

Cato Institute Policy Analysis No. 105: The Canada-U.S. Free Trade Agreement: Now or Never

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Executive Summary

Before moving to Washington in June 1987, my family lived in Quebec's Eastern Townships, about 12 miles from the Vermont border. To us, the adjacent communities of Rock Island, Quebec, and Derby Line, Vermont, were constant testimonials to the inefficiencies of barriers to choice. The larger community (population 5,000), in high-tax, high-tariff Canada, is almost entirely bereft of shops and service stations; the Canadian side of its only factory (which straddles the border) is vacant despite the available work force, a near majority of which receive generous provincial welfare payments. In the smaller U.S. village (population 800), stores and gas stations cater to Quebec residents who brave fines at random Canada Customs inspections. Since customs officers are particularly nasty about imported alcohol, the Régie des alcools du Québec (Quebec Liquor Commission) outlet in Rock Island does a thriving business selling mediocre domestic wines at inflated prices. High-quality California wines, available across the border at low prices, are nowhere to be seen in Rock Island because of discriminatory commission markups of up to 1,000 percent.

A continent away, southwestern British Columbia has been hurt by the departure, to the U.S. border town of Sumas, Washington, of four manufacturers of cedar shakes. The cause of the uprooting of these companies is U.S. protectionism--a hefty 35 percent tariff imposed, without any economic basis, by the Reagan administration on shake and shingle imports.(1) "We built a brand new treating plant in Abbotsford [British Columbia] and spent a couple of million on it," said the president of one of the companies. "Then, bingo, a year later there is a 35 percent tariff. You're talking about saving a couple of extra million dollars a year because of the move. We only had two choices. One was to shut down.

... The other was to move to the United States."(2)

Mutually impoverishing distortions such as these highlight the importance of the Free Trade Agreement (FTA) that was hastily initialed by the world's two largest trading partners on October 3 and finalized on December 11, 1987, and is now awaiting approval by the U.S. Congress and the Canadian Parliament. Canadian journals have been jammed with editorials (mostly unfavorable and usually simplistic) about the FTA, while U.S. magazines and newspapers have remained comparatively oblivious to it, despite U.S. Trade Representative Clayton Yeutter's recent claim that the agreement "is of comparable historic significance to the arms control agreement reached earlier [in December]".(3) Analysis reveals that effective lobbying has prevented the FTA from ushering in true free trade. Nevertheless, and despite the claims of detractors in both countries, the agreement is mutually advantageous. Unfortunately, its implementation in Canada is not guaranteed, due to psychological and constitutional factors that Americans have for too long ignored. The perilous state of the FTA in Canada necessitates positive congressional action on the implementing legislation that the Reagan administration and Congress will develop jointly.

The Historical Backdrop of Canadian-U.S. Trade Relations

In Canada the complex environment of Canadian-U.S. trade relations has historical roots as old as the country itself.

The British conquest of New France in 1760 was for a time imperiled by a dearth of Anglophone immigrants, a problem resolved only by an influx of loyalist refugees into what are now Quebec and Ontario during and after the American Revolution.⁽⁴⁾ Other colonists, immigrating from England and Scotland after the conquest to corner British North America's trade, greatly feared competition from New England entrepreneurs. From Canada's beginnings, then, substantial portions of its governing elite owed their status to the existence of staunch barriers with the United States. A century later, confederation consolidated an east-west commercial axis-- symbolized by the transcontinental railroad promised to British Columbia--that has always contrasted with more natural--that is, more efficient--north-south cultural and geographic pulls.⁽⁵⁾ The Fathers of Confederation, many of whom had a financial stake in the railroad (which was not viable if Westerners could buy goods from the United States), spoke unceasingly of the need to shield the country from pernicious U.S. influences.

In 1878 John A. MacDonald, Canada's first (and arguably most famous) prime minister, instituted a national policy of heavy tariffs--providing firm protection for, and encouraging sloth in, central manufacturers--that has essentially survived to this day. An attempt to abandon this conception of Canada was fatal to Wilfrid Laurier's Liberals, who were defeated in 1911 for having negotiated a reciprocity arrangement of lower duties with the United States. Subsequent efforts to free up trade were abandoned as too risky politically, at a relatively advanced stage of negotiations, by W. L. MacKenzie King's Liberals in 1948. Even Prime Minister Brian Mulroney, campaigning for the leadership of the Progressive Conservative party in 1984, declared that "free trade affects Canadian sovereignty and we will have none of it, not during the leadership campaign or at any other time."⁽⁶⁾

As this brief summary implies, there endures in Canada's political culture an important strain of existential angst that is not adequately conveyed by the facile observation that the country has only one-tenth the population of its southern neighbor. Other nations--including Denmark, Belgium, Luxembourg, and Austria--thrive on free relations with larger countries next door. The subconscious Canadian image--paradoxical for a country for which almost all citizens, including this author, have strong positive feelings--seems simply to be that its citizens would lose their will to maintain the nation if they were allowed freedom in their consumption decisions. Speeches by the Liberals' official opposition leader, John Turner (a recent convert to the anti-free-trade movement), and by socialist New Democrat head Ed Broadbent quite plainly contend that economic coercion is a public good in Canada--that a "Canadian way of life" prized by all necessitates government shelter from foreign temptations. Their insinuated folksy image of an insecure, better-off- in-their-ignorance Canadian family was illustrated this way by commentator Charles Gordon:

Think of it as a family. Here's Dad. He looks like something out of a magazine ad for Export cigarettes. He wears a tartan shirt, sits in a canoe and has a pipe in his mouth. Mom cooks lunch for the children, who come home from school, and they all listen to The Happy Gang. If they have a television, they watch the CBC most because it comes in the clearest. American stations just across the border--in Watertown, Duluth, Buffalo, Minot --don't always come in well. When the adults manage a glimpse of the Tournament of Roses Parade . . . they feel a sense of living in a country foreign from the one they see on their television screen.

Once a year these Canadians pile into the Meteor, a Canadian-made car something like a Mercury, and drive to the United States to load up on cheaper clothes in the latest styles. They lie a little bit about how much they bought when the man at the Canadian border asks them if they have anything to declare. They think there's more to buy and things are a bit more exciting on the American side of the border.

This family has an uncle who went to live in California and made it big. When he visits he brings terrific presents and joshes his relatives about their slower ways, their lower incomes, their costlier cars. The kids envy their uncle but, as they grow older, find that their dream of living like him fades away so gradually that they eventually forget they ever had it.⁽⁷⁾

This irrational but deeply rooted inferiority complex gives rhetorical force to statements that would seem nonsensical to any outsider with knowledge of price theory.⁽⁸⁾ Thus, the president of Canada's largest trade union congress seriously predicts that the FTA will cost the country 800,000 net jobs.⁽⁹⁾ Truckers claim that free trade would let "American

operators . . . make the short journey into Canada, drop off their load, and either return empty or pick up a full or partial load for a U.S. destination," but that the same deal would "give Canadian truckers far fewer opportunities in the U.S. market." (10) The litany of similar complaints is more than routine protectionist sentiment; it can be understood only in the historical context briefly sketched above.

That free trade would be in Canada's best economic interests is, of course, quite obvious both from a theoretical point of view and from applying conventional quantitative economic indicators. (11) Serious macroeconomic estimates see the benefit of free trade to Canada as approximately 4 percent of its gross national product, but the eventual figure could be much higher than that, both for technical reasons and also because dormant productive forces in Canada would most likely be stimulated by outside competition and outside markets. (12) The Canadian Department of Finance estimated in January 1988 that the FTA would result in a 10.5 percent increase in manufacturing output and a 3.5 percent increase in overall exports, as well as a general lowering of factor and consumer prices.

The economic advantages of dismantling tariffs have always existed. Advocacy of free trade in March 1985 by an elected politician who had forsworn it less than a year earlier is not so easy to explain. It can best be seen, it seems, as a product of serendipity:

-- When the Mulroney administration came to power in 1984, it enjoyed great popularity. Yet it promptly lost much of its support, through both inept management and assorted petty scandals and as a result of the furor surrounding the continuing decline in the value of the Canadian dollar (brought about, admittedly, by measures of the preceding Liberal government). This resulted in increasing interest and inflation rates and more expensive Florida winter vacations.

-- When the giant 1985 photo opportunity with President Reagan (now known as the Shamrock Summit) at Quebec City came, the need to create headlines and to heighten the prime minister's international profile was acute.

-- The free-trade rhetoric of the Reagan administration has in fact been accompanied by a menacing surge of U.S. protectionism, threatening Canada's largest export market. (13)

-- Finally, a prestigious and hugely expensive royal commission report on Canada's economic future, appearing just after Mulroney's taking office, endorsed free trade as the last best hope for realizing Canada's economic potential. (14) The report had been solicited by the Liberals before their 1984 defeat, and it had been written by a former Liberal cabinet minister. The clout and the political pedigree of this report took much wind out of the official opposition's sails.

On the U.S. side, where the political culture does not discourage free trade initiatives, good fortune was also present. Under 1979 and 1984 trade acts, bills implementing agreements with foreign countries may be submitted to Congress on a so-called fast-track basis (that is, they may be adopted or defeated but are not subject to "killer amendments") only if the Senate Finance Committee does not disapprove of this procedure within 60 days of official notification of ongoing talks. The Republican-dominated committee, after intense lobbying by several industries, failed to object to fast-track proceedings by a 10-10 vote in 1985. Today's Democratic Senate would almost certainly have rejected the fast-track technique, and this would have signified an abrupt end of the talks.

In both countries this story of past good fortune and present politico-cultural reality reinforces the feeling that it is now or never for the FTA.

General Highlights of the Agreement

The crux of the FTA is undoubtedly the gradual elimination of tariffs on movements of goods between the two countries. This would establish the countries as a free-trade area under the terms of article XXIV (8b) of the General Agreement on Tariffs and Trade and would shield both nations from accusations of discrimination in their treatment of foreign products. (15) The free-trade area would not be a common market (free movement of people is not sanctioned by the agreement) or a Common Market-like customs union; rather each nation would maintain distinct tariffs for goods and services from third countries. This requires a strict 50 percent origination quotient on cross-border transit, to prevent third parties from sneaking goods in through the back door. (16) Finally, and importantly, neither country

would abandon its social or fiscal policies; thus, Canada's welfare state would require high taxes to be levied on U.S. and Canadian goods alike. Canadians would still pay more for goods than Americans and would still be subject to checks at entry points (although they would pay only excise tax, not duties). The foundation of the FTA is simply that each government would treat goods coming from the other country as domestic goods.

The actual process would commence on January 1, 1989. It would be of disproportionate benefit to Canadian consumers since Canada's duties on U.S. goods are on average about twice as high as their U.S. counterparts.⁽¹⁷⁾ Tariffs on some goods (from computers to animal feed) would disappear immediately; most others (chemicals, pulp and paper products, and furniture, for example) would be phased out during a five-year period; a few (on most agricultural products, tires, textiles, and softwood plywood) would be eliminated over ten years, as both countries encouraged firms in politically sensitive industries to adapt to a more competitive environment.

Opponents of the FTA point out that about 75 percent of the goods crossing the Canadian-U.S. border already do so duty free; this figure, however, doesn't consider the huge benefit of trades that do not presently take place. Indeed, each country's government has traditionally protected selected industries from foreign competition: the United States in agriculture, and more recently in lumber products, Canada in textiles and appliances, for example. A loosening up of the market for goods would clearly be of mutual benefit. The risk of the 5- or 10-year adaptation period, of course, is that each country's sheltered industries will use the time to lobby for modifications (or abrogation) of the accord instead of becoming more competitive or simply reallocating their investments in the interim. (Additionally, any delay time will result in a clear loss of short-term mutual wealth to consumers in both countries.)

Several outright--including some outright silly-- exclusions of imports would be terminated, thanks to the agreement. Canadian residents would obtain the right to import used cars and airplanes from the United States (only 8-year-old cars in 1989, but cars of any age by 1994). Americans would at last be able to legally purchase lottery tickets north of the border.

More importantly, the Canadian government has surrendered the right to prohibit--or, equivalently, to fix above-market prices for--sales to the United States of oil, gas, and electricity by private firms or provincial agencies. This removes an important obstacle to U.S. energy security and greatly accommodates Hydro-Quebec, whose previous attempts to sell electricity in the United States were often thwarted by the National Energy Board's astounding requirement that Canadian energy not be sold in the United States at any price lower than that at which the customer could purchase it from alternate suppliers. Canada would also abandon its requirement that uranium be processed before export to the United States. Abandoning past tit for tat, the United States would no longer embargo enriched Canadian uranium. Canada would also be eligible to receive up to 50,000 barrels a day of Alaskan oil: sadly, though, the western shipping lobby has succeeded in requiring that this oil be shipped to the lower 48 states before being exported north to Canada.

Most, but not all, service industries are also covered by the FTA. The agreement provides for unimpeded flows of construction (including architectural and engineering), clerical, advertising, insurance, and real estate services, to name a few. At U.S. negotiators' insistence, however, U.S. transportation and basic telecommunications services remain shielded from efficient Canadian competition. And pressures by professional associations in both countries have denied free markets (that is, free cross-border movement of professionals, with relaxed licensing requirements) in legal, dental, and medical services.

The FTA continues the trend toward free financial services markets, but hardly advances it. Canadian banks will maintain access to interstate banking in the United States to the extent that state laws allow; U.S. banks already enjoy this privilege across Canada, where provincial banking restrictions would be unconstitutional. Following Canada's 1986 deregulation of its securities industry, the "little bang," banks (of whatever nationality) may trade in securities, but Canadian banks are bitter that the Glass-Steagall Act will continue to restrict their involvement in this activity in the United States. However, they will be allowed to market Canadian securities south of the border. And U.S. banks will still be unable to purchase more than 25 percent of any Canadian banking concern; nevertheless, since the agreement will allow them to do business freely in Canada, competition will in reality be unfettered.⁽¹⁸⁾

Who Loses?

Obviously, if freer trade ensues, consumers in Canada and the United States will be big winners. Correspondingly, of course, those who reaped monopolistic profits by denying Canadians or Americans freedom of choice will lose.

In several cases groups have lobbied successfully to obtain exemptions from the agreement. Among the more egregious cases are the following:

-- Canada's notoriously inefficient beer industry has received total shelter from the accord, thanks to an intensive (and embarrassing) domestic lobbying effort that sought to identify Canadian beer with national identity (remember the McKenzie brothers?).(19) This protection will prove difficult to remove piecemeal since the FTA provides that any modification of the rules on beer will trigger total free trade in that industry. This often unnoticed aspect of the agreement will make it harder for Ottawa and the provinces to achieve their intention of dismantling the infamous inter-provincial trade barriers without jeopardizing the protected beer industry.(20)

-- U.S. maritime transporters have sheltered themselves from Canadian competition. The infamous Jones Act, which provides that only U.S. ships may carry cargo between U.S. ports, survives the FTA intact, despite the negotiators' initial attempts to obtain its abrogation.

-- Atlantic Canada's fish processors have retained their immunity from New England rivals, in that no raw fish may be exported from this area.

-- U.S. producers of softwood lumber keep for 10 years the unwarranted protection recently obtained.

In all these cases, consumers in the so-called protected country--and producers in the other country--will lose.

But the glass is half full, not half empty: many inefficient barriers to trade have indeed gone by the wayside. Those who had constrained our choices will, of course, be losers here, but their loss will be dwarfed by gains to consumers. As an example, the inefficient Canadian wine industry, and much of its peach industry, lose their immunity immediately and will almost certainly go out of business, as they cannot compete for price and quality with products from California and Georgia. In an interesting twist, Canadian grape growers will be helped by the U.S. government in their conversion to other crops. This aid will be indirect. For the next 20 years, both countries may impose seasonal import duties on certain fresh fruits and vegetables, under certain circumstances, to help local growers. However, an increase in Canadian export of a fruit produced by Canadian grape growers switching to alternative products must not be subject to the duties levied by the United States. In this way, access to the Canadian market by U.S. wine growers will benefit U.S. consumers of other foods.

Important changes to the existing U.S.-Canadian automobile pact will effectively eliminate the present minimum Canadian-content safeguards that so annoy U.S. firms and that so hearten the breakaway Canadian Auto Workers union.(21)

The present pact, which is skewed in Canada's favor, enables the Big Three auto makers to ship cars and parts duty free across the Canadian-U.S. border, as well as to import parts and cars into Canada duty free from any other country in the world.(22) The latter privilege is contingent on the manufacturers' producing one car in Canada for each car they sell there. The Big Three must also disburse in Canada an amount above a 1965 base level (roughly 60 percent of the value of their annual Canadian car sales) on parts, assembly costs, and other value-added expenses.

Under the new pact, all cars will eventually (by 1998) cross the border duty free if 50 percent of the direct cost of their production has been spent in North America.(23) As of that time, should (as this author anticipates) any of the Big Three wish to forgo the opportunity of bringing cars into Canada duty free from outside North America, they need only conform to the 50 percent North American content requirement. In this way, they need not live up to the Canadian-content safeguards of the current auto pact, all the while retaining duty-free access to the Canadian market. It is thus fair to say that unbiased continental free trade in automobiles will gradually be implemented under the FTA. It will be interesting to note the effects of this process on the CAW, whose very existence was made possible by these distortions.(24)

As usual, companies, unions, and farmers, mostly but not exclusively in Canada, claim that they will not be able to

compete with giant international and/or "imperialist" firms and will be driven from business at great cost in jobs and general welfare.(25) The rejoinder to their cry for help, of course, is that the opening of the large new markets for their products provides an important payoff for efficiency.

Finally, rationalization of fragmented industries may be expected to occur following trade liberalization. It is comforting to see that under the FTA, Prime Minister Mulroney's government is pursuing its policy of relaxing the restrictions on foreign investment that so impoverished Canada (and so weakened the Canadian dollar) under the previous Liberal administration. Government examination of direct takeovers of Canadian companies will gradually be phased out for companies with gross assets worth less than CDN \$150 million (the present floor is only \$5 million). Vexatious review of indirect takeovers (when one U.S. firm takes over another U.S. company that happens to be the parent of a Canadian corporation) will be eliminated altogether by 1992. (Canadian investment in the United States has never been fundamentally limited by statute, to the great benefit of U.S. consumers and Canadian shareholders.) A gradual rise in the value of the Canadian dollar toward--and quite possibly beyond--its purchasing-power-equivalent of 85 cents U.S. should occur when and if the market anticipates implementation of the agreement.(26) This will go a long way to reducing the U.S. trade deficit with Canada, all the while raising the real purchasing power of Canadians, a majority of whom travel to the United States each year.(27)

Enforcement Mechanisms

The enforcement mechanisms for the FTA, while novel, fall short of legitimate hopes. Canadian politicians and negotiators had created high expectations in this field. Brian Mulroney declared to the New York Times on April 20, 1987, that any agreement must exempt Canada from all U.S. trade-remedy laws. Canadian chief negotiator Simon Riesman declared in March of that year that "any agreement which did not restrict the use of U.S. dumping and countervail statutes . . . would not be worth the powder it would take to blow it to hell."(28) It is fortunate that public opinion has a hard time fathoming issues like these, for Canada did not here achieve its negotiating objectives.

Existing antidumping and countervailing laws will remain in effect under the FTA, even though this totally contradicts the reciprocal national treatment of goods that underlies the agreement. Thus, for example, if a steel company in Chicago cuts its price, a U.S. rival can stay competitive by cutting its own price in that city. But if a Canadian steel maker tries to do the same thing, it would have to cut its prices all across Canada or face a charge of dumping under the U.S. antidumping law. An important business tool is thus denied Canadian companies.

Canada's major gain in terms of trade remedies is the institution of new bilateral ad hoc panels to review actions taken under present antidumping and countervailing statutes. These five-member panels may hear complaints lodged by a government or by individuals or firms against such actions. They can declare them contrary to national laws, and their decisions are binding. This is a unique form of judicial review that in practice will replace the U.S. courts as a forum for enforcing U.S. trade laws.(29) The forum will essentially be a final one, except for a three-member judicial panel available to hear administrative law complaints against the bilateral panels (conflict of interest, gross legal error, jurisdictional defect, etc). Effective work by these panels in their interpretation of U.S. trade legislation may well mitigate the capriciousness and politicization in the administration of U.S. trade laws that Canadians have long complained of.(30)

The bilateral panels can also, but more weakly, assess the compatibility of any changes in the trade laws with GATT provisions, or with the spirit and purpose of the FTA. If a panel recommends modification of the changes, consultations must follow. But if no remedial action is taken, the aggrieved government's recourse is limited to adopting identical legislation or terminating the whole agreement.

Finally, a Canadian-U.S. trade commission will be created to supervise the implementation of the FTA and to resolve interpretive disputes.

Will the Free Trade Agreement Be Adopted?

On January 2, 1988, President Reagan and Prime Minister Mulroney signed the FTA in separate ceremonies. Enabling legislation will now be submitted to Congress and to Canada's Parliament.

Prime Minister Mulroney's Progressive Conservative party enjoys a healthy majority in the House of Commons, which would no doubt approve the agreement if requested to do so. This does not mean, however, that approval of the accord is certain or even probable in Canada. In effect:

-- Canada's bicameral Parliament, like Great Britain's, includes a mostly symbolic Senate whose members are appointed for life. The Liberal party has a crushing majority in the Senate, and Liberal leader John Turner vows to "tear up" the treaty when he becomes prime minister.

Will he incite or permit the Senate to hold up implementing legislation? He says he would not, as this would violate parliamentary tradition. His claim should be greeted skeptically, as the same Liberal Senate is presently delaying a bill that would guarantee to U.S. companies copyright royalties on pharmaceuticals sold in Canada.

-- Although their standing has recently improved slightly (probably because of the free-trade deal), the Conservatives still do not fare well in public opinion polls. Plagued by scandals and allegations of incompetence and corruption, they presently attract somewhat less than a third of Canada's electorate. The Liberals and the New Democrats (dominated by trade unions) each seem to have as much support as the Conservatives; both have called for the defeat of the FTA and have challenged Mulroney to call an immediate election on the issue. The Liberals, afraid of being outflanked on the left, planned an April 1988 mailing of "100 Reasons Why the Free- Trade Deal Is Bad" to 1.6 million strategically selected homes.

-- Canada must hold general elections before Mulroney's five-year mandate expires in October 1989; this is only nine months after the FTA would take effect. Moreover, tradition mandates elections at four-year intervals, so it is conceivable that writs of election could be issued before Congress has even acted on the agreement. In this case, Canada's opposition parties could argue that the deal should be defeated by Canadians before it is rejected or amended by the Americans. In addition, if the Conservatives were to lose the next election, increasing importance would be attached to December changes to the October draft of the FTA that provide for termination of the agreement on only six months' notice by either country. This is not reassuring for potential investors.

-- Under Canadian constitutional law, provinces cannot legally veto a treaty; on the other hand, no pact can affect a province's powers without its consent. Thus, for example, notwithstanding the FTA, any province may enact legislation preventing out-of-province architects from practicing in that province, or prohibiting marketing efforts by out-of-province (read "U.S.") vineyards. At present writing, seven provincial governments have informally expressed satisfaction with the FTA. However, three others--the Liberal governments in Ontario and Prince Edward Island and the New Democratic government in Manitoba (Canada's only NDP government)--say they are opposed to the deal. Ontario has 35 percent of Canada's total population, and the province's industries (but not necessarily present-day firms or labor unions) would be prime beneficiaries of increased access to U.S. markets. Nevertheless, Ontario's Liberal premier, David Peterson, has said his government will not implement the agreement's provisions forbidding discriminatory taxes on wine, and the province's New Democratic opposition has gone so far as to express (most unpersuasively) doubts about the constitutionality of the FTA.(31)

-- Recent public opinion polls in Quebec show a resurgence of the separatist option. This may just be a temporary shift due to public sympathy following the death of Ren' L'vesque, the Parti Qu'b'cois founder and former premier. But the new leader of the party, former cabinet minister Jacques Parizeau, ascribes some of the increase in ind'pendantiste feelings to the free-trade option, which (he says) unshackles the province from the national market and opens up the continent to it. This, claims Parizeau, has made Quebecers less averse to the risks of independence and less concerned about the recurring threats from English speaking Canada to cut Quebec off should it secede from the confederation. In some federalist circles, this problem compounds the traditional fears (outlined earlier in this paper) that the country can be held together only by closing off outside markets.

-- As economic theory, public choice doctrine, and Canada's political culture might all lead us to predict, pollsters find slightly more Canadians favorable to the FTA than opposed, but many more are strongly opposed than are strongly in favor of the deal.(32) Spurred on by the entreaties of such cultural activists as novelist Margaret Atwood disseminated by Canadian magazines and by the Canadian Broadcasting Corp. (all have benefited from protection from U.S. competition), many Canadians who will never read the 2,500- page final version of the FTA feel that their country will

be "gobbled up" by the United States if individual Canadians are allowed to choose consumption patterns for themselves.⁽³³⁾ The Toronto Globe and Mail noted that many intellectual Canadians are concerned for the survival of "Canadian culture" under the agreement; simultaneously, it revealed that 9 of the 10 most-watched television programs in English-language Canada were U.S. shows, despite legislation restricting prime-time showing of "non-Canadian content."⁽³⁴⁾

Conclusion

The FTA is flawed and incomplete. Agricultural subsidies persist and must await solution in the context of the GATT.⁽³⁵⁾ Canadian culture remains shielded from American competition, although, as implied above, the shelter is rather porous. U.S. merchant ships and sugar producers retain their monopolies.

Despite these problems and others, firm U.S. support for the FTA is urgently needed, given the precarious politics of the deal in Canada. Under applicable U.S. legislation, the president's signing of the accord before January 3 set off the fast-track process.⁽³⁶⁾ Congress seems to favor delaying its study of the agreement; many are angry that the two-month delay in reaching a final wording of the agreement prevented informed action in the interval, and House Speaker Jim Wright has said the FTA vote won't come until late summer at the earliest.⁽³⁷⁾ Congress could also try to bluff to obtain additional concessions from Canada before acquiescing to the agreement; given the tense political situation in Ottawa, this would almost certainly doom the agreement there. Finally, Congress could decide to include Canada within the provisions of the upcoming omnibus trade package, being debated in the spring of 1988 before the FTA enabling legislation is even ready. The resulting trade bill would give U.S. firms handy tools to claim that almost any foreign imports are "unfair competition."⁽³⁸⁾ This would also deal a fatal blow to the success of the agreement in Canada, and thus ensure the defeat of the Conservatives at the next election.

It is plausible to surmise that the Reagan administration's debacle in Iran spurred the president to conclude the Intermediate-Range Nuclear Forces Treaty as a device to reclaim the moral high ground in world affairs. Similarly, the Mulroney government's unprecedented ill-repute has transformed its free-trade agenda into a lifeline that it might in easier times have jettisoned to placate rent seekers.

The United States could set an example through speedy passage of the FTA, perhaps accompanied by a strong reminder that the alternative to the FTA is not the status quo but a continued slide toward protectionism on both sides of the border. Such passage could help open up to entrepreneurs and consumers what will in 10 years become the largest free-trade zone in the world. Alternatively, myopic U.S. elected officials could seal the fate of Canada's first quasi-free-market government in decades. Hanging in the balance is a measure that represents, arguably, one of the most significant advancements in the cause of freedom on this continent since 1787.

FOOTNOTES

(1) The tariff, put in effect on the same day the first round of free trade negotiations between the two countries was completed, was implemented under a provision of U.S. trade laws that does not require proof of foreign unfair trade practices. In fact, the Canadian lumber industry is competitive and unsubsidized. As an aside, it is worth emphasizing that tariffs, in this author's opinion, are clearly unjustified even if an entity, including a foreign government, is subsidizing the export. Scholars have long argued that selling each item at a loss but making it up on volume just doesn't work, but if someone wants to bestow a gift on us, why should we discriminate on the basis of that person's citizenship?

(2) Toronto Globe and Mail, October 10, 1987, p. B2.

(3) Ibid.

(4) Indeed, the granting of linguistic and religious rights to French-speaking settlers was a direct result of fears that those settlers would join American revolutionaries against the Crown. It is fairly well known that General Benedict Arnold's invasion of Quebec might have succeeded had it not been so ineptly planned.

(5) Donald Creighton's classic work of Canadian history, *The Empire of the St. Lawrence* (Toronto: Macmillan, 1970),

demonstrates that much of the thrust of early Canadian history can be seen as the creation and imposition of an inefficient east-west market structure. The transcontinental railroad has never been cost-efficient, and even today, despite heavy subsidy, it loses money.

(6) This interesting quote may be found in William A. Niskanen, "Stumbling toward a U.S.-Canada Free Trade Agreement," *Cato Institute Policy Analysis* no. 88, June 18, 1987, p. 10.

(7) Charles Gordon, "Trading in the Canadian Identity," *Maclean's*, July 7, 1986, p. 9.

(8) Canada's resource base, excellent transport infrastructure, high education levels, relative racial harmony, and cosmopolitan flavor make it a potentially redoubtable competitor. On January 1, 1900, Prime Minister Wilfrid Laurier asserted that just as the 1800s had witnessed colossal American growth, the twentieth century would belong to Canada. It hasn't quite turned out that way. Peter Brimelow reminds us in his recent book, *The Patriot Game: National Dreams and Political Realities* (Toronto: K. Porter, 1986), that Canada's turn-of-the-century social commentator Goldwyn Smith observed that his country was, *par excellence*, "rich by nature, poor by policy."

(9) Shirley Carr, president of the Canadian Labour Congress, addressing the House of Commons Committee on Free Trade in St. John's, Newfoundland, December 4, 1987.

(10) Testimony of the Manitoba Trucking Association before the House of Commons Committee on Free Trade in Winnipeg, Manitoba, November 27, 1987.

(11) Since Adam Smith's 18th-century classic, *The Wealth of Nations*, little has been added from a purely economic standpoint to the argument condemning tariffs. See N. Rosenberg and L. Birdzell, *How the West Grew Rich* (New York: Basic Books, 1986) for a contemporary historical treatment of free trade.

Adam Smith presumed that people knew, or were capable of knowing, what they wanted. It has been asserted above that much of the pseudo-intellectual Canadian opposition to the FTA is actually paternalistic; that is, free choice to consume U.S. products, like free choice to consume heroin, will lead Canadians to abandon their former ways and be worse off by their own standards. Philosophical opposition to this sort of thesis can await another paper. Here, it suffices to invite U.S. readers to tour any Canadian city and observe how similar to their own is the lifestyle of its inhabitants, after which they may judge whether this paternalism is more than camouflage for rent seeking by inefficient producers and labor unions.

(12) See Niskanen, pp. 2-5.

(13) In addition to the softwood lumber and shake/shingle fiascos, firm measures have been undertaken by the Reagan administration to shelter U.S. automobile and microelectronics manufacturers and textile and sugar producers from efficient foreign competition. The U.S. steel industry is one of the world's least productive, yet Reagan has imposed import restraints on many foreign steel imports. See generally Sheldon L. Richman, "'With Free Traders Like This . . .': Ronald Reagan's Trade Record," *Cato Institute Policy Analysis*, forthcoming 1988.

(14) Hon. Donald MacDonald, ed., *Report/Royal Commission on the Economic Union and Development Prospects for Canada* (Ottawa: The Queen's Printer, 1985).

(15) To be valid under GATT, an agreement must establish a zone where "duties and other restrictive regulations of commerce are eliminated on substantially all trade between the constituent territories in products originating in such territories" (emphasis added). Many accords presently acknowledged to be valid under this article of the GATT are not nearly as comprehensive as the FTA, and there is therefore no reason to suppose that the agreement could be successfully challenged as discriminatory. Claims to the contrary, like that of the president of Toyota Canada Inc. ("We are not treated equally [with U.S. car makers] and therefore it might violate the principles of GATT") in the *Toronto Globe and Mail* (December 12, 1987, p. B5) reflect posturing.

(16) Because the FTA is not a customs union, the thorny problem of duty remissions had to be addressed. Canada has for some time granted remissions of import duty on some imports (from third countries) to the extent that they were

transformed into exports (mainly to the United States). Economically, of course, these remissions of Canadian duties benefit the ultimate foreign consumer (see, for example, footnote 1 above); nevertheless, such practices are typically seen as "tax expenditures" by the Canadian government--that is, unfair subsidies of exports. Existing duty-remission programs on auto parts have severely aggravated preexisting strains on the bilateral automobile pact (see below). Under the FTA, as of June 30, 1988, no new duty-remission plan may be instituted but existing plans may remain in effect for 10 years. This has prompted Canada to plan a new duty-remissions program on imported textiles, to take effect just before the June deadline. U.S. government pressure, in response to producer interests, seems sure to deprive U.S. consumers of the benefit of this plan. See, for example, "U.S. Warns Canada," Washington Post, February 5, 1988, p. B1.

(17) Virtually all Canadian tariffs on imports from the United States are higher than U.S. duties on similar Canadian exports. The gap ratio ranges from about 1.5 to 1 (clothing, electrical machinery) to 2 to 1 (rubber and metal products, textiles, footwear), 3 to 1 (furniture), and even 10 to 1 (chemicals).

(18) At the present time, foreign banks in Canada are limited in size and activity. Under the FTA, these restrictions will end.

(19) There are indications that the Canadian government was willing to move on the beer issue had the United States agreed to relax protection of its politically powerful (since the Cuban trade embargo) sugar industry. This demand was turned down, and all foods with a sugar content of 10 percent or more remain banned from import into the United States.

(20) Nine of Canada's ten provinces do not permit sales of beer that has not been brewed in that province. This is one of the many reasons why Canada's beer industry is so inefficient and (with due respect to American yuppies) why its beer is so insipid. Fortunately, the United States has refused to relinquish its right to lodge attacks against the Canadian beer industry from another angle--that is, through GATT (where the United States has successfully contested Canada's discriminatory wine taxes).

(21) Not surprisingly, the president of the CAW (and prospective leader of the New Democratic party), Bob White, is one of the most outspoken critics of the FTA.

(22) The Big Three are General Motors Corp., Ford Motor Co., and Chrysler Corp. A joint venture under construction in Ontario between GM and Suzuki will also qualify as a Big Three venture. Other (that is, Asian-owned) North American producers will attain duty-free status only gradually. This is an eloquent recognition of the Big Three's ability to successfully form cartels and obtain pressures for voluntary restraints from the U.S. government.

(23) This is, of course, another volley in the U.S. campaign against the Asian producers whose products have proved so attractive to U.S. consumers.

(24) Following the adoption of the pact over 20 years ago, automobile production was rationalized by the Big Three. Different plants (including the Canadian ones) produced components necessary for the efficient operation of other factories. As long as each manufacturer dealt with one labor union, this arrangement worked smoothly. Now, however, the breakaway CAW can affect operations across the continent by striking one plant. Normally this threat could be countered by the employer's power to close the striking plant. However, because of minimum-production requirements, both parties know that this would be a prohibitively costly move for the employer, as it would subject all of its Canadian sales to duties.