Despite Canada-US Deal on Steel and Aluminum Tariffs Many Questions Remain

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On May 17, to much fanfare, Canada and the United States issued a joint statement announcing an agreement under which the United States removes its Section 232 tariffs on Canadian steel and aluminum, Canada lifts its retaliatory surtaxes on U.S. goods, and each country terminates its WTO litigation against the other arising from the Section 232 tariffs. Mexico and the United States announced a similar, separate agreement.

The ending of these trade measures is welcome news for Canadian steel and aluminum producers, including downstream manufacturers that rely on imports, and for the many North American businesses, from the automotive sector to confectionary makers, whose supply chains it disrupted for almost a year. Removal of the tariffs also eliminates a significant political obstacle in all three NAFTA countries to the ratification of the revised NAFTA agreement signed last November.

Nevertheless, key terms of the Canada-US agreement, as described in the joint statement, raise important operational questions for steel and aluminum exporters to Canada and import-dependent Canadian businesses, it also raises an overarching question of whether, in the guise of a settlement of the Section 232 issue, Canada has agreed to far-reaching managed trade with the United States. These questions should be considered in the light of the aggressive trade remedy measures the Canadian Government announced on April 26 after the Canadian International Trade Tribunal mostly rejected the Government's justifications for safeguards on imported steel. The joint statement announces that Canada and the United States will "implement effective measures" to prevent the importation of aluminum and steel that is unfairly subsidized or dumped and, in consultation with one another, prevent the "transshipment" of steel and aluminum made in third countries to Canada or the United States via the other country.

Given that Canada has one of the more robust trade remedy systems in the world, under which there are already anti-dumping or countervailing duty orders in force against imported steel and aluminum (and some more expansive than corresponding measures in the U.S.) it is reasonable to wonder what additional measures Canada may have in mind. The April 26 announcement suggests the answer.

The measures announced in April include:

- targeted reviews of dumping cases to “boost protections through higher duties”, which implies a zealous use of normal value reviews under an administrative process that came into force recently;
- measures to make it easier for the CBSA to “address price and cost distortions in foreign markets when determining whether dumping has occurred”, which implies investigating so-called “input dumping” such as the United States has done in the case of Chinese steel inputs in Korean finished goods, and greater recourse to “particular market situation” findings in determining normal values;
- an unspecified framework for the Canada Border Services Agency to self-initiate anti-dumping and subsidy investigations, a power that has existed in Canadian law for many years.
- The most likely of these measures to be applied quickly is the increased use of the nascent (in Canada) “particular market situation” provision. Although this provision has been part of Canada’s trade remedy law for a few years, Canada has chosen not to publish any administrative policy or guidance on the criteria for “a particular market situation”. Intentionally or not, the conclusion is that it is whatever Canadian authorities want it to be, whenever they want it to be. This arguably undermines the predictability of Canada’s trade remedy enforcement, a principal benefit of the system long touted by Canadian governments.

The prevention of “transshipment” also raises questions. Transshipment is not illegal under international trade law; on the contrary, Canada and the United States are required, as WTO Members, to allow goods to move through their territory to destinations elsewhere. What the joint statement seems to have in mind is imports from, principally, China that are destined for the United States but travel through Canada to circumvent U.S. trade remedy measures. The Government of Canada and Canadian primary steel producers raised the spectre of that sort of circumvention as a justification for the provisional steel safeguards that Canada imposed last year. However, Canadian safeguards never made sense for that purpose, which is more effectively addressed through the enforcement of U.S. and Canadian marking requirements and origin-declarations. One of the elements for “protecting against unfair trade practices” in Canada’s April 26 announcement hinted at even more stringent import information requirements and audits of product origin precisely to address the circumvention of trade remedy orders.

A further question though, is the extent to which concerns regarding “transshipment” extend to the use of third-country inputs in goods further produced or manufactured in Canada. Here again, the rules of origin negotiated under Canada's free trade agreements already establish when steel, aluminum and other inputs are sufficiently refabricated or incorporated into new products in Canada to lose their third-country status and become part of a Canadian-origin product for tariff purposes.

However, the joint statement troublingly indicates that Canada will allow the United States to disregard these rules of origin at its choice for the purpose of managing steel imports. In particular, the joint statement says that Canada and the Untied States will monitor for “surges” in steel and aluminum imports from the other, and, for that purpose, can treat steel that is “melted and poured in North America separately from products that are not”. That is not how steel and aluminum rules of origin are worded in any trade agreement, nor is it how they work.

Moreover, the joint statement indicates that Canada has agreed to a new mechanism to allow the United States to address such "surges" by unilaterally re-imposing duties on steel and aluminum imports from Canada. This mechanism that seems to give the United States considerably more latitude than it currently has under the safeguard provisions of the WTO Agreement or the current and revised NAFTA.

The joint statement says that "[i]n the event that imports of aluminum or steel products surge meaningfully beyond historic volumes of trade over a period of time, with consideration of market share", the importing country may, following consultations with the other party, impose duties of 25 per cent for steel and 10 per cent for aluminum on the individual product categories in respect of which the surge took place. The joint statement lists 54 such product categories for steel and 9 for aluminum.

The unaddressed questions raised by this new surge mechanism include:

- Whether and how it can operate consistently with the safeguard rules in the WTO Agreement and the NAFTA;
- What the threshold requirements are for identifying a surge and imposing the duties, including:
    - what is a "meaningful" increase in imports;
    - the time period over which the surge must be identified;
    - whether the party imposing the duties must show that the surge is injurious (as it must under other trade rules);
    - whether, as it appears, the party imposing the duties can do so without referring the matter for an investigation and determination by an independent investigating authority (as it must under other trade rules).

The joint statement also indicates that the exporting country will be entitled to retaliate in response to such surge duties only in the affected sector (i.e. aluminum or steel). This will deprive Canada of the right to retaliate against other products for maximum political leverage as it, the European Union and other countries have done in the case of the Section 232 tariffs, where they have imposed surtaxes on, for example, bourbon and Harley-Davidson motorcycles.

Given the trade deficit Canada has with the U.S. in steel products, this is a significant, unprecedented concession by Canada. It is also unclear whether retaliation will exist as a matter of right and if so, whether that right will apply immediately upon the imposition of surge duties.

The answers to some of these questions may become clearer if Canada and the United States circulate a more formal text of the "understanding" described in the joint statement. However, it is not clear if or when they are planning to do so. Nor is it clear what legal status the agreement will have. The fact that it is described as an "understanding" and the limitations on the U.S. Administration under its domestic law in negotiating trade agreements suggest that it is something less than a binding legal instrument.

In the meantime, the overriding takeaway for Canadian businesses reliant on steel and aluminum imports and foreign exporters of those products to Canada is that, despite the Canadian Government's stated commitment to trade diversification, the measures

announced in the joint statement aim to appease the protectionist leanings of the current U.S. Administration by ring-fencing the North American steel and aluminum market for U.S. and Canadian suppliers to the detriment of third-country imports, including those from countries with which Canada has been making overtures to increase bilateral trade.

While the disruptive effects of the Section 232 tariffs and the Canadian countermeasures are gone, the uncertainties arising from the surge mechanism announced in the joint statement as well as the more aggressive trade remedy measures that Canada previously announced means that foreign manufacturers and Canadian importers and users of imported steel and aluminum products, including products that undergo substantial transformation in Canada prior to being exported to the U.S., will need to remain vigilant about their exposure to new or additional duties and their commensurate supply chain risks.

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