the United States and Canada concluded a hazardous waste trade agreement in 1986; more recently, transboundary shipments of solid waste, particularly from Ontario to Ohio, Michigan, and other U.S. states, have been under review, and have been the subject of legislation in the U.S. Congress. The two countries have continued the long-standing debate over the ecological impact of possible development in Alaska's Arctic National Wildlife Refuge. Finally, the two sides continue to monitor the progress of the 1991 Canada-United States Air Quality Agreement. On January 7, 2003, Canadian and U.S. officials announced a new Joint Border Air Quality Strategy; under the initiative, pilot programs to reduce air pollution will be developed involving stakeholders at the state, provincial, and local levels.

Canada and Afghanistan⁶⁸

Issue Definition

Canada has participated in military operations in Afghanistan from the outset of the conflict in the fall of 2001. In early 2002, Ottawa deployed troops to Kandahar. However, as the mission changed focus from peacekeeping to counter-insurgency operations involving combat and casualties, Canadian public support declined. Parliament approved legislation requiring Canada to end its combat role by July 2011, and for all troops to be withdrawn by the end of that year. In the fall of 2009, a long-running scandal erupted when it was alleged that Canadian troops had turned over insurgent prisoners to Afghan officials, who subsequently tortured the detainees. The Obama Administration has expressed support for a continued role in Afghanistan by Canada. In late 2010, the Canadian government announced that, among other measures, it would maintain a sizeable military training contingent in Afghanistan through 2014.

⁶⁷ "Devil Down South." *The Economist*. July 16, 2005. "Little-Known White House Office Negotiates Devils Lake Dispute." *AP*. September 5, 2005. "U.S. Promises Devils Lake Filter, But Water May Flow Before Installation." *Canadian Press*. April 25, 2006. Manitoba Scores Partial victory In Water Dispute With North Dakota. *The Canadian Press*. February 22, 2008; "ND governor to Manitoba: No deal on water dispute," *Fargo Forum*, May 8, 2009.

⁶⁸ Prepared by Carl Ek, Specialist in International Relations; Foreign Affairs, Defense, and Trade Division.

Background and Analysis

Canada was one of the first countries to join the U.S.-led military operation in Afghanistan. In October 2001, the Canadian government launched Operation Apollo, in support of Operation Enduring Freedom. Nearly 900 infantry troops and approximately 40 members of Canada's Special Forces unit, Joint Task Force 2, served in the initial combat in Afghanistan. Canadian forces—about 2,800 during most of their deployment—served on the front line in combat operations in southern Afghanistan to counter attacks by al Qaeda and Taliban fighters. It was the fifth-largest national contingent. Canadian troops operated without national combat operational restrictions (“caveats”). Canada has suffered among the heaviest casualties proportionally of the NATO coalition member states; a total of 158 Canadians, including one diplomat, have been killed in Afghanistan.

In addition to infantry troops, Canada contributed a helicopter squadron and Operational Mentor and Liaison Team (OMLT) trainers; in addition, Royal Canadian Mounted Police have assisted the Afghan National Police. In August 2005, Canada established a Provincial Reconstruction Team in Kandahar in the volatile southern part of the country. Ottawa also has provided humanitarian and reconstruction assistance to Afghanistan, which is the number one recipient of Canadian foreign aid. Canada is among the top five donors to the country, and pledged C\$1.9 billion (about \$1.9 billion) through 2011 in reconstruction and development assistance. Canada also shared the leadership of Regional Command-South with the Netherlands and the UK.

As Canadian military operations in Afghanistan shifted from peacekeeping to counter-insurgency, public support for Canada's presence diminished. However, Prime Minister Harper was willing to challenge public opinion over Canada's participation in Afghanistan; he relied upon an approach that emphasized training Afghan troops to replace departing Canadians. In 2006, he won a narrow vote in parliament to keep Canadian troops in Afghanistan for two additional years. Harper initially characterized the mission as humanitarian in nature and also asserted that it was in Canada's national interest to demonstrate its ability to play a leadership role internationally.

In the fall of 2007, Harper appointed an advisory panel to review options on the mission. The commission found that the troop presence was justifiable and that the mission should be maintained until 2011, but recommended that Canadian forces be withdrawn unless NATO allies stepped up their contributions. This became the basis of a compromise between the Liberals and Conservatives. Harper declared that Canadian troops would be withdrawn unless other NATO countries provided an additional 1,000 troops. At the April 2008 NATO summit in Bucharest, France and the United States announced that they would commit 800 additional troops.

Canada's Afghanistan mission was thrown into the national spotlight in November 2009, when a Foreign Ministry whistleblower publicly alleged that, in 2006 and 2007, Canadian forces had turned combatant prisoners over to local Afghan authorities, who subsequently tortured the detainees; Foreign Affairs Minister Peter MacKay and other officials denied the charges, but later backtracked somewhat. The controversy, which generated considerable public interest, continued into mid-2010.

In November 2010, Canada's Ministers of Foreign Affairs, Defense, and International Cooperation announced that the Afghan mission would be extended until 2014. They outlined a new role for Canada to help promote security, stability, and self-sufficiency in Afghanistan, and stated that it would focus on four areas: education and health of children and youth; promoting security and rule of law; supporting regional diplomacy; and providing humanitarian assistance.

Toward that end, the ministers said that up to 950 Canadian troops would be provided to help train the Afghan National Army, and up to 45 Canadian civilian law enforcement officers to help develop Afghan police forces. The ministers declared that the estimated cost of these various initiatives from 2011-2014 would be approximately C\$700 million.

Status of the Issue

In March 2010, U.S. Secretary of State Hillary Clinton said during a visit to Ottawa that she hoped Canada would continue its presence in Afghanistan after 2011, suggesting “a training role instead of a combat role, a logistics-support role instead of front-line combat.” Some observers noted that the Obama Administration and NATO officials had privately expressed concerns that the withdrawal of Canadian troops might prompt other allies to bring their troops home. As noted above, Canada ended its combat role there in July 2011, however, Canadian troops (510 as of January 2012) will remain until 2014 to help train Afghan national security forces. In December 2011, it was reported that Canadian Foreign Affairs Minister John Baird said that Canada would provide C\$100 million per year to Afghanistan between 2011 and 2014.

Questions

1. Please describe Canada’s new role in Afghanistan. Will Canadian military trainers be accompanying Afghan troops on patrols? If so, under what rules of engagement will the Canadian troops operate?
2. Do you believe that Canada’s decision to extend its mission in Afghanistan has influenced the policies of other allies?

Canada’s Arctic Sovereignty Claim⁶⁹

Issue Definition

Scientists have forecast that, by 2030 or earlier, global warming will reduce the Arctic ice pack in Canada’s northern archipelago sufficiently to create a “northwest passage” that will permit commercial ship traffic through the summer months. If created, a northwest passage would significantly reduce transit distances for commercial ships operating between certain ports. It could also be used by commercial fishing or cruise ships, ships supporting Arctic scientific research or resource exploration, or military vessels. The presence of ships in the passage could require the establishment and enforcement of shipping lanes and other rules for ensuring safe ship operations, add to existing demands for maritime search and rescue capabilities, and create a risk of environmental damage to the Arctic. The use of the passage by foreign military ships might be viewed as creating potential security risks to Canada (and the United States). Successive Canadian governments have maintained that such a passage would be an inland waterway, and would therefore be sovereign Canadian territory, subject to Ottawa’s surveillance and regulation. The United States, the European Union, Japan, and others assert that the passage would constitute an international strait between two high seas.

⁶⁹ Prepared by Carl Ek, Specialist in International Relations; Foreign Affairs, Defense, and Trade Division.

Background and Analysis

Arctic sovereignty has been an issue for Canada for decades. In 1985, a U.S. icebreaker, the *Polar Sea*, caused an uproar in Canada when it traversed the waters of the northern archipelago without first seeking permission. Afterward, Washington and Ottawa came to an agreement in 1988 under which the United States pledged to notify Canada when its ships would transit the region, and Canada agreed to grant its consent. In recent years, however, the question over who, if anyone, would have control over the regional waters has intensified as scientific consensus has grown that the melting of the polar icecap will open up a Northwest Passage during the summer months.

The debate over the Northwest Passage has commercial, environmental, and security considerations. The opening of a channel of water during the summer months through Canada's 36,000-island arctic archipelago would cut shipping routes between Europe and Asia by 3,000-4,000 miles, saving time and fuel costs. However, many Canadians are concerned that unfettered maritime traffic through the region could result in serious environmental hazards ranging from the catastrophe of an oil spill to more cumulative pollution caused by ocean dumping of ballast and garbage by transiting vessels. In terms of security, the Canadians are concerned that recognition of the passage as international waters would result in free access to naval warships and submarines, including, for example, those of Russia and China.

Canada seeks recognition of its sovereignty over the entire area, among other reasons, because of a strong national identification with its northern regions. Ottawa argues that it has a historical claim based on centuries of Inuit inhabitation—of the islands and of the ice extending from them. From a practical standpoint, Canada wishes to have the ability to enforce protection of the fragile arctic ecosystem and to ensure sustainable commercial fishing practices. In addition, the Canadians want there to be no doubt that they have rights to the region's abundant natural resources, including oil, natural gas, minerals, and precious metals.

The Harper government has been seeking to bolster Canada's sovereignty claim by maintaining and expanding the "Northern Strategy" launched by his Liberal predecessors. The most visible part of Conservatives' plan has been the establishment of a stronger military presence. In July 2007, Harper announced plans for the construction of 6-8 armed, medium-sized icebreakers to patrol the north. The following month, he traveled to Resolute Bay, Nunavut, and announced plans to construct a winter warfare training center and deep-water port in the region. He declared that "Canada's new government understands that the first principle of Arctic sovereignty is: Use it or lose it." Some Canadians, however, have criticized Harper for seeking to militarize the debate.

The prospective passage raises jurisdictional questions. Canadians maintain that it would be an internal waterway and would likely require all vessels to register with their coast guard's vessel traffic reporting system. They contend that this would facilitate possible search-and-rescue missions, and would dissuade ships bearing contraband from sailing through the region. There is general agreement that the natural resources in the region are Canadian; the debate concerns free transit rights. Analysts note that the U.N. Convention on the Law of the Seas calls for the right of transit passage "between one part of the high seas ... and another part of the high seas." In addition, some analysts believe that the recognition of the Northwest Passage as a Canadian inland waterway would set an international precedent that might be viewed as applicable elsewhere in the world. Other governments could echo Canada's sovereignty claim and prohibit the passage of U.S. naval ships, as well as of oil tankers bound for the United States; the Straits of Malacca and Hormuz have been cited as examples. Others, however, such as former U.S.

Ambassador to Canada Paul Cellucci, argue that it would be in the interests of U.S. national security if Canada were to manage and police shipping through the straits.

Several possible solutions have been put forward. Some argue that Canada could achieve its objectives through regulations approved by the U.N. International Maritime Organization. Also, it has suggested that NORAD and the Arctic Council might be able to coordinate cooperative patrolling of the passage. Others—though not the United States—have proposed that the countries bordering the Arctic adopt an agreement prohibiting military, residential, or commercial use of the region, as was done for Antarctica in 1959. Finally, some believe that a renewed and updated version of the 1988 U.S.-Canada agreement would suffice.

Status of the Issue

On January 9, 2009, the outgoing Bush White House issued National Security Presidential Directive 66, entitled Arctic Region Policy. The document reiterated the Administration's stance regarding Canada's sovereignty claim, stating that "the Northwest Passage is a strait used for international navigation." The Obama Administration is currently operating under the policy directive. For the time being, Ottawa and Washington will continue to "agree to disagree." However, Canadian analysts have argued that the debate over who should manage the straits will intensify if ships carrying hazardous materials or illegal immigrants are discovered in the region. In mid-2011, Foreign Minister Lawrence Cannon announced a new "Statement on Canada's Arctic Policy," which reaffirmed the government's commitment to Canada's sovereignty, to economic and social development, to environmental protection, and to empowerment of the peoples of the region. The statement also emphasized the government's intention to negotiate settlements to long-standing boundary disputes with the United States and Denmark. The government has emphasized its commitment to the Arctic through frequent visits by government officials; Prime Minister Harper made his sixth annual trip to the north in August 2011. Because it has been highlighted as a priority area for the Harper government, this issue will likely continue to be the subject of bilateral discussions between U.S. and Canadian policymakers.

Questions

1. Several governments have taken issue with Canada's assertion of sovereignty over the Arctic waters. Do any foreign countries support Canada on this question? Has the Canadian government offered a legal precedent for its claim?
2. If Canada were to win recognition of its sovereignty over the passage, how might it regulate shipping traffic through the straits?
3. What might be the security, economic and environmental consequences for the United States if Canada were to win its sovereignty claim? If the passage were to be declared international waters?

Inter-American Cooperation⁷⁰

Issue Definition

In 2007, Prime Minister Harper declared that the Americas are a critical foreign policy priority for Canada, and committed to deepening and broadening Canada's engagement in the region. Since then, Canada has sought to expand its presence throughout the region while reinforcing bilateral ties and strengthening regional organizations. The Conservative government's current objectives for the hemisphere closely align with those of the Obama Administration, with both countries advancing policies designed to reinforce democratic governance, increase economic prosperity, and enhance regional stability and security.

Background and Analysis

Although Canada has long been active in the region, its commitment to sustained engagement in inter-American relations is relatively recent. Throughout the 20th century, Canada forged strong diplomatic and commercial ties with many Latin American and Caribbean countries. Nevertheless, it generally did not consider the region to be a top foreign policy priority. Authoritarian governance and widespread poverty fueled negative perceptions of the region and led Canada to focus its attention elsewhere. According to a number of analysts and former officials, Canada was also reluctant to engage extensively in hemispheric affairs out of concern that it could be drawn into disputes with the United States, which had traditionally played a dominant role in the region.

Canada began to reexamine its role within the Western Hemisphere as the Cold War drew to a close and Latin American and Caribbean countries opened their markets and reestablished democratic governance. In 1989, the Progressive Conservative government of Brian Mulroney (1984-1993) completed a full cabinet review of Canada's position in the hemisphere and declared that inter-American cooperation was integral to its interests. Canada became a full member of the Organization of American States (OAS) in 1990, where it has been a leader in democracy promotion efforts and one of the drivers of the Summits of the Americas process. Canada also sought to expand commercial ties in the region by pursuing trade liberalization. In 1994, Canada entered the North American Free Trade Agreement (NAFTA) with Mexico and the United States, and participated in the initiation of negotiations over a hemispheric Free Trade Area of the Americas (FTAA). Although the FTAA negotiations were effectively abandoned in 2005, Canada continued to pursue bilateral trade agreements with many countries in the region.

Since taking office in 2006, Prime Minister Harper has sought to reinvigorate Canada's engagement in the hemisphere. He created a new Minister of State of Foreign Affairs position with special responsibility for the Americas. He also placed a renewed emphasis on trade, signing agreements with Colombia, Honduras, Panama, and Peru, and pursuing negotiations with several other nations. Within the OAS, Canada continues to support efforts to strengthen democratic governance. It also is encouraging the organization to better define its priorities and become more effective and accountable. Additionally, Canada has provided substantial amounts of assistance to support security and economic and political development efforts in the region. In fiscal year

⁷⁰ Prepared by Peter J. Meyer, Analyst in Latin American Affairs; Foreign Affairs, Defense, and Trade Division.

2009-2010, Canada provided over C\$807 million (about U.S.\$811 million) in bilateral and multilateral aid to Latin America and the Caribbean. Selected issues in Canada's hemispheric relations are discussed below.

Organization of American States

Although Canada remained outside of the OAS for many years, it became a permanent observer in 1972 and a full member in 1990. Canada is currently the second-largest financial contributor to the OAS after the United States. In 2011, Canada had an assessed contribution of U.S.\$11.3 million, and provided an additional U.S.\$10.8 million in voluntary contributions to support activities such as electoral observation missions and the special OAS missions in Haiti and Colombia. The Harper government's emphasis on effective, results-oriented multilateralism has led it to support efforts to improve the organization's governance. Canada is providing funding to introduce results-based management at the OAS, and chairs a working group seeking to improve the priority-setting process and accountability of the organization. It also is working with the OAS to improve aid effectiveness in the hemisphere, supporting donor coordination efforts and chairing a working group to strengthen the Inter-American Committee for Integral Development.

Since becoming a full member of the OAS, Canada has taken a particular interest in advancing democratic governance in the hemisphere. One of its first initiatives was to create the Unit for the Promotion of Democracy, which focused on strengthening democratic institutions and observing elections. Canada was also instrumental in the drafting of the Inter-American Democratic Charter, a document signed by all 34 participating member states asserting that all peoples of the Americas have a right to democracy and their governments have an obligation to promote and defend it. Canada joined with the rest of the member states in voting to invoke the charter and suspend Honduras from the OAS following the June 2009 ouster of that country's president. After Honduras held elections in November 2009, Canada quickly recognized the new government and pushed to end the OAS suspension, which was ultimately lifted in June 2011.

Haiti

Although Canada has few historic ties to Haiti, it has worked closely with the United States and Latin American and Caribbean partners to support stability and development efforts in the country over the past 17 years. As part of a U.N. mission in 1994, a contingent of the Canadian armed forces and members of the Royal Canadian Mounted Police assumed control from departing U.S. forces who had helped restore the democratically elected government of Jean-Bertrand Aristide. In 2004, after the Aristide government stepped down in the face of armed rebellion, Canada joined the United States and other partners in providing peacekeepers to the U.N.-authorized Multinational Interim Force (MIF). Canada initially deployed nearly 500 troops to the MIF, and has continued to participate in the Brazilian-led U.N. Stabilization Mission in Haiti (MINUSTAH). Following the January 2010 earthquake that devastated Haiti, Canada temporarily dispatched over 2,000 armed forces personnel to assist in security and humanitarian relief efforts. It currently has 131 police and military personnel serving in MINUSTAH.

In addition to assisting in security efforts, Canada has sought to foster development in Haiti. Haiti receives over 41% of Canada's aid to Latin America and the Caribbean, and was the largest recipient of Canada's international assistance world-wide in fiscal year 2009-2010. Canada is a member of the Interim Haiti Recovery Commission and has provided over C\$1 billion (about U.S.\$1.005 billion) in aid to Haiti since 2006, including an estimated \$252.9 million (about U.S.

\$254 million) in fiscal year 2010-2011. The country's assistance to Haiti is concentrated in three areas: increasing food security, securing the future of children and youth, and stimulating sustainable economic growth. Canada has also been a leader in debt relief efforts. It forgave C\$2.3 million (about U.S.\$2.31 million) in loans to Haiti in September 2009, and was one of the first countries to call on the international community to forgive Haiti's debts in the aftermath of the earthquake. In June 2010, Canada paid off C\$33 million (about U.S.\$33.1 million) in Haitian debt to the international financial institutions, becoming the first of the G20 countries to fulfill its pledge and pay off its share of Haiti's debt.

Status of the Issue

Despite Prime Minister Harper's efforts to boost engagement with the countries of Latin America and the Caribbean, Canada's presence and influence in the region remains limited. Total two-way trade between Canada and the region increased over 67% between 2006 and 2011 to U.S.\$57.7 billion. This represents a small portion of Canada's global trade relations, however, as Latin American and Caribbean countries are the destination of only 3% of Canada's exports. Similarly, while Canada's total aid to the region is substantial, it is heavily concentrated in Haiti and a few Andean and Central American nations. In 2011, the principal Canadian think-tank that focused on hemispheric affairs—the Canadian Foundation for the Americas (FOCAL)—shut down due to lack of funding. An internal evaluation of Prime Minister Harper's Americas strategy that was released in 2011 by the inspector general of the Canadian Foreign Affairs Department found that Canada's influence with individual nations in the region is uncertain, as high-level visits and announcements have raised hopes but concrete action has been slow. The evaluation also noted that the strategy lacked direction, coordination, and funding. Prime Minister Harper reportedly intends to reinvigorate his government's Americas strategy at the Sixth Summit of the Americas, scheduled to be held in Cartagena, Colombia on April 14-15, 2012. The revised strategy is expected to place a larger emphasis on economic prosperity through trade.

Questions

1. How have Canada's relations in the hemisphere changed as a result of Prime Minister Harper's Americas strategy? What are the primary objectives of the strategy? What do you consider to be the strategy's major successes thus far?
2. How would you assess the current direction of the OAS? How are Canada's reform efforts within the organization proceeding? What outcomes do you expect from the Sixth Summit of the Americas?
3. Canada has committed substantial personnel and resources to Haiti over many years. What is your assessment of the reconstruction efforts since the earthquake? How well are the efforts of international donors and the Haitian government being coordinated? What progress has been made in the reform and rebuilding of Haiti's educational system, for which Canada has taken on a leadership role among donors? What do you foresee as Canada's level of involvement in Haiti in the coming years?

Border Security Issues⁷¹

Issue Definition

Border security has emerged as an area of public concern, particularly since the September 11, 2001 terrorist attacks. The United States and Canada attempt to balance adequate border security with the facilitation of legitimate cross-border travel and commerce. In the wake of statutory and administrative steps to enhance border security, concerns persist with respect to the potential for terrorists and criminals to exploit the border and about the adequateness of infrastructure and personnel at the U.S.-Canadian border and ports of entry.

Background and Analysis

The U.S.-Canadian border between Washington State and Maine spans about 4,000 miles, includes vastly different types of terrain, and is the site of about 150 ports of entry, including 20 major land ports. In 2010, northern border ports admitted 5.4 million trucks, 26,000 trains, 116,000 busses, and 28.9 million passenger vehicles according to the U.S. Bureau of Transportation Statistics—numbers which exceed analogous data for the U.S.-Mexican border for trucks and trains, while passenger traffic is higher on the southern border.

Border Infrastructure and Personnel

A series of laws since 2001 have increased the number of enforcement personnel at the U.S.-Canadian border and strengthened border screening technology. The USA PATRIOT Act of 2002 (P.L. 107-56) authorized the Attorney General to triple the number of border patrol personnel and immigration inspectors along the northern border and authorized additional technological improvements and equipment. The Enhanced Border Security and Visa Reform Act of 2002 (P.L. 107-173) similarly authorized additional personnel, technology, and infrastructure improvements. The Trade Act of 2002 (P.L. 107-210) required 285 additional customs inspectors for the northern border in FY2003. And the Intelligence Reform and Terrorism Prevention Act of 2004 (IRTPA, P.L. 108-458) authorized an increase of 2,000 border patrol agents per year for FY2006-FY2010, while stipulating that 20% of the increases in agent manpower be assigned to the northern border.

A total of 2,237 border patrol agents were posted in northern border sectors in FY2011, up from 340 in FY2001, along with 3,706 U.S. Customs and Border Protection (CBP) inspectors at ports of entry, up from 1,550 in FY2001. These increased deployments represent substantial growth in border enforcement personnel, but lag slightly behind the goals established by the USA-PATRIOT Act and the IRTPA. Some Members of Congress have raised concerns about staffing levels at the northern border.

Western Hemisphere Travel Initiative

The IRTPA also required the Secretary of Homeland Security, in consultation with the Secretary of State, to develop and implement a plan to require all travelers (i.e., including American and

⁷¹ Prepared by Marc R. Rosenblum, Specialist in Immigration Policy, Domestic Social Policy Division.

Canadian nationals) to use a passport or other secure document when entering the United States. Under WHTI rules in effect since June 1, 2009, travelers no longer may use driver's licenses and birth certificates as proof of identity and citizenship at the border. Approved documents include passport books, passport cards, and trusted traveler cards (such as Secure Electronic Network for Travelers Rapid Inspection, NEXUS, and the Fast and Secure Trade programs), as well as additional documents for military personnel and certain other special groups. Four states (Michigan, New York, Vermont, and Washington) and four Canadian provinces (British Columbia, Manitoba, Ontario, and Québec) issue enhanced driver's licenses that are also valid for WHTI purposes.

Prior to its implementation, WHTI fostered concern in both countries that the increased documentation requirements could suppress U.S.-Canadian travel, but no such effect has been observed. A Government Accountability Office (GAO) review in March 2011 found CBP's outreach campaign had led to a greater than 95% compliance rate with WHTI requirements in FY2010. And an October 2011 GAO report singled out WHTI technology that facilitates inspections at land borders as one of seven government-wide "successful major acquisitions."

U.S.-Canadian Collaboration

The United States and Canada have a long history of collaboration around border security. Such efforts date to February 24, 1995, when the two countries signed a joint accord, *Our Shared Border*, followed by the 1999 *Canada-U.S. Partnership Forum (CUSP)*. Shortly after the 9/11 attacks, the United States and Canada signed a joint statement of cooperation on border security and migration that focused on the detection and prosecution of security threats, the disruption of illegal migration, and the efficient management of legitimate travel. The agreement produced a 30-point plan (later updated to 32 points) commonly referred to as the "Smart Border Accord," signed on December 12, 2001. The points include coordinated law enforcement, intelligence sharing, infrastructure improvements, compatible immigration databases, visa policy coordination, biometric identifiers in travel documents, prescreening of air passengers, joint screening for high risk travelers, and improved processing of refugee and asylum claims, among other things. In July 2010, the countries signed an Action Plan for Critical Infrastructure intended to strengthen the safety, security, and resilience of critical shared infrastructure.

Three collaborative law enforcement programs exist along the U.S.-Canadian border. As part of the Smart Border Accord, the countries have established 15 Integrated Border Enforcement Teams (IBET), operating at 24 border locations. The IBETs are binational, multi-agency, enforcement teams jointly led by U.S. Customs and Immigration Enforcement (ICE) and the Royal Canadian Mounted Police (RCMP). IBETs share intelligence to identify, investigate, and interdict common national security threats and transnational criminal activity.

Second, beginning in 2007, ICE also operates four Border Enforcement Security Task Forces (BEST) in Blaine, WA; Detroit, MI; Buffalo, NY; and Massena, NY. The BEST program also emphasizes information sharing to combat cross-border crime, and brings in a larger number of federal, state, provincial, local, and tribal stakeholders from both sides of the border, all under ICE leadership.

Third, since 2005, the countries have operated a pilot program called Shiprider, which places fully cross-trained, cross-designated RCMP and U.S. Coast Guard agents on law enforcement vessels operating along certain international waterways. Agents from each country conduct joint enforcement activities on both sides of the border. The Obama and Harper Administrations signed

an agreement in 2009 to extend and expand Shiprider, but implementation of the agreement awaits authorizing legislation in the Canadian Parliament; and it may be superseded by the *Beyond the Border* agreement, discussed below.

In addition to these programs, the U.S.-Canada Cross Border Crime Forum, which includes the Secretary of Homeland Security, the Attorney General, and the Canadian Ministers of Public Safety and Justice, provides a regular meeting place for the top law enforcement officials from both countries to discuss cross-border criminal activity and to coordinate their responses.

Beyond the Border Agreement and Action Plan

On February 4, 2011, President Obama and Prime Minister Harper signed a joint declaration describing their shared visions for a common approach to perimeter security and economic competitiveness: the *Beyond the Border* agreement. The agreement describes four key areas of cooperation, including efforts to identify and address threats before they reach the U.S.-Canadian perimeter, trade facilitation, integrated cross-border law enforcement, and critical infrastructure and cybersecurity.

On December 7, 2011, President Obama and Prime Minister Harper released the *Beyond the Border Action Plan*, which includes a series of concrete steps to be taken within each of these areas, along with deadlines and metrics for measuring progress toward each goal. The plan is most ambitious with respect to trade facilitation, calling for a harmonized approach to cargo screening under the principle of “cleared one, accepted twice.” Additional provisions related to border security include, among others: plans for joint inventories and gap analyses for intelligence work related to travel and trade threat assessments (due by September 2012) and to border surveillance (October 2012), automated biographic (2013) and biometric (2014) data sharing to verify the identity of travelers and to share risk assessments and watchlist information, an integrated entry-exist system so that the record of a land entry into one country can be used to establish an exit record from the other (pilot program September 2012; full implementation June 2014), broader pre-clearance programs for goods and travelers (pilot programs December 2012), and the expansion of integrated law enforcement efforts including interoperable radio systems (2012) and the deployment of cross-designated officers to four additional Shiprider teams and to inland locations (between 2012 and 2016).

Status of the Issue

The *Beyond the Border Action Plan* lays out an ambitious agenda for deeper cooperation. The countries have expanded the NEXUS trusted traveler program to 19 border crossing locations, 33 marine reporting locations, and 8 Canadian pre-clearance locations. Since 2004, they have taken steps to share passenger information on high-risk travelers en route to either country through a joint risk-scoring scheme and shared “lookout” data. How the countries will implement additional steps identified in the *Beyond the Border Action Plan*, such as more deeply integrated cross-border law enforcement efforts, widespread cargo and passenger pre-clearance, and an integrated biometric entry-exit system, remains to be seen.

CBP and other observers still consider the U.S.-Canadian border to be the locus of a wide range of security threats, including transnational terrorist entities present along both sides of the U.S.-Canadian border; criminal enterprises focused on illegal drugs, firearms, tobacco, intellectual property, and currency; and vulnerabilities related to migration, agriculture, and transnational

health issues. Based on CBP's current measure for assessing border security—which is in the process of being replaced—the agency considered only 69 of the nearly 4,000 miles of the U.S.-Canadian border to be under an acceptable level of control, according to a 2010 GAO report.

Questions

1. A number of different technologies, including the U.S. Visitor and Immigrant Status Indicator Technology (US-VISIT) entry-exit program, have been implemented at northern ports of entry in recent years. With the advent of these technologies and the WHTI, the demand for improved screening and passenger processing infrastructure is critical. What measures has the Canadian government taken to enhance border infrastructure? Are there additional collaborative efforts that could alleviate some of the pressure on busy ports of entry? How can the United States and Canada make progress on an integrated entry-exit system?
2. The Beyond the Border agreement calls on the two countries to develop a common security perimeter and to move customs inspection activities away from the border under the principle of “cleared once, accepted twice.” Such an approach currently is limited mainly to Canadian airports. What is the Canadian government doing to facilitate pre-clearance and pre-inspections for travel through land ports? What safeguards will be in place to protect the integrity of pre-cleared truck shipments? How will common perimeter programs address differences between U.S. and Canadian attitudes about privacy protections and civil liberties and in how the countries define certain criminal offenses?
3. When will authorizing legislation be considered that would allow full implementation of the Shiprider Agreement governing full cross-designation of law enforcement officers? What are the prospects for expanding the program to include integrated land-based law enforcement programs?

Border Security: Trade and Commercial Concerns⁷²

Issue Definition

The aftermath of the terrorist attacks on the United States on September 11, 2001, increased scrutiny of the Canadian border as a possible point of entry for terrorists or for weapons of mass destruction. The potential for economic disruption that closing the border would cause has spurred cooperation between the United States and Canada to improve border security in an atmosphere conducive to continued and expanded commerce. This brief details commercial considerations in U.S.-Canadian border security discussions.

Background and Analysis

The issue of border security is linked to the increased integration of the United States and Canadian economies. This integration has been aided by several trade agreements, culminating in the North American Free Trade Agreement of 1994 (NAFTA). These trade agreements not only

⁷² Prepared by Ian F. Fergusson, Specialist in International Trade and Finance, Foreign Affairs, Defense, and Trade Division.

eliminated tariff barriers between the two nations, but also reoriented Canada's industrial structure towards the United States. Industries in each country are now able to produce goods for a larger continent-wide market, and productivity has increased through increased economies of scale and specialization. Such specialization led to increased bilateral trade, much of it in intermediate products. This integration has, in turn, led to industrial practices such as "just in time" parts procurement that depend on a relatively open border.

The volume of economic activity across the border underscores the extent of economic integration between the United States and Canada. With the U.S. and Canadian economies recovering from the global economic downturn, the two nations continue to have the largest trading relationship in the world with over \$1.5 billion per day in goods and services crossing the border in 2011. In that year, Canada purchased 19.0% of U.S. exports and supplied 14.3% of all U.S. imports. The United States supplied 49.5% of Canada's imports of goods in 2011 and purchased 73.7% of Canada's merchandise exports; two-way trade with the United States represented 40.2% of Canadian GDP. In 2010, the Ambassador Bridge and Detroit-Windsor Tunnel complex that links Detroit, Michigan and Windsor, Ontario was the largest trade link in the world with more than 3,340 daily truck crossings with cargo valued at more than \$91.7 billion per year.

Action Programs and Initiatives

Several initiatives to increase security of the border without impeding the flow of commerce were implemented under the Security and Prosperity Partnership (SPP), which in turn expanded on previous bilateral efforts by the United States and Canada, including the Smart Border Action Plan of December 2001 consisting of four pillars: the secure flow of people, the secure flow of goods, a secure infrastructure, and coordinated enforcement and information sharing. The pillar concerned with the flow of goods consists of initiatives on harmonized commercial processing, supply chain management, clearance away from the border, joint or shared facilities, enhancement of information sharing, and infrastructure improvements.

The U.S. Bureau of Customs and Border Protection's *Customs-Trade Partnership Against Terrorism (C-TPAT)* and the Canadian Border Security Agency's *Partners in Protection Program* are supply-chain security initiatives in which companies undertake audit-based compliance measures to enhance security along the supply chain. Goods shipped under these programs are eligible for preclearance away from the border.

The *Free and Secure Trade (FAST)* is a joint harmonized commercial processing initiative at 21 border locations, which provides for dedicated inspection lanes to goods carried by approved lower-risk shippers, to goods purchased from pre-authorized importers such as C-TPAT, and to goods transported by pre-authorized drivers and carriers. A complementary program (NEXUS) to expedite the secure movement of people has also been established for frequent travelers who have undergone security clearances on both sides of the border.

Another objective of the border security efforts has been the screening of goods entering North America. The ongoing U.S. *Container Security Initiative (CSI)* is designed to pre-screen high risk containers entering the United States at overseas ports of departure. Under the SPP, the three countries will develop common screening methods and technology, establish criteria to identify high risk cargo, and harmonize cargo information technology. Preclearance and prescreening is a possible first step in the creation of a North American security perimeter, a concept whereby clearance occurs at the first point of entrance rather than at the final border.

President Obama and Prime Minister Harper signed the Beyond the Border declaration on February 4, 2011, committing both nations to a shared vision of perimeter security and economic competitiveness. On December 7, 2011, the two leaders announced the Beyond the Border Action Plan (See also, Border Security Issues, above). Regarding trade facilitation and trans-border commerce, the Action Plan has identified such issues as providing a “single window” for submitting customs and other regulatory information, harmonizing the low value shipment process to enhance supply chain connectivity, and increasing the transparency of existing border fees. Additionally, the February 2011 declaration created the Regulatory Cooperation Council to increase regulatory cooperation to ensure the simplicity, transparency, and compatibility of regulations where possible to promote commerce and eliminate barrier to trade between the two nations. The December statement announced that initial work would be focused on regulations concerning agriculture and food, transportation, health, personal care products, workplace chemicals and the environment.

Status of the Issue

Land preclearance away from the border by U.S. and Canadian customs agents working in each other’s territory is an issue that has proven controversial, primarily due to concerns about sovereignty. Joint U.S.-Canada customs teams already operate in the CSI ports of Halifax, Montreal, and Vancouver, as well as Newark and Seattle-Tacoma, although the visiting agent serves only an advisory role with no enforcement powers. The SPP called for negotiations on a U.S.-Canada preclearance agreement with implementation of two pilot sites, the Peace Bridge (Buffalo, NY-Fort Erie, ON) and the Thousand Islands Bridge (Alexandria Bay, NY-Landsdowne, ON). However, these negotiations were suspended on April 26, 2007. A 2008 GAO report cited disagreements over arrest authority, fingerprinting practices, and the right of individuals to withdraw an application to enter the United States while at the preclearance station. The Obama Administration reviewed this decision, but in August 2009 Secretary Napolitano announced that negotiations to construct a preclearance site adjacent to the Peace Bridge would not be reopened.

A second issue is the ability of the transportation infrastructure to cope with increased security measures. The aging condition and limited capacity of the land border infrastructure preceded the terrorist attacks. For example, the Ambassador Bridge and the Detroit-Windsor Tunnel, which together carry 25% of total U.S.-Canada cross-border traffic, both opened in 1930. Approaches to the crossings, often city streets, have been criticized as inadequate to the commercial needs of the 21st century. This issue affects the efficient implementation of security measures. The FAST system provides for dedicated lanes at land border ports for expedited preclearance. However, these lanes will not save time if the FAST participant cannot access this lane due to congestion or delays at the points of access. The SPP completed a pilot program that attained a 25% improvement in border crossing times at the Detroit-Windsor gateway in December 2005, yet the aging and adequacy of the border infrastructure may affect whether such improvements are sustainable.

There are two competing plans to build additional bridge capacity over the Detroit River to ease truck congestion on the Ambassador Bridge. One proposal involves building a new span adjacent to the Ambassador and has been put forward by the private owner of the bridge. A competing proposal, the Detroit River International Crossing (DRIC), would be built approximately 2 miles south of the Ambassador between Zug Island in Detroit and the Brighton Beach area of Windsor. The DRIC proposal is supported by the Canadian government, which believes a new span should not be privately held. To this end, then-Canadian Transport Minister John Baird offered to loan

the state of Michigan \$550 million to fund its share of the new bridge, the total cost of which is expected to be \$5.3 billion. Michigan Governor Rick Snyder endorsed the construction of the bridge in January 2011, but a bill creating a bridge authority was rejected by a Michigan state Senate committee in October 2011. Meanwhile, the owner of the Ambassador Bridge, the principal opponent of the new crossing, has brought a North American Free Trade Agreement (NAFTA) investor-state dispute over his contention that the proposed rival bridge would divert traffic (and tolls) from his bridge.

Questions

1. Is Canada doing enough to secure the border against the transit of terrorists or weapons of mass destruction? Do Canadians think that the United States has placed too much emphasis on securing the northern border against terrorists to the detriment of efficient trade relations?
2. Are Canadian business and government officials concerned that another terrorist-related border shutdown could cause the relocation of business to the United States or dampen the attractiveness of Canada as a recipient of foreign investment?
3. How important is building a new Detroit-Windsor bridge to cross-border trade? The owner of the Ambassador Bridge has offered to assume the cost of building a twin span adjacent to the current bridge. Why not let him?
4. Do you believe aspects of the Beyond the Border declaration threaten Canadian sovereignty? How has the Canadian government communicated the specifics of the negotiations to legislators or to average Canadians?

Canada's Free Trade Agreement Agenda⁷³

Issue Definition

While the current Doha Round of multilateral World Trade Organization (WTO) negotiations remains stalled, regional and bilateral free trade agreements (FTA) have become a prominent, if controversial, feature of the world trading system. In the past, the United States was relatively more aggressive in pursuing FTAs, while Canada emphasized multilateral trade liberalization to supplement liberalization with its predominant partner, the United States, first through the U.S.-Canada FTA and subsequently through the North American Free Trade Agreement (NAFTA). This trend has shifted with Canada now negotiating several FTAs as it seeks to join the Trans-Pacific Partnership (TPP), a proposed FTA being negotiated among the United States, Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, and Vietnam.

⁷³ Written by Ian F. Fergusson, Specialist in International Trade and Finance; Foreign Affairs, Defense, and Trade Division

Background

After concluding the U.S.-Canada FTA in 1988 and expanding it to include Mexico in 1994, both countries made the new WTO the cornerstone of further trade liberalization. While both countries concluded FTAs, political rationales were often paramount. For example, close ties prompted both countries to conclude FTAs with Israel. Canadian attempts to establish a greater role in Latin America were reflected in FTAs with Chile (1997) and Costa Rica (2002). Negotiations were started with the European Free Trade Area (EFTA) nations (Norway, Switzerland, Iceland, and Liechtenstein) in 1998, with Singapore and with the Central American Four (El Salvador, Guatemala, Honduras, Nicaragua) in 2001, and with South Korea in July 2005. However, none of these negotiations yielded an agreement during the Liberal governments of Jean Chrétien and Paul Martin. Moreover, the importance of such agreements was overshadowed by the overwhelming volume of Canadian trade that continued to be conducted under NAFTA, with the United States continuing to account for the bulk of that trade.

In 2001, the George W. Bush Administration embarked on a new trade strategy known as “competitive liberalization.” This policy pushed forward trade liberalization simultaneously on bilateral, regional, and multilateral fronts. It was designed to spur trade negotiations by liberalizing trade with countries willing to join FTAs, and to pressure other countries to negotiate multilaterally. A pending agreement with Jordan, negotiated with the Clinton Administration was passed by Congress in 2001. Under trade promotion authority (TPA) passed by Congress in 2002 and in effect until 2007, FTAs were negotiated and approved by Congress with Chile, Singapore, Australia, Morocco, the countries of the Central American Customs Union and Dominican Republic (Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic), Bahrain, Oman, and Peru. In addition, negotiations were conducted with the nations of the South African Customs Union (SACU) (Botswana, Lesotho, Namibia, South Africa, and Swaziland), the United Arab Emirates, Malaysia, and Thailand, but they resulted in no agreement. Long pending agreements with Colombia, Panama, and South Korea concluded under TPA were approved by Congress in October 2011. Currently, the Obama Administration’s trade policy has stressed enforcement of existing trade agreements rather than negotiating new ones. The one exception has been the TPP negotiations.

The Conservative government of Prime Minister Stephen Harper, first elected in 2006, has placed greater emphasis on negotiating regional and bilateral FTAs. Existing negotiations with EFTA were concluded in January 2008, resulting in an agreement that was approved by Parliament in January 2009 and received Royal Assent in April 2009. Negotiations with Peru and Colombia were initiated in June 2007. An agreement was signed with Peru in May 2008, which was approved by Parliament in June 2009 and received Royal Assent later in the month. Negotiations with Colombia were concluded in November 2008, and was approved by Parliament and received Royal Assent in June 2010. The Canada-Colombia FTA went into effect on August 15, 2011. Legislation to implement FTAs with Jordan (signed in August 2008) and Panama (signed in May 2010) were re-introduced in the 41st Parliament on November 15, 2011. In general, the Conservative and Liberal parties have voted to approve these agreements, but have been opposed by the labor-influenced New Democratic Party (NDP) and the Québec-separatist Bloc Québécois.

In addition, negotiations have been started with Morocco, the Dominican Republic, India, Ukraine, and the nations of CARICOM, and are continuing with South Korea, Singapore, and the Central American Four. With South Korea, issues familiar to U.S. negotiators, such as market access for beef and non-tariff barriers in the auto sector, are complicating the talks. Most recently,

during a trip to Asia, Prime Minister Stephen Harper announced the launch of negotiations with Japan and Thailand as well.

At the Asia-Pacific Economic Cooperation Forum (APEC) in November 2011, the leaders of Canada, Japan, and Mexico announced that they would seek consultations with TPP partner countries with a view towards joining the negotiations. Canada has held consultations with the United States and other countries, and the U.S. Trade Representative has sought public comment from interested stakeholders on Canada's potential participation. Canada reportedly has encountered resistance from New Zealand and the United States over its dairy supply management policies, and from the United States over its intellectual property rights regime. For its part, Canada has vigorously pursued membership, attempting to make the case that Canada was willing to meet the high level of ambition for the talks.

In May 2009, Canada and the European Union (EU) agreed to launch FTA negotiations, known as the Comprehensive Economic and Trade Agreement (CETA), and nine rounds of negotiations have occurred thus far. This negotiation is significant in that it raised issues of concern to countries at a similar level of development and with relatively low tariffs. Issues that have been flagged include the regulation of professional services, temporary entry for business workers, and provincial participation in government procurement agreements. Agreement on this latter point may become easier following the U.S.-Canada agreement on Buy American provisions in the U.S. economic stimulus. Negotiations on agriculture likely will prove challenging, as both sides will likely seek to protect sensitive sectors, yet negotiations on traditional sticking points such as the EU's desire to protect geographic indications and Canadian supply-management policies reportedly have not been precluded.

Status of the Issue

The Conservative government's new enthusiasm for negotiating FTAs was expressed by then-International Trade Minister Peter Van Loan on April 23, 2010. Canada is pursuing FTAs "with a vigor right now because we're a trading country, our businesses need it, our workers need it, our prosperity depends on it, so we're going to make it happen for Canada and not simply depend on the WTO." While in some ways this policy resembles the "competitive liberalization" policy undertaken by the George W. Bush Administration, it remains to be seen whether agreements resulting from such negotiations, will increase trade flows and lessen the dependence of Canada on the U.S. market. It also remains to be seen whether Canada will retain its traditional engagement in the WTO.

Questions

1. How controversial is the Canadian government's trade policy? Does the public approve of further trade liberalization? How does the continuing decline of the Canadian manufacturing sector affect public attitudes towards free trade generally?
2. Do you think the emphasis on negotiating bilateral and regional FTAs complements or weakens the multilateral trading system? Does this policy reflect a lack of confidence in the ability to conclude the WTO Doha Round, or that Canada will not benefit much from a Doha agreement?
3. Canadian negotiators are actively pursuing TPP participation and maintain that Canada can meet the high level of ambition for the talks, while not appearing to negotiate with itself on issues

such as supply management. How well do you believe this balance is being achieved? Do you believe that Canada should encounter resistance in joining the negotiations, given the level of economic development of certain existing negotiating partners such as Vietnam and Malaysia?

4. Would joining the TPP advance the objective, promoted by successive Canadian governments, of expanding Canada's role in the Asia-Pacific region? If Canada is not invited to join the TPP, would the recently announced negotiations with Japan and Thailand represent an acceptable "Plan B"?

5. FTA negotiations are continuing between the European Union and Canada. How optimistic are you that the negotiations will be concluded this year? Do you believe that "there is no more important trade negotiating priority today than the CETA," quoting the communique from the annual Federal-Provincial trade ministers meeting in Ottawa on February 28, 2012, or that it is "jumping on a sinking ship," quoting a Canadian commentator?

North American Cooperation on Competitiveness and Security⁷⁴

Issue Definition

How can the United States improve cooperation with its North American neighbors on issues related to trade, transportation, and security? How are the United States, Canada, and Mexico currently cooperating on improving competitiveness, promoting economic growth, and enhancing security in North America? Should the three countries continue cooperating trilaterally or would separate, bilateral cooperation efforts with Canada and Mexico be more effective due to the different issues facing each country?

Background and Analysis

The United States, Canada, and Mexico have made efforts since 2005 to increase cooperation on security and economic issues through various endeavors, most notably by participating in trilateral summits known as the North American Leaders Summits. The most recent Summit was hosted by President Barack Obama on April 2, 2012 in Washington, DC at the White House where he met with Canadian Prime Minister Stephen Harper and Mexican President Felipe Calderón to discuss the economic well-being, safety, and security of the United States, Mexico, and Canada.

After the meeting, the three leaders issued a joint statement in which they renewed their commitment to North American cooperation in the following key areas of interest: protection and enforcement of intellectual property rights (IPR); enhancement of collective energy security, including the safe and efficient exploration and exploitation of resources; advancement of the goals of the Energy and Climate Partnership of the Americas and enhancement of electricity interconnection in the Americas; support of efforts to advance a lasting global solution to the

⁷⁴ Prepared by Angeles Villarreal, Specialist in International Trade and Finance, Foreign Affairs, Defense, and Trade Division.

challenge of climate changes; and the recognition of the importance of adopting the Budapest Convention on Cybercrime, including Canada's commitment to ratifying the Convention and Mexico's necessary preparations for signing it. In addition, the leaders announced the North American Plan for Animal and Pandemic Influenza (NAPAPI) to strengthen North America's response to future animal and pandemic influenza events. In the area of strengthening security in the Americas and concerns about transnational organized crime, the three governments agreed to launch in 2012 a consolidated Central America Integration System-North America Security Dialogue to deepen regional security coordination and cooperation.

The first North American Leaders' Summit took place on March 23, 2005, in Waco, TX; this was followed by several trilateral summits in Mexico, Canada, and the United States. The March 2005 Summit resulted in increased efforts to enhance North American regulatory cooperation through the former initiative known as the Security and Prosperity Partnership of North America (SPP). The main goal was to increase and enhance prosperity in the United States, Canada, and Mexico through regulatory cooperation. The SPP was endorsed by all three countries, but it was not a signed agreement or treaty and contained no legally binding commitments or obligations. Although the SPP built upon the existing trade and economic relationship of the three countries, it was distinct from the existing North American Free Trade Agreement (NAFTA).

The SPP has evolved to other efforts pursued by the Obama Administration for regulatory cooperation, which have included separate bilateral endeavors. In May 2010, the United States and Mexico released the Declaration Concerning Twenty-first Century Border Management and, in December 2011, the United States and Canada announced the Beyond the Border Action Plan: A Shared Vision for Perimeter Security and Economic Competitiveness. In February 2012, the United States and Mexico announced the High-Level Regulatory Cooperation Council (HLRCC) to help align regulatory principles, an effort similar to the U.S.-Canada Regulatory Cooperation Council. In March 2012, the Defense Ministers of the three countries met in Ottawa, Canada for the first ever "Trilateral Meetings of North American Defense Ministers" to increase cooperation on national security issues.

Most efforts to increase North American regulatory cooperation generally have followed the recommendations of special working groups created under the SPP. These recommendations have included (1) increasing the competitiveness of North American businesses and economies through more compatible regulations; (2) making borders smarter and more secure by coordinating long-term infrastructure plans, enhancing services, and reducing bottlenecks and congestion at major border crossings; (3) strengthening energy security and protecting the environment by developing a framework for harmonization of energy efficiency standards and sharing technical information; (4) improving access to safe food and health and consumer products by increasing cooperation and information sharing on the safety of food and products; and (5) improving the North American response to emergencies by updating bilateral agreements to enable government authorities from the three countries to help each other more quickly and efficiently during times of crisis.

Some critics of North American trilateral cooperation contend that it has been an attempt to create a common market or economic union in North America. Others have contended that past efforts under the SPP were contributing to the creation of a so-called "NAFTA Superhighway" that would link the United States, Canada, and Mexico with a "super-corridor." Proponents of North American competitiveness and security cooperation view the initiatives as constructive to addressing issues of mutual interest and benefit for all three countries. Business groups generally

support increased North American cooperation and believe that it is necessary to enhance the competitiveness of U.S. businesses in the global market.

Status of the Issue

The United States, Canada, and Mexico have made progress in recent years in addressing issues related to North American competitiveness and security. The Obama Administration has affirmed its commitment to continue past efforts on North American cooperation under a different approach from the Bush Administration's SPP framework. The 2012 North American Leaders Summit and the former SPP have served as mechanisms to increase communications among North American trading partners on issues of mutual interest, but because there are no binding agreements, their role in improving prosperity and security has been limited.

Questions

1. How effective has North American cooperation been in improving competitiveness through its focus on intellectual property rights protection and regulatory harmonization? What other steps can be taken by the three countries to improve competitiveness of U.S. businesses?
2. How effective has North American cooperation been in improving safety, security, and the flow of goods and services among NAFTA partners? What other steps could be taken in these areas?

Canada's Financial System⁷⁵

Issue Definition

Canadian banks on the whole weathered the 2008-2009 financial crisis better than banks in the United States and Europe. Nevertheless, Canada's financial system was buffeted by the financial crisis as equity and housing prices fell and as economic growth slowed as a result of the downturn in global trade. Canada's economy is also feeling the effects of the European sovereign debt crisis. Are there lessons to be learned from Canada's banking system, which has proven to be somewhat more immune to the financial troubles that have brought down better known banks?

Background and Analysis

Canada's financial system proved to be more resistant to the failures and bailouts that marked systems in the United States and Europe. No Canadian financial institution failed or required public capital injections. Nevertheless, the financial crisis and global economic recession battered the Canadian economy in ways that are similar to those in the United States and in Europe. According to the International Monetary Fund (IMF), the Canadian economy contracted by -2.5% in 2009, before rebounding to a positive growth rate of 3.0% in 2010. Canada's economy is estimated to have grown by 2.4% in 2011, but forecasts for 2012 indicate that economic growth

⁷⁵ Prepared by James Jackson, Specialist in International Trade and Finance, Foreign Affairs, Defense, and Trade Division.

could slow slightly to 2.0% The vast economic and financial linkages between Canada and the United States means that Canada is feeling the impact of the slowing U.S. economy.

Much of Canada's economic recovery is attributed to low interest rates and a \$33 billion fiscal stimulus package—one of the largest among advanced economies—over two years in infrastructure spending, tax decreases, worker retraining, housing, and aid to struggling industries. In addition, the federal government pumped additional liquidity into the economy by purchasing insured mortgages. In April 2009, the Bank of Canada lowered the nation's key interest rate to 0.25%. A drop in commodity prices caused the Canadian dollar to fall relative to the U.S. dollar, which improved the cost competitive position of Canada's exports. In relative terms, Canada's fiscal outlook is among the best in the G-20.

According to the Bank of Canada, major risks to Canada's economic recovery are (1) global sovereign debt issues associated with some European countries that potentially could raise borrowing costs for Canadian banks; (2) an economic downturn in advanced economies, especially in Europe, could drag down economic growth; (3) the risk that global financial imbalances arising from large current account (exports and imports of goods, services, and income) imbalances could be disorderly and create sharp adjustments to exchange rates and other financial asset prices; (4) high levels of indebtedness among Canadian households leave them vulnerable to economic and financial shocks; and (5) low interest rates could encourage excessive risk taking. Although Canadian banks are not highly exposed to public or private entities in Greece, Italy, Spain, or Portugal, Canadian banks are exposed to banks in Europe and the United States that are themselves highly exposed to the four countries. This high level of financial linkages could amplify shocks throughout the global financial system.

The IMF has concluded that Canada's financial system is highly mature, sophisticated, and well-managed. In addition, the system is characterized by strong prudential regulation and supervision, stringent capital requirements, low risk tolerance, a well-designed system of deposit insurance and arrangements for crisis management and resolution of failed banks, a well-regulated and conservative mortgage market, and comprehensive mortgage insurance coverage. Supervisory responsibility for the financial sector in Canada is divided among the federal government, the provincial governments, and among a group of agencies within the federal government. The federal government is responsible for supervising all banks, federally incorporated insurance companies, trust and loan companies, cooperative credit associations, and federal pension plans. Provincial governments are responsible for supervising securities dealers, mutual fund and investment advisors, credit unions, and provincially incorporated trust, loan, and insurance companies. As a result, there are 13 regulatory authorities, each administering a separate set of securities laws and regulations.

Within the federal government, the Financial Institutions Supervisory Committee (FISC) acts as the chief coordinating body that sets regulatory policy and supervises financial institutions. The Committee is comprised of the Department of Finance of the Ministry of Finance and four independent government agencies: the Office of the Superintendent of Financial Institutions (OSFI); the Bank of Canada; the Canada Deposit Insurance Corporation; and the Financial Consumer Agency of Canada (FCAC). All of these agencies report to the Minister of Finance, who is responsible to the Canadian Parliament. The Bank of Canada is responsible primarily for conducting monetary policy by setting interest rate targets and adjusting the supply of credit. The bank also serves as the key component in the payments system by providing a check clearing function, and it serves as the traditional lender of last resort. The Office of the Superintendent of Financial Institutions plays a key role in Canada's financial supervisory scheme by supervising all

domestic banks, branches of foreign banks operating in Canada, trust and loan companies, cooperative credit companies, life insurance companies, and property and casualty insurance companies.

The financial system is dominated by five large banking groups (Royal Bank of Canada, TD Canada Trust, Bank of Nova Scotia, Bank of Montreal, and Canadian Imperial Bank) that account for about 60% of total assets. In comparison, foreign banks account for about 4% of assets. The low representation by foreign banks is attributed to the “widely-held” rule for large banks that limits the concentration of bank share ownership and, therefore, reduces the scope for mergers and for foreign entry through acquisition. Canada’s financial legal framework has allowed Canadian banks to concentrate on their low-risk, profitable domestic retail banking activities (services provided to individuals including: deposits, savings accounts, mortgages, credit cards, etc.), leaving large domestic borrowers to conduct their wholesale banking activities (services provided to corporations, governments, and other entities) abroad. Canada’s insurance sector is dominated by three large domestic groups, which account for over 80% of the assets in this sector. The securities sector is marked by large Canadian, as well as U.S. and UK securities firms.

Unlike the United States and some European countries, subprime mortgages account for less than 5% of Canadian mortgages, which sharply limited Canada’s direct exposure to the meltdown that occurred in the subprime mortgage market. In addition, Canadian law requires that all bank-held mortgages above a loan-to-value ratio above 80% be insured, which has curtailed the securitization of mortgages by banks in Canada. In addition, prepayment penalties and the lack of interest deductibility reduces the demand for long-term mortgages, so the maturity of most mortgages does not exceed 5 to 10 years.

Canada’s financial supervisory system and regulatory structure have proven to be less susceptible to the bank failures that have loomed in the United States and Europe. Nevertheless, Canada’s approach has a number of drawbacks. Canada’s system of regulating securities markets at the provincial level means that regulations regarding market participants and investor protection differ by province and that the nature, structure, and powers of the provincial regulators also vary. In addition, the conservative, risk-adverse approach employed by Canada’s banks shielded the banks from some of the current financial turmoil, the approach also reduces efficiency in the market and reduces competition. Acquisitions of Canadian banks is significantly impeded by the rule that bank stocks be widely held and mergers are effectively prohibited. With reduced competitiveness pressures, Canadian banks maintain low-risk balance sheets at the expense of greater innovation and more efficient capital allocation. This approach also means that financing for small firms and venture capital for potentially high-growth companies is sharply reduced. In concert with other advanced economies, Canada is moving to provide greater oversight of the over the counter (OTC) derivatives market by developing central counterparty services and a central clearing of standardized OTC derivatives contracts.

Questions

1. Do the differences in the size and the scope of the U.S. and Canadian financial markets reduce the importance of the Canadian system as a model for the United States to potentially follow?
2. Are there aspects of Canada’s federal supervision of its banking system that could serve as a model for bank supervision by the United States?

3. Canada's approach to financial supervision concentrates the majority of that responsibility in an authority that is separate from the central bank. Is this an approach that the United States should consider as it evaluates the effects of changes it has made to its own regulatory structure?

U.S. Imports of Canadian Softwood Lumber⁷⁶

Issue Definition

The U.S. lumber industry has long argued that imports of subsidized Canadian lumber are injuring U.S. producers. In May 2002, after the U.S. lumber industry filed antidumping and countervailing petitions to restrict imports, agency determinations of Canadian subsidies, dumping, and injury to the U.S. industry led to a duty of 27% (later reduced) on most Canadian softwood lumber imported into the United States. Canada challenged these findings under NAFTA and before the WTO. Negotiations led to a seven-year Softwood Lumber Agreement in 2006 with Canadian export charges depending on U.S. lumber prices, and the United States revoked the countervailing and antidumping orders. On January 23, 2012, the United States and Canada agreed to extend this agreement—as provided for in the agreement—for two years beyond its October 2013 expiration.

On February 26, 2009, a tribunal found that four Canadian provinces had violated the Agreement in calculating 2007 quotas; the United States rejected the Canadian offer of compensation, and on April 15, 2009, the United States began collecting 10% *ad valorem* duties from the four provinces to compensate for the 2007 breach.

Background and Analysis

U.S. lumber producers have long expressed concerns about imports of subsidized Canadian lumber. The current lumber agreement is termed Lumber IV, because it is the result of the fourth dispute since 1981, with various findings of subsidy levels and agreements in the previous disputes.

Tension between the United States and Canada over softwood lumber trade may be inevitable. Both countries have extensive forest resources, but vastly different population levels and development pressures; vast stretches of Canada are still largely undeveloped, while less area in the United States (outside Alaska) remains relatively pristine. These differences have led to divergent forest policies. In Canada, 90% of the forests are owned by the provincial governments, which have allocated and priced timber to encourage development of the extensive timber reserves and settlement of unpopulated areas. In the United States, 58% of timberlands are privately owned, and private markets dominate the allocation and pricing of timber. U.S. federal and other government-owned forests are regionally important, but the timber is typically sold in a competitive market.

⁷⁶ Prepared by Ross W. Gorte, Specialist in Natural Resources Policy, Resources, Science, and Industry Division, and Jeanne J. Grimmett, Legislative Attorney, American Law Division and updated by Ian F. Fergusson, Specialist in International Trade and Finance.

U.S. lumber producers assert that subsidies have given Canadian producers an unfair advantage in the U.S. market. Canadian provincial stumpage fees (for the right to harvest trees) are asserted to be subsidized, leading to lumber prices that are less than their fair market value. The provinces generally use leases and administered fees to allocate and price timber. Administered fees are unlikely to match market values, but determining whether the fees are below market values has been controversial, because of differences in tree species, sizes, and grades; in measurement systems; in requirements on harvesters; in environmental protection; and in other factors.

Log export restrictions in British Columbia are also alleged to be subsidized, because they assure more supply (less competition for timber and thus lower costs) for Canadian producers. Evidence from the U.S. Pacific Northwest, where private logs can be exported but public timber cannot, indicates substantially higher prices for exported logs.

Injuries to U.S. lumber producers are difficult to establish decisively, although the U.S. International Trade Commission (ITC) has found injury every time it has examined the issue. Canada's share of the U.S. lumber market has risen substantially, from less than 7% in the early 1950s to more than 33% since the mid-1990s. Under the 1996 agreement, the quantity of imports continued to rise, but the market share was relatively stable. The impact of restrictions on U.S. lumber prices is not easily estimated, but restrictions have probably put upward pressure on prices.

Status of the Issue

In 2001, after the 1996 U.S.-Canada softwood lumber agreement expired, the U.S. Coalition for Fair Lumber Imports filed countervailing duty and antidumping petitions, asking the DOC to investigate Canadian imports again. The Department of Commerce issued final determinations of subsidies on March 22, 2002. On May 3, 2002, the ITC determined that the U.S. lumber industry was threatened with material injury by Canadian imports. A duty averaging 27% was imposed on May 22, 2002.

Canada challenged each of the agency determinations under the North American Free Trade Agreement (NAFTA) and in the World Trade Organization (WTO). The NAFTA panels largely supported the Canadian positions. The WTO proceedings resulted in mixed decisions. Canada was also concerned that the US\$5 billion in estimated duties on softwood lumber collected by the United States would eventually be distributed to U.S. lumber producers under the Continued Dumping and Subsidy Offset Act (Byrd Amendment). Canada obtained a U.S. court decision, however, holding that the Byrd Amendment did not apply to Canadian lumber imports.

On April 26, 2006, a tentative seven-year Softwood Lumber Agreement, with an optional two-year renewal, was announced to resolve the dispute. The United States revoked the countervailing and antidumping duty orders and returned about US\$4 billion to the importers of record. The remaining deposits (about US\$1 billion) were split evenly between the members of the Coalition for Fair Lumber Imports and jointly agreed-upon initiatives. Canada is collecting export charges ranging up to 15%, depending on a weighted average lumber price, or up to 5% with volume restraints. A surge mechanism would raise export charges if a Canadian region's exports exceed its allocated share. Lumber from logs harvested in the Atlantic Provinces, Yukon, Northwest Territories, or Nunavut is exempt from the export charges. Disputes are to be resolved through bilateral consultations, non-binding mediation, or binding arbitration in the London Court of International Arbitration (now LCIA).

U.S. interest groups have questioned whether Canada is faithfully implementing the agreement. The 2008 farm bill (P.L. 110-246) included a provision (§3301) establishing a softwood lumber importer declaration program to verify and reconcile data on softwood lumber imports. In August 2007, U.S. officials requested a ruling from the London Court of International Arbitration (LCIA) on export quota volumes and export tax levels. In March 2008, the Court ruled that Canada had violated the export quota volumes for Manitoba, Ontario, Québec, and Saskatchewan for the first six months of 2007, but was not required to collect taxes related to export surges from Alberta and British Columbia during that period. To comply with the above ruling, an LCIA tribunal issued a decision that Canada must collect an additional 10% *ad valorem* export charges from the four provinces until C\$68.26 million (then valued at US\$54.8 million) had been collected on February 26, 2009. The U.S. Trade Representative rejected the Canadian offer of a compensation payment of US\$36.66 million, and on April 15, 2009, began collecting 10% duties on lumber from the four provinces.

In January 2008, the United States requested arbitration over six provincial forest sector assistance programs in Quebec and Ontario, programs that the United States believes contravene the anti-circumvention provision of the SLA. In January 2011, the LCIA found certain of these programs breached the SLA, and Canada began imposing additional charges on lumber from Quebec and Ontario for the duration of the agreement.

U.S. lumber producers and some Members of Congress, including Senators Max Baucus and Olympia Snowe, have urged the Administration to seek consultations under the SLA over certain timber pricing practices in British Columbia. They claim that the BC government has been classifying an increasing amount of its cut as salvage Grade 4 lumber and charging less for it than better grades, resulting in a subsidy for Canadian timber processors. Canada attributes this increase to an infestation of mountain pine beetles, but U.S. producers dispute this, claiming that BC has changed its grading procedures and producers are heating lumber prior to grading, resulting in greater cracks and defects. In October 2010, the USTR announced consultations with Canadian officials, but the unsuccessful negotiations led the USTR to file a request for arbitration in the LCIA on January 18, 2011. An LCIA tribunal hearing was held in Washington D.C. from February 27-March 9, 2012 on the dispute.

Questions

1. The modern dispute over U.S. imports of Canadian lumber has persisted for nearly 30 years. Do Canadian producers have a significant cost advantage because of Canadian timber practices and/or subsidies? Should Canadian practices be modified to enhance competition for timber? Do the systems and situations vary sufficiently to warrant different responses to each Canadian province? What might be the environmental consequences of various possible changes?
2. In January 2012, the SLA was extended until 2015. Given the three arbitrations, do you believe it has performed satisfactorily enough to extend it? Are the current oversight mechanisms sufficient to assure that implementation of the agreement is acceptable to all parties? Are there ways to provide adequate and timely data to identify possible violations (deliberate or unintentional) and thus the delay and cost of arbitration and subsequent remedies? What unilateral U.S. enforcement measures might be acceptable to Canada under the agreement?
3. What approaches are feasible to compensate communities and workers for injury from weak lumber markets without providing subsidies to the lumber industry?

Canada's Supply Management Programs for Dairy, Poultry, and Eggs⁷⁷

Issue Definition

Canada uses supply management to support its dairy, poultry, and egg sectors. Its main features (1) provide price support to producers based on their production costs and return on equity and management, (2) limit production to meet domestic demand at the cost-determined price, and (3) restrict imports to protect against foreign competition. The Canadian government has supported producers' decisions to use this approach for more than 40 years, and succeeded in limiting imports of these products in negotiating the U.S.-Canada Free Trade Agreement and its multilateral commitments in the Uruguay Round's Agreement on Agriculture. Canada's interest in participating in the Trans-Pacific Partnership (TPP) trade negotiations has renewed calls from interest groups in the United States and New Zealand for Canada to open its borders to imports of these products. While Canadian dairy, poultry, and egg producers generally oppose trade liberalization, others argue that Canada should consider making concessions so that other Canadian economic sectors can benefit from export openings negotiated in the TPP context with the growing Asian economies.

Background and Analysis

According to the World Trade Organization, Canada in recent years has introduced an agricultural policy framework that includes a number of business risk management measures designed to partially compensate producers for revenue or income losses arising from low commodity prices, increased production costs, reduced production, or natural disasters. However, the supply management systems for dairy, poultry, and eggs "remain unchanged."

National bodies and provincial commodity marketing boards, granted statutory powers by the federal and provincial governments, control the supply management systems for these commodities. At the national level, the amount of each commodity that producers can market is controlled by a quota system. Imports of each commodity are limited by tariff rate quotas. These allow a specified amount to enter annually under Canada's trade commitments at little or zero duty, but apply a very high tariff on imports above the specified level or quota amount. Both tools work together to control the supply of each commodity, but the objective is to ensure that producers receive a price that guarantees them a return that covers their production costs. The quota is set to balance supply with demand at that price, and is frequently adjusted to ensure that this balance is achieved. Producers of these commodities must participate in their respective supply management systems, with farm-level production subject to individual quota limits that can only be sold into permitted marketing channels.

Supply management for dairy is divided into a nationally-managed system for industrial milk (used to manufacture dairy products such as cheese and butter) and provincial-level systems for the marketing of fresh milk. The Canadian Milk Supply Management Committee (CMSMC) oversees the national system for industrial milk. It is chaired by the Canadian Dairy Commission

⁷⁷ Prepared by Remy Jurenas, Specialist in Agricultural Policy, Resources, Science and Industry Division.

(CDC), a federal agency that provides a framework for federal-provincial participation. The CMSMC determines the national domestic supply of industrial milk and allocates this volume among provinces.

The Farm Product Council of Canada (FPCC) oversees four national marketing agencies for poultry (chicken and turkey) and eggs that seek to balance the interests of stakeholders from producers to consumers. These agencies (Chicken Farmers of Canada, Turkey Farmers of Canada, Egg Farmers of Canada, and Canadian Hatching Egg Producers) are managed by representatives primarily from provincial commodity boards plus a few members representing processors and consumer associations. The provincial commodity boards regularly consult with their stakeholders to determine their poultry and egg needs. This information is used to set the national production level, which the agencies implement under a quota order that the FPCC must approve. Each provincial board allots its share of each quota to registered producers, and negotiate producer selling prices with processors.

Producers of these commodities point out they have benefited from the supply management approach because it has significantly reduced price volatility. The stability of prices over time, combined with the guarantee that covers production costs, has served to provide income support. Others point out that these features have resulted in the lack of market orientation for these commodities, as the value of supply management has become capitalized, or incorporated, into the value of the quota. In other words, those who hold the quota benefit more than producers.

Status of the Issue

In November 2011, Prime Minister Harper expressed Canada's interest in seeking to join the TPP talks and initiating consultations with the nine countries already negotiating the TPP. This interest has focused attention on how Canada's supply management systems for dairy, poultry, and eggs could be affected. Harper subsequently stated that Canada will not negotiate this issue in order to gain entry, and has remained non-committal on how supply management would be handled if Canada is welcomed as a TPP participant. He has stated that Canada expects to negotiate and debate "all manner of issues" if it were to join the TPP, and also has said if that occurs, Canada would attempt to "promote and to defend [its] interests not just across the economy, but in the individual sectors as well." President Obama when asked whether Canada would have to drop supply management in order to join the TPP reportedly only hinted in his response that Canada may have to make some adjustments in this area.

Though the United States exports dairy and poultry products to Canada, the import quotas in place under supply management have significantly limited access to this next-door market. The National Milk Producers Federation representing U.S. dairy farmers and dairy cooperatives, and the U.S. Dairy Export Council representing this sector's export interests, have stated they would support Canada's inclusion in the TPP only if the United States and Canada finally negotiate comprehensive market access for all agricultural sectors, including the full range of dairy products. Also, both groups would want to see negotiators tackle outstanding non-tariff measures that have and could limit access for U.S. fluid milk and cheese in the Canadian market.

The National Chicken Council has reportedly urged the U.S. Trade Representative to condition Canada's inclusion in the TPP talks on its agreement to open up its market to U.S. poultry in a short period of time.

Questions

1. Most of the support for Canada's supply management systems is concentrated in Ontario, Quebec, and the Maritime provinces. What would be the internal politics associated with completely changing these systems or modifying them to allow for increased imports of dairy and poultry products from the United States and other TPP countries?
2. How strong is support among other Canadian economic sectors for maintaining Canada's supply management programs?
3. Could Canada ensure that the objectives of supply management (stable prices and income support to producers) are met if additional imports are allowed? Please elaborate on why or why not this would be the case?

Country of Origin Labeling⁷⁸

Issue Definition

Mandatory country-of-origin labeling (COOL) in the United States for specified agricultural products took effect on March 16, 2009. This was the culmination of a near decade-long legislative effort to arrive at an accommodation that addressed the concerns of competing interests. U.S. food retailers are now required to label the country of origin for fresh produce (fruits and vegetables), meats, nuts, and seafood, among other products. Canada and Mexico are major suppliers of live cattle and hogs that are fed in U.S. facilities and/or processed into beef and pork in U.S. meat packing plants. As the U.S. meat processing sector geared up to implement COOL, U.S. imports of Canadian and Mexican cattle and of Canadian hogs noticeably declined. Concerned that this development adversely affected their livestock sectors and not satisfied with the outcome of consultations held with U.S. officials, Canada and Mexico pressed their case using the World Trade Organization (WTO) dispute resolution process. The WTO panel handling this case found that COOL with respect to meat labeling violates international trading rules. The United States appealed these findings, and a WTO decision on this appeal is expected to be reached by late June 2012.

Background and Analysis

Under the Tariff Act of 1930, as amended, most unprocessed agricultural commodities had long been exempt from requirements that every import be clearly marked to indicate country of origin for the "ultimate purchaser." However, provisions in the 2002 farm bill (Section 10816 of P.L. 107-171) require that retailers covered by the Perishable Agricultural Commodities Act (i.e., those which deal in at least \$230,000 per year in produce—fresh and frozen fruits and vegetables) begin to provide such information. Other covered commodities specified in the 2002 farm bill were: ground and muscle cuts of beef, lamb and pork; seafood; and peanuts. Labeling is not required if these commodities are ingredients in processed foods, or if they are sold in dining-out settings.

⁷⁸ Prepared by Remy Jurenas, Specialist in Agricultural Policy, Resources, Science and Industry Division.

Passage of the initial COOL provisions in 2002 did not end debate over the value and efficacy of mandatory COOL, particularly with regard to meats. COOL opponents argued that record-keeping and verification costs will far exceed any perceived economic benefits to producers; that smaller-sized farms and firms will have the most difficulty with compliance; that little evidence exists showing consumers actually want labeling; and that COOL is a protectionist policy that undermines free trade. Supporters countered that compliance would not be nearly as burdensome as some large industry groups and USDA have portrayed it; that studies show U.S. consumers, if offered a clear choice, will pay extra for fresh foods of domestic origin, thereby strengthening demand and prices for them; and that consumers have a right to know where their foods were produced. They pointed out that all but two of the North American cases of “mad cow” disease (*bovine spongiform encephalopathy*, or BSE) occurred in Canadian-born cattle, yet the United States is permitting the import of large quantities of Canadian beef and cattle. (COOL opponents argue that country of origin labeling is a matter of marketing, not food safety, and that food safety concerns are best addressed through science-based regulation.)

Initially scheduled to take effect on September 30, 2004, Congress postponed COOL implementation until September 30, 2008, for all but seafood, because of ongoing debate. Some issues were addressed in talks held among key players during consideration of the 2008 farm bill, and incorporated into Section 11002 of the Food, Conservation, and Energy Act of 2008, P.L. 110-246. These provisions retained the implementation schedule, and added other commodities (chicken meat, goat meat, ginseng, pecans, and macadamia nuts) to its coverage. However, several new types of label categories were created that are intended to facilitate and simplify compliance in specifying the country or countries of red meat products. For all covered commodities, the amended law also seeks to ease recordkeeping and verification requirements, and to lower non-compliance penalties.

Status of the Issue

Following enactment of the amended COOL provisions, USDA moved quickly to issue rules to implement them. The August 2008 interim rule for meat labeling requirements generated the most controversy, in large part because of the steps that U.S. feeding operations and packing plants took to segregate, hold, and slaughter foreign-origin livestock (e.g., Canada and Mexico) from U.S. livestock. With U.S. bilateral trade agreements with Canada and Mexico having led to free trade in livestock and resulted in a more integrated North American livestock sector, imports of live cattle and hogs from both countries became subject to mandatory COOL. On December 1, 2008, Canada filed a request for formal WTO consultations on COOL with the United States, expressing concern about changes in normal livestock trade flows in reaction to the interim rule and questioning COOL’s legality under international trade rules. Bilateral consultations were held twice, but failed to resolve differences. On October 7, 2009, Canada requested the establishment of a WTO dispute settlement (DS) panel to review its claims. On November 19, 2009, the WTO agreed to establish a panel to examine this and Mexico’s nearly identical case on COOL.

Canada asserted that COOL is inconsistent with several WTO-related trade commitments, including those providing that imports must be treated no less favorably than products of domestic origin; that laws on marks of origin should not damage imports, reduce their value, or unreasonably increase their cost; and that laws, rules, and procedures on country of origin should not themselves create or disrupt international trade. Canadian officials stated that the COOL requirements are “so onerous” that Canadian exporters of cattle and hogs were discriminated against in the U.S. market. U.S. officials regretted that consultations did not resolve Canada’s

concerns, and stated their belief that U.S. implementation of COOL provides consumers with information that is consistent with WTO commitments. They noted that countries had agreed that country of origin labeling was legitimate policy long before the WTO was created, and that other countries (including Canada) also require goods to be labeled with their origin.

On November 18, 2011, the WTO DS panel found that COOL treats imported livestock less favorably than like U.S. livestock (particularly in the labeling of beef and pork muscle cuts), and does not meet its objective to provide complete information to consumers on the origin of meat products. The panel reached these conclusions by examining the economic effects of the measures taken by U.S. livestock producers and meat processors to implement COOL, and by accepting arguments that the labeling of meat, indicating where the multiple steps of livestock birth, raising, and slaughtering occurred, is confusing.

The Obama Administration welcomed the WTO's affirmation of the U.S. right to require COOL for meat products. Participants in the U.S. livestock sector had mixed reactions, reflecting the heated debate on COOL that occurred over the last decade. Those in the industry and some Members of Congress that favor COOL as now implemented urged the Administration to appeal the WTO panel's findings. Other groups and some Members that have questioned COOL called for the Administration to accept the report's findings, and begin to take steps to bring COOL into compliance with WTO rules. On March 23, 2012, the United States appealed the panel report to the WTO Appellate Body (AB). The AB that will consider this appeal has from 60 to 90 days to uphold, reverse, or modify the panel findings. If, as a result of the appeal, the United States is found to be in compliance with its WTO obligations, it would be free to continue COOL as now in effect. If the appeal fails, the United States would need to bring COOL into compliance with the AB's findings within a reasonable period of time. COOL opponents may use the opportunity to seek legislative changes as Congress considers the 2012 farm bill. Options would be to consider regulatory and/or statutory changes to the COOL regulations and/or law. Proponents in turn can be expected to vigorously defend a policy they worked for more than a decade to secure. If the United States does not comply, Canada and Mexico would have the right to seek compensation or retaliate against imports from the United States.

Questions

1. Reports in meat trade publications have suggested that the COOL requirements have strained marketing relationships between Canadian and U.S. livestock producers and meat processors. What economic adjustments if any have occurred in Canada's beef and pork sectors in response to the decrease in Canadian cattle and hog exports to the United States? To what degree have other market developments (e.g., exchange rates, impact of the economic recession, meat exports to third markets) affected the beef and pork sectors in both markets?
2. How does Canada's country of origin labeling program for agricultural commodities and food products compare to that implemented under the U.S. COOL program? Is it a voluntary or mandatory program?
3. If the WTO Appellate Body upholds the dispute settlement panel's findings (meaning the United States loses its appeal), what statutory and/or regulatory changes could be considered to bring the U.S. COOL program into compliance with such findings?

The Canadian Steel Sector⁷⁹

Issue Definition

The impact of the 2008 global financial crisis and the subsequent economic downturn has had substantial negative effects on manufacturing industries in the United States and Canada, including the steel industry. An earlier slump in steel, which occurred in the 1990s, led to numerous bankruptcies and takeovers of many U.S. and Canadian steel makers. As a result, almost all of the major steel makers in Canada are now foreign owned. Therefore, decisions to close or idle plants or reduce production in Canada have raised national economic and political concerns.

Pittsburgh-based U.S. Steel Corp. (U.S. Steel) idled many of its Canadian operations in 2009 when steel orders fell precipitously. The Canadian government, the United Steel Workers, and local steel manufacturers took legal actions against it under the Investment Canada Act (ICA), a Canadian federal law governing large foreign direct investment in the country. The Canadian government alleged that U.S. Steel is not abiding by commitments (such as investment and level of local employment) it made under the ICA when it acquired the Canadian steelmaker, Stelco, in 2007. After lengthy legal proceedings, the Canadian government and U.S. Steel reached an agreement to settle the case in December 2011.

Background and Analysis

During the 1990s and the first decade of the 21st century, many U.S. and Canadian steel companies experienced a downturn that led to a major restructuring and reorganization of the steel industry in North America. Today, the Canadian steel industry looks very different than it did in 2000. The major Canadian integrated steel producers, such as Stelco and Algoma Steel, are now owned by international companies. In 2006, Mittal Steel acquired several Stelco subsidiaries and U.S. Steel purchased the remaining part of Stelco, which was renamed U.S. Steel Canada Inc. Algoma Steel was purchased by Essar Steel of India in 2007, and operates as Essar Steel Algoma Inc.

The Canadian minimill steel sector also went through a restructuring process. Minimills produce steel from scrap metal in electric arc furnaces (EAFs). In 2002, the Canadian firm, Co-Steel, merged with Ameristeel, the North American subsidiary of Gerdau S.A., of Brazil. Dofasco, another big steel company, was acquired by Luxemburg-based Arcelor in 2006. At about the same time, Arcelor agreed to merge with Mittal Steel of Rotterdam and became ArcelorMittal. Dofasco is now a subsidiary of ArcelorMittal, the world's largest steelmaker. More recently, in 2008, Russia's Evraz Inc. S.A. acquired another major Canadian minimill steel maker, IPSCO Canada.

The U.S. and Canadian steel industry struggled from 1997 through 2002. In March 2002, President Bush imposed safeguard measures (in the form of increased tariffs) in response to surging imports of steel that were deemed to have seriously injured U.S. domestic steel producers. One goal of the safeguards was to enable a restructuring of the domestic steel industry to improve its efficiency and competitiveness. To a great extent, that restructuring has been

⁷⁹ Prepared by Rachel Tang, Analyst in Asian Affairs; Foreign Affairs, Defense, & Trade Division.

achieved. There are now two dominant players among integrated steel mill companies in the United States and Canada, and two clear market leaders among the minimill producers.

The recovery of pricing power in the domestic industry may have been attributable to industry consolidation, as well as to rising global demand spurred, in large part, by China. The establishment of industry pricing power, plus the rise of global demand, higher steel prices, and the falling exchange rate of the dollar, also made establishment of new production facilities in the United States a more attractive proposition. After removal of the safeguard measures, steel prices generally moved upward through August 2008, when the benchmark price of hot-rolled steel reached nearly \$1,200 per metric ton (MT)—up from \$222 per MT in 2002.

Starting in September 2008, the global economic crisis caused a decline in steel demand, falling prices, and reduced production. Like many other industrialized countries, the impact of the market downturn was felt by all the major steel consuming sectors in Canada (as well as the United States)—automotive, construction, manufacturing, appliance, and energy. Furthermore, given the overall difficult economic environment, the steel export market was also lackluster.

During the first half of 2009, the overall capacity utilization rate in U.S. steel mills lingered in the low to mid-40% range. By 2009, U.S. crude steel production dropped more than 36% from the 2008 production level to 58 million metric tons, with steel mills running at a capacity utilization rate slightly over 50%. In early 2009, U.S. Steel shut down or heavily curtailed production at a number of its plants in the United States.

Canadian steel production also experienced a sharp drop in 2009, to approximately 9 million MT of crude steel, nearly 40% less than the 15 million MT produced in 2008. In 2009, the steel-making capacity utilization rate in Canada was about 43%. U.S. Steel moved to idle much of its Canadian operations in March 2009, largely because of low demand for steel. Affected U.S. Steel plants in Canada included the flat-rolled steel plant in Hamilton, Ontario, known as Hamilton Works, and Lake Erie Works in Nanticoke, Ontario. U.S. Steel met strong resistance from the Canadian government and the local United Steelworkers union (USW), which raised questions about why more facilities in Canada were affected than in the United States. On May 5, 2009, Canadian Minister of Industry Tony Clement sent a “demand letter” to U.S. Steel under Section 39 of the Investment Canada Act, asking the company to comply with its alleged contractual commitments:

When U.S. Steel acquired Stelco Inc. in 2007, it committed to a series of undertakings regarding, among others, capital expenditures, research and development and production. I am concerned by the actions of U.S. Steel in cutting operations in Canada and by the impact this has on its workers. While I recognize that these are challenging economic times, we expect the company to live up to its commitments.

A demand letter is the first step in the enforcement process under the Investment Canada Act. If a company is found in violation of the act, it could be forced to sell its Canadian operations or pay fines of C\$10,000 per day (roughly US\$10,000). In July 2009, after reviewing U.S. Steel’s response, the Canadian government took U.S. Steel to the Federal Court of Canada, asking the Court to order appropriate measures to remedy the situation.

In 2010 and 2011, the steel sector in the United States and Canada showed measurable recovery from the previous years, but production level and capacity utilization were still below 2007 levels. Canadian annual steel output was approximately 13 million MT in 2010, as well as in

2011, lingering at a capacity utilization rate of 62%. Utilization rate in the U.S. steel sector was 70% in 2010 and 74% in 2011.

Status of the Issue

U.S. Steel moved to file a challenge to the Investment Canada Act (ICA) in November 2009, claiming that certain provisions of the law violated its constitutional rights. Among them is the stipulation that companies that fail to comply with promises made under the ICA must pay fines or must divest their assets, but are not given a chance to mount a proper defense. U.S. Steel also argued that the penalty of C\$10,000 a day was akin to criminal punishment. The Canadian government is seeking the dismissal of U.S. Steel's challenge and "is trying ... to force U.S. Steel to either operate its Canadian assets or sell them to a party that will operate them."

On April 15, 2010, U.S. Steel and USW Canadian local union 8782 reached a three-year labor agreement for employees at U.S. Steel Canada's Lake Erie Works. The deal will allow U.S. Steel to restart production at the facility based on improving steel demand. Production at Hamilton Works had restarted earlier.

On April 28, 2010, U.S. Steel Canada announced that it has entered into an agreement to sell its bar mill and bloom and billet mill at its Hamilton Works to Max Aicher (North America) Inc., a wholly-owned subsidiary of Max Aicher GmbH & Co. KG of Germany. Max Aicher had previously entered into talks to purchase the bar and bloom mills in 2007, prior to their purchase by U.S. Steel. Max Aicher (North America) Inc. officially took ownership of the bar and bloom mills in November 2010.

In June of 2010, the Federal Court of Canada ruled in favor of the Canadian government, upholding a portion of the Investment Canada Act being challenged by U.S. Steel as unconstitutional. U.S. Steel subsequently appealed the decision. On July 26, 2010, a federal appeals judge in Canada ruled that the case by the Canadian government against U.S. Steel can proceed. This marks the first time in history that the Canadian government has sued a company for not living up to employment and production promises made earlier in exchange for federal approval of a foreign investment.

On November 7, 2010, about 900 workers were locked out of U.S. Steel Canada's plant in Hamilton, after labor negotiations over issues such as pensions had made little progress. On June 8, 2011, The workers represented by the USW local union 1005 in Hamilton, Ontario, moved to block the Burlington Canal Lift Bridge leading into the city's port in an effort to prevent two vessels carrying steelmaking coke from leaving the area. The locked-out U.S. Steel workers later left the port after a Canadian court issued injunctions against the union on June 10, 2011. On October 15, 2011, U.S. Steel and Local 1005, which represents union workers at Hamilton Works, reached a new three-year labor contract and has since resumed operations.

In November 2011, the Supreme Court of Canada declined to hear U.S. Steel's contention that laws governing investments in Canada are unconstitutional, upholding rulings previously made in lower courts.

On December 12, 2011, the Canadian government and U.S. Steel came to an agreement. According to the agreement, U.S. Steel has committed to continue operations in Canada until 2015, with \$50 million in capital investments above its original undertaking of \$200 million and a contribution of \$3 million toward community programs in Hamilton and Nanticoke.

Questions

1. To what extent can American investors be assured that economic and market conditions that affect their Canadian businesses will not be subject to legal action under the Investment Canada Act?
2. Do you believe that the Investment Canada Act is working appropriately? Does the perception that an act regulating foreign investment and business operations is a tool of industrial policy cause you any concern?
3. With the significant restructuring of the North American steel sector after 2002, the collapse of global steel markets in 2008 and 2009, and the slow recovery in 2010 and 2011, should the U.S., Canadian, and Mexican governments begin discussions on a common steel policy that will protect the North American market from import surges?
4. In light of the trade actions brought by the United States and other parties against China's export restrictions on raw materials such as rare earths, tungsten, coke, magnesium, and zinc (some of which are important to steel production), what is Canada's position? Should the North America Free Trade Agreement (NAFTA) countries work to secure supply of raw materials that are crucial to industrial production?

Intellectual Property Rights⁸⁰

Issue Definition

The United States contends that Canada's protection and enforcement of intellectual property rights (IPR) are inadequate and do not meet international standards. Protection and enforcement of IPR are important to bilateral relations because of the high levels of trade between the two countries. U.S. stakeholders have expressed concern about the levels of counterfeiting and piracy in Canada, as well as the transit of IPR-infringing products across Canada's borders. Areas of bilateral engagement on IPR include Canada's efforts to reform its copyright regime and IPR enforcement system.

Background and Analysis

Canada and the United States have entered into a range of international commitments on IPR. Bilateral commitments on IPR exist in the North American Free Trade Agreement (NAFTA). As members of the World Trade Organization (WTO), both countries are signatories to the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement), which sets standards for IPR protection and enforcement. Both countries also have ratified the World Intellectual Property Organization (WIPO) Copyright Treaty and WIPO Performance and Phonograms Treaty (the "WIPO Internet treaties"), which focus on IPR protection and enforcement in the digital environment. Canada ratified the WIPO Internet treaties in 1997, but

⁸⁰ Prepared by Shayerah Ilias, Analyst in International Trade and Finance, Foreign Affairs, Defense, and Trade Division.

remains one of few developed countries that has not brought its laws into compliance with the treaties. The United States implemented the WIPO Internet treaties in 1998 through the Digital Millennium Copyright Act (DMCA) (P.L. 105-304).

In addition, Canada and the United States were among the nearly 40 countries that negotiated the Anti-Counterfeiting Trade Agreement (ACTA), a new international IPR agreement which would build on the TRIPS Agreement. ACTA negotiations were concluded in 2010. The ratification (“formal approval”) of the ACTA is in a state of uncertainty, despite the fact that most negotiating parties (Australia, Canada, the EU and 22 member states, Japan, South Korea, Morocco, New Zealand, Singapore, and the United States) have signed the proposed agreement. In recent months, controversy over the ACTA has escalated in the EU, where several member states (including some that had previously signed the agreement) have decided to suspend or not initiate their domestic adoption of the ACTA. The ACTA would enter into force after the sixth instrument of ratification, acceptance, or approval is deposited by ACTA negotiating parties. No party has submitted a formal instrument of approval to date.

One key area of U.S. concern is Canada’s domestic copyright regime. The Canadian government periodically has attempted to overhaul its domestic copyright regime to bring its domestic law in line with international standards, including the WIPO Internet treaties. Some copyright-based industry and other groups assert that Canada does not sufficiently combat online piracy or the circumvention of technological measures that protect copyrighted works. Others, including consumers and Internet service providers (ISPs), call for greater exceptions to copyright for educational, research, and other purposes to promote the free flow of information and innovation. Some stakeholders have opposed efforts to revise Canada’s copyright law on the basis that such changes may reflect U.S. DMCA-style laws that they believe excessively limit the rights of users of copyright works.

On September 29, 2011, the Canadian government introduced the Copyright Modernization Act (Bill C-11), in the 1st session of the 41st Parliament. A committee report on the bill, as amended, was presented on March 15, 2012. Bill C-11 is a reintroduction of Bill C-32, which was introduced in the 40th Parliament and failed to advance before the dissolution of that Parliament. Among its provisions, Bill C-11 would:

- incorporate the WIPO Internet treaties into domestic law;
- introduce provisions prohibiting the circumvention of technological protection measures (“digital locks”);
- clarify the roles and responsibilities of ISPs for the copyright infringements of their subscribers;
- include a “notice and notice” provision (a copyright holder notifies the ISP that a subscriber has made available or accessed content without authorization, and the ISP passes on the notification to the subscriber, but takes no subsequent action to remove the content);
- permit the copying of legally obtained content onto other devices provided it does not circumvent digital locks (“format shifting”);
- provide expanded “fair dealing” exceptions—a concept similar to “fair use” in the United States—for education use, parody, and satire; and

- lower statutory damages in cases of non-commercial infringement from \$500-\$20,000, as in current Canadian law, to \$100-\$5,000.

The debate about copyright reform in Canada has been heightened with legislation introduced in the United States in the 112th Congress—the Preventing Real Online Threats to Economic Creativity and Theft of Intellectual Property Act (PROTECT IP Act, S. 968), Stop Online Piracy Act (SOPA, H.R. 3261), and Online Protection and Enforcement of Digital Trade Act (OPEN Act; S. 2029, H.R. 3782)—to tackle online piracy issues similar to some of those addressed by the ACTA. Following protests by civil society groups and several Internet-based companies, congressional consideration of these bills has been postponed.

Another key area of bilateral engagement is Canada’s enforcement of IPR. Presently, the Canada Border Services Agency (CBSA) is not authorized to seize products at the border that are believed to be pirated or counterfeit without a court order, which requires detailed information. The United States contends that this lack of *ex-officio* authority limits the effectiveness of IPR enforcement in Canada. The United States also contends that the enforcement penalties imposed by Canada do not serve as sufficient deterrents for future IPR infringement.

Canada’s IPR protection and enforcement remain an ongoing area of concern for the United States. In 2011, the Office of the U.S. Trade Representative (USTR) continued to place Canada on its Special 301 “Priority Watch List” (PWL), a designation of criticism for a country’s inadequate IPR protection and enforcement. The USTR cited ongoing issues with Canada’s copyright reform and IPR enforcement efforts at the border. The USTR first placed Canada on the PWL in 2008. Canada previously had been on the “Watch List,” the mildest category of criticism for a country’s IPR regime, since 1985. Some supporters of Canada’s IPR regime assert that the Special 301 process is overly industry-driven and that Canada’s piracy rates are significantly lower than those of other countries on the PWL in 2011 (China, Russia, Algeria, Argentina, Chile, India, Indonesia, Israel, Pakistan, Thailand, and Venezuela). Some industry groups maintain that Canada’s placement on the PWL accurately reflects inadequacies in Canada’s IPR regime. The United States and Canada remained engaged on key bilateral IPR issues.

Status of the Issue

Canada could have to pass new laws in order to implement the enforcement standards of the ACTA, including granting *ex-officio* authority to customs officials to initiate criminal investigations in cases of trademark infringement and copyright piracy and providing legal remedies for circumventing technological protection measures. Canada’s possible revision to its domestic copyright law could help it to meet some of the ACTA standards related to IPR in the digital environment. The Parliament may act on Bill C-11 in the coming months. Bill C-11 is subject to two votes in the House of Commons, and if passed, will be submitted to the Senate for consideration.

Questions

1. What issues have arisen in developing legislation to implement the WIPO Internet treaties? What is Canada’s vision of a fair and balanced copyright law? What are key issues in the Parliament’s consideration of Bill C-11? How could Canada’s implementation of the WIPO Internet treaties differ from the DCMA?

2. What steps has Canada taken to promote international protection and enforcement of IPR? What are the opportunities and challenges that Canada sees in the proposed ACTA? What is Canada's status with respect to ratification of the ACTA? What changes to Canada's laws, if any, would be required for implementation of the ACTA?
3. What measures is Canada currently taking to address trade and transshipment of pirated and counterfeit goods? What steps can Canada undertake to improve IPR border and domestic enforcement? What can the United States do to assist Canada in improving IPR enforcement?
4. How does Canada view the U.S. Special 301 process? How does the Special 301 process and Canada's continued placement on the Priority Watch List affect bilateral relations? If passed, to what extent might Bill C-11 affect Canada's placement on the Special 301 list?

Electric Reliability, Trade, and Access to Renewable Power⁸¹

Issue Definition

The electric power grids of the United States and Canada are physically connected. Consequently, electric power reliability problems can easily cross the international border. This was demonstrated by the 2003 power blackout, which originated in Ohio and eventually spread into eastern Canada and the northeastern United States. The United States and Canada are therefore mutually dependent for the reliable operation of their common electric power systems. The interconnected grid also creates opportunities for trade and joint expansion of the use of renewable power.

Background and Analysis

There are three components of electric power delivery: generation by power plants, transmission over long distances by high voltage power lines, and final delivery at low voltage by distribution lines. The transmission lines that constitute the North American power grid cross state and international boundaries. The U.S. and Canadian grids are, in fact, inextricably linked:

- At the broadest level of organization, the North American grid is divided into regional "interconnections" within which power moves freely (the links between the regions are very limited). The large Eastern and Western Interconnections cover most of the contiguous United States and the heavily populated regions of Canada.
- At the level of major transmission lines, the Canadian grid has evolved by building south from heavily populated areas to connect with U.S. generation and load. Consequently, while the grid in the conterminous United States is a web crisscrossing the lower 48 states, the Canadian backbone system consists of north-south lines closely linked to the United States. More electricity actually

⁸¹ Prepared by Richard Campbell, Specialist in Energy Policy; Resources, Science, and Industry Division.

- moves north and south between the United States and Canada than east and west among Canadian provinces.
- In terms of system reliability, as discussed further below, the North American Electric Reliability Corporation (NERC) has responsibilities for the reliable operation of the power grid in both countries. Three of the eight regional reliability entities through which NERC performs much of its work extend from the United States into Canada and cover that nation's entire southern tier.

Reliability

In reaction to the 2003 blackout, the Energy Policy Act of 2005 (P.L. 109-58) required the Federal Energy Regulatory Commission (FERC) to designate an Electric Reliability Organization (ERO) charged with ensuring the reliability of the bulk power system, largely by issuing mandatory reliability standards. In 2006 FERC selected NERC for this role (NERC is an industry organization whose reliability recommendations had been voluntary prior to its designation as the ERO). NERC's members include Canadian power companies and it has memoranda of understanding (MOUs) with Canadian provinces and the Canadian federal government to help coordinate reliability activities. However, NERC does not have the same statutory authority in Canada as in the United States. The MOU between the Canadian National Energy Board (NEB) and NERC recognized NERC as the ERO for the Canadian part of international transmission lines but not for lines located entirely within Canada's borders (which are under provincial, not federal, regulation). NERC currently has agreements with most Canadian provinces that make, or will make in the future, NERC's reliability standards mandatory and enforceable. NERC's standards also cover critical infrastructure protection (including measures to enhance the cybersecurity of the grid).

Authorities in both Canada and the United States are monitoring space weather. The Sun is entering an especially active period for solar storms. Northern latitudes are more susceptible to extreme space weather caused by solar storms. These storms could induce geomagnetic induced currents which can adversely affect bulk power system components like transformers, or cause voltage instability and power system collapse.

Transmission capacity and congestion issues that can impair reliability and increase power costs exist in the United States and Canada, and the solution is often to construct new transmission capacity or enhance existing facilities. Many transmission projects are under construction or planned in both nations. However, transmission planning and construction in the United States and Canada face similar challenges, particularly for long-distance projects. These challenges include permitting and siting approvals that often involve multiple jurisdictions, and finding the funding for the large investments in transmission (and power generation) that will be needed to meet demand growth. Two international transmission projects of note include

- The Montana-Alberta Tie Line project (expected to be completed in 2012) will be the first transmission link between that state and province. This is a 214-mile, US\$213 million project that is expected to facilitate the export of wind power from both regions and improve transmission system reliability. The project received a US\$161 million loan under the American Recovery and Reinvestment Act.
- A proposed high capacity transmission line to ship up to 1,200 megawatts of hydroelectric power from Québec to New England. Although this project has

received preliminary approval from the U.S. Federal Energy Regulatory Commission, its future is uncertain because declining power prices in the United States (linked to low natural gas prices) may make the project uneconomical for the Canadian partner in the venture, the large utility Hydro-Québec.

Another Canadian project, the Northwest Transmission Line planned for northern British Columbia, may eventually connect southeastern Alaska to part of the Canadian power system.

Trade and Renewable Energy Development

The United States is a net importer of electricity from Canada, and imports had been increasing, from 42.7 terawatt-hours (Twh) in 2006 to 50.3 Twh in 2007 and 56.0 Twh in 2008. But imports have decreased recently with 51.8 Twh in 2009 to 44.4 Twh in 2010. From the U.S. perspective, while these imports can be locally important (e.g., in New York and New England), on a national basis they are very small, equivalent to 1.1% of net U.S. electric power generation (4,125 Twh) in 2010. Electricity trade is more significant from Canada's standpoint. Canada generated 589 Twh of electricity in 2010. Exports to the United States represented 7% of Canada's domestic generation.

The United States relies on coal for about half its electricity production, while Canada derives about 75% of its electricity from non-fossil fuel sources (i.e., hydropower, nuclear, and wind energy). Electricity trade between the countries is likely to become intertwined with renewable energy development and transmission planning issues. Both nations currently have policies for the increased use of renewable power. The United States and Canada have established a "Clean Energy Dialogue" (CED) to facilitate the development of low carbon energy sources. Elements of the CED include, among other things, collaboration on expansion and modernization of the North American transmission grid to improve reliability and facilitate trade in low carbon power; advancement of smart grid technology; and development of electricity storage technology.

Canadian sources of renewable power may have the potential to reduce the need to build new, long-distance transmission projects (which can take up to a decade or more to permit and construct) in the United States. For example, imports of hydropower from Québec into New England and New York, using new but relatively short power lines, have been suggested by the transmission system authorities in those regions as an alternative to building power lines to Midwestern wind farms. However, as discussed above, one of these projects has been thrown into question by declining natural gas and power prices. Disputes at the state or provincial level can also complicate energy project development. The potential development of new gas resources (i.e., from coal bed methane and tight shale formations) in both the United States and Canada could have a major impact on technology and energy choices in both countries.

In the United States, the intersecting issues of renewable power development, transmission system expansion and reliability, and long-standing difficulties in multi-state permitting of new projects, has spurred suggestions for new regulatory and planning processes. The planning element of some proposals envisions creating transmission "master plans" on a wide geographic scope to facilitate renewable energy development and other purposes. While these proposals are limited to planning within the United States, they will inevitably have an impact on Canada because of the grid connections and the much larger size of the U.S. power system.

Status of the Issues

NERC and FERC are continuing a process of developing and implementing mandatory reliability standards for the grid, with cybersecurity a growing concern. In Canada, the National Energy Board is reportedly working with provincial authorities on implementation of mandatory reliability standards, although it is not clear if in all cases these will be the same as the NERC standards or whether NERC will function as the ERO in every province.

Questions

1. Will all Canadian federal and provincial regulators approve and enforce NERC electric reliability standards? Without identical standards in the United States and Canada, the reliability of the electric power system could be reduced.
2. Given that the United States and Canadian power grids are integrated, what steps should be taken to coordinate transmission planning and development of smart grid protocols? Is this an area for NERC to establish a formal leadership role?
3. To what degree is Canada interested in increasing exports of renewable power to the United States, rather than reserving these resources for domestic consumption?
4. How can the United States and Canada effectively resolve energy development issues that may involve both federal and state/provincial authorities? Given the likelihood for increasing energy integration, should a formal bi-national body be instituted to oversee energy trade and energy security issues?

U.S. Energy Security and Canadian Oil Sands⁸²

Issue Definition

Canada ranks as the United States' number one source of imported crude oil and thus plays an important role in U.S. energy security. Canada's oil sands make up an increasing proportion of its petroleum resources, and Canada's oil sands producers continue to look primarily to the United States as the major market for their oil exports. Of the approximately 2.3 million barrels per day (mbd) of crude oil Canada has exported to the United States during 2012, over 50% is delivered to the Midwest. This region's current capacity to process increasing volumes of Canadian crude oil is limited in the near term. However, planned refinery expansion coupled with new refinery and infrastructure construction, may place the region in a position to receive increased oil exports from Canada in the longer term. Another possibility for processing additional Canadian oil is expanded capacity in refineries along the U.S. Gulf coast, which is also likely to require new pipeline construction.

Although U.S. refinery capacity is forecast to increase from 17.7 mbd in 2011 to nearly 19.0 mbd in 2030—a 1.3 mbd increase, the deteriorating economics of the refining industry may bring these

⁸² By Robert Pirog, Specialist in Energy Economics, Resources, Science, and Industry Division.

projections into question. Since 2009, the U.S. refining industry has been characterized by plant closures and divestiture. Actual, as well as projected, capacity expansion may not be enough to keep up with Canada's projected increase in oil sand production, especially if the investment climate continues not to warrant expansions to include upgrades for heavy oil processing. Canada is also pursuing additional refinery capacity for its heavier oil. Refinery expansions based on the use of heavy oils will have environmental effects, and Congress will likely continue to face controversy over the balance between energy security and the environment. In addition, investment and production plans are likely to be altered by the reduced demand for petroleum products in the United States, associated with high prices and the ongoing effects of the economic recession that began in the last quarter of 2007.

Another possible impediment to expanded Canadian oil use is Section 526 of the Energy Independence and Security Act of 2007 (P.L. 110-140) which prohibits federal procurement of an alternative or synthetic fuel "unless the contract specifies that the lifecycle GHG emissions are less than or equal to such emissions from the equivalent conventional fuel produced from conventional petroleum sources." The provision is intended to ensure that federal agencies are not spending taxpayer dollars to promote new fuel sources that will exacerbate global warming, and would apply to fuels derived from "oil sands," which are currently associated with producing higher greenhouse gas emissions than fuels derived from conventional, lighter crude oils.

Background and Analysis

When it comes to future oil supplies, production from Canada's oil sands will likely make up a larger share of U.S. oil imports. Oil sands account for nearly 50% of Canada's total oil production, and oil sand production is increasing as conventional oil production declines. Since 2004, when production from a substantial portion of Canada's oil sands were deemed economic, Canada has been ranked second behind Saudi Arabia in proved oil reserves. Canada has over 175 billion barrels of reserves and a total of over 300 billion barrels of potentially recoverable oil sands (an attractive investment under high oil price conditions, demonstrated by the billions of dollars already committed to Canadian development). Canadian crude oil exports (from oil sands and conventional petroleum sources) were over 2 mbd in 2011, of which 99% went to the United States. Canadian crude oil accounts for about 25% of U.S. crude oil imports, and about 19% of all U.S. crude oil and petroleum products supplied. U.S.-based oil companies are major investors in Canadian oil sands. The infrastructure to produce, upgrade, refine, and transport oil from Canadian oil sand reserves to the United States is already in place although additional pipeline capacity is planned. Oil sands production is expected to rise to 3.6 mbd by 2030.

Greenhouse gas "emissions intensity" (CO₂/barrel) from oil sands are significantly higher than that from conventional oil production. Canada's federal government classifies the oil sands industry as a large industrial air pollution emitter and expected it to produce half of Canada's growth in greenhouse gas (GHG) emissions in 2010. Reducing air emissions is one of the most serious challenges facing the oil sands industry. Between 1995 and 2004, the oil sands industry reduced its emission intensity by 29% while oil production rose. Overall, CO₂ emissions have declined from 0.14 tons/barrel (bbl) to about 0.08 tons/bbl since 1990. However, Alberta's GHG goals of 238 megatons of CO₂ in 2010 and 218 megatons CO₂ in 2020 are not expected to be met.

Status of the Issue

New refinery capacity that would accommodate heavier crude from Canadian oil sands is being challenged in Indiana, Michigan, South Dakota, and elsewhere. Some of these expansions or new refineries are several years away from operation. A BP refinery upgrade and expansion in Whiting, IN, expected to be completed in 2011, is progressing, but faces lawsuits from environmental groups. A new \$10 billion refinery in Union County, SD, being planned to process heavy crude from oil sands, would be the first new refinery in the United States in over 25 years. Environmental groups continue to promote standards for low-carbon emission fuel and oppose the permitting of these refinery projects on the basis that processing heavy crude from Canadian oil sands would generate much higher greenhouse gas emissions than from conventional petroleum sources.

Another impediment to expanded use of Canadian heavy oil in refineries in the United States is the opposition to the construction of the Keystone XL pipeline, which is designed to deliver up to 900,000 barrels per day of Canadian crude oil to new refining capacity that is expected to be built in the U.S. Gulf Coast region. Opposition to the project in the United States centers on the inherently high carbon emissions of liquids derived from oil sands, while Canadian opposition is focused on likely job losses associated with the export of unprocessed crude oil. Unions in Canada claim that processing the crude oil in Canada, and exporting finished products like gasoline and diesel fuel to the United States, would create thousands of high-paying jobs for Canadian workers.

Questions

1. What changes are necessary to significantly reduce the environmental footprint of heavy oil from Canadian oil sands?
2. How much capital investment in pipeline and refinery infrastructure is needed to support increased crude oil imports from Canada?
3. What would be the impact on U.S. federal and defense fuel procurements if Section 526 restrictions remain in place on fuel produced from Canadian oil sands?
4. As a result of the supply bottlenecks and resultant price discounts on Canadian crude oil, how likely is it that Canadian oil sands development will be slowed because of revised investment strategies by the major oil companies?

Keystone XL Pipeline⁸³

Issue Definition

In September 2008, TransCanada (a Canadian company) applied to the U.S. Department of State for a permit to cross the U.S.-Canada international border with the Keystone XL pipeline project.

⁸³ Prepared by Paul Parfomak, Specialist in Energy Policy; Resources, Science, and Industry Division.

If constructed, the pipeline would carry crude oil produced from the oil sands region of Alberta, Canada, to U.S. Gulf Coast refineries. Because the pipeline would connect the United States with a foreign country, it requires a Presidential Permit issued by the State Department. Although similar pipelines from Alberta have been approved in recent years, the permitting process for the Keystone XL pipeline has become highly controversial. Some Members of Congress have expressed support for the proposed pipeline's potential energy security and economic benefits while others have expressed reservations about its potential environmental impacts. Though Congress, to date, has had no direct role in permitting the pipeline's construction, it may have an oversight role stemming from federal environmental statutes that govern the pipeline's application review process. Congress also may seek to influence the State Department permitting process, or may seek to assert direct congressional authority over permit approval, through new legislation.

Background and Analysis

In 2010, Canada was the largest supplier of imported petroleum to the United States. Of the 11.4 million barrels per day (Mbpd) the United States imported last year, Canada supplied 2.7 Mbpd (24%), more than the combined imports from the next two largest suppliers—Mexico and Saudi Arabia. Pipeline infrastructure for Canadian petroleum exports to the United States has been growing rapidly in support of this trade. Five major pipelines with a combined capacity of 3.3 Mbpd currently link Canadian petroleum producing regions to markets in the United States. Two of these pipelines, Alberta Clipper and Keystone, with a combined capacity of just under 0.9 Mbpd (26% of the total) began service in 2010.

The permit for Keystone XL, which would add an additional 0.8 Mbpd of import capacity, was denied by the U.S. State Department in January 2012. However, TransCanada subsequently announced that it would proceed with development of the Keystone XL segment connecting Cushing, OK, to the Gulf Coast as a stand-alone project not requiring a Presidential Permit. The company also informed the State Department that it intended to file a new Presidential Permit application for the remaining cross-border segment of the Keystone XL project from the Canadian border through Nebraska. If ultimately approved and constructed, Keystone XL would bring Canada's total U.S. petroleum export capacity to over 4.1 Mbpd, enough capacity to carry over 35% of U.S. petroleum imports in 2011. Given that Canada actually supplied the United States 2.7 Mbpd in 2011, large increases in Canadian supply will ultimately be possible, although the industry anticipates significant excess pipeline capacity for the next decade. In addition, several large pipeline projects are proposed within the United States to increase movements of Canadian petroleum to and from key U.S. market hubs, including refineries in the Midwest and on the Gulf Coast that employ complex technology in order to process "heavy" crude oils like those from Canada, Mexico and Venezuela.

The recent expansion of petroleum pipelines from Canada, particularly Keystone XL, has generated considerable controversy in the United States. Proponents of the pipeline, including Canadian government agencies, petroleum industry stakeholders, and pipeline construction workers, have based their public interest justifications primarily on increasing the diversity of the U.S. petroleum supply and on expected economic benefits to the United States, including near-term job creation associated with pipeline construction and operation. Some contend that the Keystone XL project would secure growing Canadian oil supplies for the U.S. market, which could offset imports from less dependable foreign sources. They also claim that if oil sands output cannot flow to the United States, infrastructure to export it to Asia will likely develop. Opponents to the Keystone XL pipeline project, primarily environmental groups and affected communities

along the route, object to the project principally on the grounds that it supports “dirty” Canadian oil sands development, that a potential spill could pose a risk to groundwater, that alternative pipeline routes avoiding environmentally sensitive areas in Nebraska have not been fully considered, and that it promotes continued U.S. dependency on fossil fuels. Arguments criticizing the greenhouse gas emissions of oil sands production, generally, are based to some degree on the assumption that limiting pipeline capacity to U.S. markets may limit output from Canada’s oil sands. Some opponents also argue that, given the excess capacity anticipated in the existing Canadian petroleum pipelines noted above, additional pipelines are not needed.

Status of the Issue

On January 18, 2012, the State Department, with the President’s consent, denied the original Keystone XL permit, citing insufficient time under a 60-day congressional deadline to obtain all the necessary information to assess the project. On February 27, 2012, TransCanada announced that it would proceed with development of the Keystone XL in two segments as stated above. The company intends to file a new Presidential Permit application “in the near future” for the northern segment of the Keystone XL project, with a future supplement to the application specifying an alternative route in Nebraska when that route is finalized. The company has previously stated that it expected to establish the new route by October 2012.

The Obama administration has lent its support for TransCanada’s plan to proceed with the southern segment of the Keystone XL pipeline, while reserving judgment on the reconfigured northern segment until completion of a new Presidential Permit review. A final State Department decision on a re-filed permit application appears unlikely before 2013, however. Congress may act to influence this decision in the meantime. The North American Energy Access Act (H.R. 3548) would transfer the permitting authority over the pipeline to the Federal Energy Regulatory Commission, requiring the commission to issue a permit for the project within 30 days of enactment. The Keystone For a Secure Tomorrow Act (H.R. 3811) would immediately approve the original permit application. S. 2041. The Energizing America through Employment Act (H.R. 4000) would also approve the original permit upon passage. All four bills include provisions for later alteration of the pipeline route in Nebraska. S. 2100 would suspend sales of petroleum products from the Strategic Petroleum Reserve until issuance of a Presidential Permit for the Keystone XL project. H.R. 3900 would seek to ensure that crude oil transported by the Keystone XL pipeline, or resulting refined petroleum products, would be sold only into U.S. markets.

Questions

1. Will the State Department approve the reconfigured Keystone XL pipeline?
2. How might the development of the Keystone XL pipeline affect the regional availability and price of petroleum products in North America?
3. What are the prospects for new Canadian pipelines to Pacific markets and how might the Keystone XL pipeline affect those?
4. Would the Keystone XL pipeline, added to the other recently constructed oil pipelines from Canada, require special safety or environmental oversight?

5. How might oil supplies from the Keystone pipeline affect U.S. oil imports from other countries?
6. What could be the nature and timing of regional economic affects associated with the pipeline's construction?

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