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Canada-U.S. Relations

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Summary

During the 1980s, the United States and Canada 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 between the two countries continued to be generally cordial. Canada's new Conservative government, under Prime Minister Stephen Harper, is regarded as more philosophically in tune with the Bush Administration than the Liberals were; some observers believe that this compatibility may facilitate bilateral cooperation.

The two North American countries continue to cooperate extensively 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 are relatively few, but sometimes sharp, as has been the case in policy toward Iraq. Since September 11, the United States and Canada have cooperated extensively on efforts to combat terrorism, particularly in Afghanistan.

The United States and Canada maintain the world's largest trading relationship, one that has been strengthened during the past fifteen years by the approval of two multilateral 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 the cultural/entertainment industry. However, these disputes affect but a small percentage of the total goods and services exchanged. Also, the United States and Canada work together closely on environmental matters, including monitoring solid waste transfers, and protecting and maintaining the quality of border waterways.

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

This report provides a short overview of Canada's political scene, its economic conditions, and its recent security and foreign policy, focusing particularly on issues that may be relevant to U.S. policymakers. This brief country survey is followed by several summaries of current bilateral issues in the political, trade, and environmental arenas. The report is updated annually.

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Canada-U.S. Relations

Overview¹

The relationship between the United States and Canada has undergone 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 1988 U.S.-Canada Free Trade Agreement, and the 1993 North American Free Trade Agreement (NAFTA). To many Canadians, however, Ottawa seemed at times to have drawn a bit *too* close to Washington, D.C., 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.² In an interview for a nationally syndicated American magazine, 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 With me, a more mature relation will exist between us and the United States.”³ Some believe, however, that this initial show of mild reserve was intended for domestic consumption, particularly during election campaigns, and that Canada and the United States in fact continued to enjoy excellent relations. For example, during their first official state meeting, in February 1995, former President Clinton and Chrétien celebrated the signing of a long-discussed “open skies” agreement easing restrictions on air travel; the meeting was described as upbeat. Chrétien and 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.

In February 2001, President George W. Bush met with Chrétien. The two leaders discussed energy, missile defense, and trade. Since September 11, however, economic and environmental issues have largely taken a back seat to joint efforts to combat international terrorism. On September 24, 2001, Chrétien met in Washington with President Bush. Canada became involved in the crisis at the outset — 24 Canadians died in the World Trade Center — and has cooperated closely with the United States in the war on terrorism. In the immediate aftermath of the attacks, U.S.

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

² “Canada Narrows Its Foreign Policy Goals to Focus on Trade.” By Charles Trueheart. *Washington Post*. Nov. 17, 1994. p. A44.

³ “Don’t Take Canada For Granted.” By Tad Szulc. *Parade Magazine*. Feb. 20, 1994.

airspace was temporarily closed and Canada allowed more than 200 flights to American destinations to be diverted to Canadian airports.

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. In addition, the Liberal government's plan to decriminalize marijuana raised concerns in Washington. But it has been over security-related matters, particularly defense spending, Iraq, and missile defense, that the two governments had their sharpest differences. Notwithstanding these controversies, Canada and the United States have been working 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 coalition in Afghanistan. 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 the catastrophe caused in September by hurricane Katrina in New Orleans.

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, D.C., Martin and Bush met once more and talked about a variety of issues, from the war on terrorism to the "mad cow" crisis; Bush described the meeting as one "between friends and allies." In November 2004, during President Bush's first official visit to Canada, he and Martin discussed missile defense, border security, and global "hot spots." In a speech in Halifax the next day, Bush thanked the Canadian people for helping stranded American travelers on September 11, 2001.⁴

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 believe that Harper's government will likely be 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 may still arise on certain issues, particularly when they touch upon matters of perceived sovereignty. For example, on January 26, 2006, days before his inauguration, Harper sharply took exception to comments made earlier by U.S. Ambassador to Canada David Wilkins and asserted Canada's

⁴ *Bush Welcomes Canadian Prime Minister to the White House*. State Department Press Release. Apr. 30, 2004. "Bush Launches Bid To Repair US-Canada Ties." *Agence France-Presse*. Nov. 30, 2004.

sovereignty over the so-called Northwest Passage — the frozen arctic region that global warming may turn into a waterway linking Asia and Europe.⁵

Canada's Domestic Scene

Background and Current Political Situation. In August 2002, Jean Chrétien, who had served as Prime Minister since 1993, announced that he would retire from politics when the Liberals held their next leadership vote. Paul Martin, the former Finance Minister, became Prime Minister in December 2003. Although elections need not have been held until late 2005, Martin decided to seek his own mandate and called for elections to be held in the late spring of 2004. Maintaining a Liberal majority appeared to be a safe bet when Martin took office, but such an outcome became doubtful in February 2004, when the “sponsorship scandal” erupted. Canada’s Auditor General published 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. The Auditor General, who characterized the program as “such a blatant misuse of public funds that it is shocking,” reported that questionable methods had been used in awarding the contracts and that little or no actual work had been performed. Martin claimed that, although he was Finance Minister at the time, he had been unaware of the funding arrangements; he launched an independent investigation of the affair.⁶

The Liberals’ standing in the polls plummeted, and the opposition parties gained strength. To the right of the Liberals, two conservative parties had merged under a popular 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 the June 2004 elections, the Liberals won 135 out of 308 seats in the House of Commons — a loss of 33 seats — and chose to govern as a minority.

The government launched an independent commission to investigate the sponsorship affair, under the leadership of John Gomery, an eminent judge. In February 2005, Chrétien appeared before the panel to defend the sponsorship program, and two days later, Martin told the commission that, while finance minister, he had not been privy to the details of the program. In April, an advertising executive testified that, in order to win federal contracts, he had made cash payments to the Liberal party. The testimony alleging kickbacks heightened the controversy, as it indicated that the governing party appeared to have been paying itself, albeit indirectly, from public coffers. One newspaper called the affair “one of the great

⁵ “Harper Tells U.S. To Butt Out On Plans For Defending Canada’s Arctic.” *The Canadian Press*. January 26, 2006.

⁶ “Canada: Martin on the Ropes in Funding Scandal.” *Oxford Analytica*. Feb. 25, 2004. “Scandalous!” By John Geddes. *Maclean’s*. Feb. 23, 2004. P. 19. “Canada’s Premier Acts to Counter Scandal.” By DeNeen L. Brown. *Washington Post*. Feb. 17, 2004.

scandals in Canadian history,” while another has referred to it as “Canada’s Watergate.”⁷

The Liberals survived — by one vote — a May 2005 proxy confidence vote and avoided spring elections. But in November they lost another confidence vote, and federal elections were held on January 23, 2006. This time, the Conservatives won a plurality.⁸ The Conservatives currently have 125 out of 308 seats in the House of Commons — a gain of 25 seats — and are governing as a minority (the Liberals have 102 seats, the Bloc Québécois 51, and the NDP 29.)

Some analysts caution that the Tory victory does not necessarily represent a “paradigm shift” to the right in Canadian politics; they note that the Conservative party won only 37% of the popular vote. Because minority governments only last an average of about 18 months in Canada, Prime Minister Harper will be keeping one eye on the next elections.⁹ In addition, Harper will need the ad hoc support of the other three parties to ensure passage of the various items on his legislative agenda. Many therefore believe that he will advocate fairly centrist policies in the near future, by seeking legislative approval of the five priorities on which he campaigned: 1) greater government accountability; 2) shorter health care wait times; 3) tax cuts; 4) child care assistance; and 5) criminal law reform.¹⁰

Harper has already begun work on these items. The first bill introduced in the current session of parliament was the Federal Accountability Act — the Conservatives’ response to the sponsorship scandal. The massive (252 pages) ethics proposal is intended to “change the way business is done in Ottawa forever” by addressing such issues as whistleblower protection, political contributions, lobbying reform, and government contracts and appointments. Some critics charge that the new law is selective, while others maintain that it represents overkill. Supporters praise the measure as an effort to bring about long-overdue changes.¹¹

In mid-March, Harper made a surprise visit to Canadian troops in Afghanistan. He 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. A recent poll showed Canadians to be almost evenly divided in their support of the Afghanistan mission.¹²

⁷ “Indepth: Sponsorship Scandal.” *CBC News*. May 5, 2005. “Brault Alleges Liberal Officials Got Kickbacks.” *Globe and Mail*. Apr. 8, 2005. “Canada’s Watergate.” *National Post*. Apr. 8, 2005.

⁸ For a description of the campaign, see “Inside Story.” By Paul Wells. *Maclean’s*. Feb. 6, 2006. p. 7.

⁹ See “Interview: Stephen Harper.” *Maclean’s*. Mar. 6, 2006. p. 12.

¹⁰ See “Conservatives To Govern From Political Center.” *Oxford Analytica*. January 24, 2006. “Harper’s Five Easy Pieces.” *Economist*. April 8, 2006.

¹¹ “Harper Rolls Out His Ethics Act.” *CanWest News Service*. April 12, 2006. “Clean Doesn’t Get Any Squeakier.” By John Ibbotson. *Globe and Mail*. April 12, 2006.

¹² “Harper’s Mission Statement.” By Andrew Coyne. *National Post*. March 15, 2006.

Fiscal Policy. The federal deficit, which stood at a record high C\$42 (as of April 28, 2006, one Canadian dollar equals US\$0.89) billion when Chrétien became Prime Minister in 1993, was reduced steadily each year until 1998, when then-Finance Minister Paul Martin introduced Canada's first balanced budget in nearly three decades. This dramatic elimination of the deficit was accomplished in part through higher than anticipated tax revenues, and through such politically risky measures as cutting federal funding for health and education transfers, and applying a means test to those eligible for Seniors Benefits.

For the past eight years, Canadian politicians have been in a post-deficit environment in which they have had to select among competing demands on annual budget surpluses. Some officeholders argue that much of the budget surplus should be devoted to large reductions in corporate and income taxes. They maintain that Canada's high taxation, relative to that of other countries, discourages job creation, reduces household incomes, diminishes worker productivity, and causes a "brain drain" of Canadian professionals, chiefly to the United States. However, other policymakers point out that Canada's current tax system enables the government to maintain a host of social programs that make Canada the envy of many countries; in addition, they note that, high taxes notwithstanding, thousands of talented people emigrate to Canada every year.¹³

On February 23, 2005 the Martin government unveiled its last major budget. The spending blueprint highlighted fiscal probity as well as funding for social programs, international affairs, the environment, and the economy; it boosted spending in such areas as health care, defense, and the environment, and also cut taxes. As was the case in the past, a portion of the surplus was devoted to paying down the national debt. Although support for the budget was fairly widespread, one prominent Canadian journalist argued that it did not stress innovation, but rather "takes existing programs and shovels money into them," and also noted that the plan may tie the hands of future governments through multi-year spending commitments.¹⁴ In November 2005, the Liberals introduced a "mini-budget" containing tax cuts for middle- and lower-income people.

The Conservatives reportedly are set to table their first budget during the first week in May. Some of the Harper government's budget priorities may be inferred from campaign themes, which, among other measures, included a pledge to reduce the Goods and Services Tax (GST, a form of national sales tax). Some funding will likely be earmarked for child care allowances and infrastructure improvements. Observers speculate that the new budget may cancel the tax cuts enacted by the Liberals in November.

¹² (...continued)

"Poll Finds Canadians Split On Afghan Mission As MPs Prepare For Debate. *Canadian Press*. April 9, 2006.

¹³ See "The Tax Trap. By Mary Janigan." *Maclean's*. Apr. 12, 1999. p. 14. And: "The Brain Drain: Myth and Reality." By Ross Finnie. *Choices*. Vol. 7, No. 6. Nov. 2001.

¹⁴ *Budget 2005: Delivering on Commitments*. Canadian Department of Finance. Feb. 23, 2005. "How the Liberals Boxed in the Tories — and Themselves." By Jeffery Simpson. *Globe and Mail*. Mar. 8, 2005.

National Unity. For four decades, an emotional debate has raged over the status of French-speaking Québec, Canada's second largest province and home to 23% 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 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 voted on whether they wished to continue to remain a part of Canada, or strike off on their own. The question was decided by the narrowest of margins; the vote went 50.6% to 49.4% in favor of keeping the country whole. The wafer-thin margin shocked federalists and separatists alike. The country is still affected by the impact of what has been called a "near-death experience."

Québec held provincial elections once again in October 1998, and the PQ retained a comfortable majority in the provincial legislature. Lucien Bouchard, the charismatic premier, subsequently announced that he would not call another referendum until "winning conditions" were evident;¹⁵ nevertheless, Bouchard pledged a renewed push for sovereignty. Then, in January 2001, Bouchard stunned the province and the nation by announcing that he would resign his post. His immediate successor, Bernard Landry, was regarded as a hard-line sovereigntist.

In April 2003, Québec voters turned out the *Pequists* 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. During his first year in office, Charest lost popularity 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 has learned from his mistakes; others point to continued low approval ratings and argue that Charest's Liberals still have a lot of work to do as they prepare for elections in 2007. Charest was said to have been encouraged by the victory of Harper, who favors greater government decentralization. The two also share an opposition to sovereignty, and, for pragmatic political reasons, will likely cooperate with one another in several areas.¹⁶

Ironically, although the sponsorship program was intended to reinforce Canadian unity, the fallout from the scandal appeared to have a contrary effect. Many Québeckers became resentful, particularly of the federal Liberal party, believing that, outside the province, the sponsorship scandal may have reinforced old stereotypes of dirty Québec politics. In April 2005, pollsters found that 54% of

¹⁵ "Separatism Near Extinction: Poll." By Campbell Clark and Robert Fife. *The National Post*. Dec. 15, 1999.

¹⁶ "Québec Union Leaders Blast Charest Three Years To the Day of His Election." *Canadian Press*. April 14, 2006. "Unpopular Charest Needs Harper's Help To Gain Re-election." By Rhéal Séguin. *Globe and Mail*. April 15, 2006.

Québeckers favored sovereignty. Although some separatists were convinced that this signaled a move toward “winning conditions” for them in a future referendum, others contended that the surge in support was a temporary phenomenon. The latter view was reinforced by a post-election poll that indicated 37% support for sovereignty. In addition, sovereignty advocates were disheartened by the poor showing of the Bloc Québécois in the January 2006 elections. Although the Bloc hoped to capture more than half of the popular vote in the province, it won just 42%.¹⁷

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. During a 1998 visit to Ottawa, former Secretary of State Albright delivered remarks — in English and French — that, in the opinion of some observers, reinforced the perception that U.S. policy favored a united Canada. And during a 1999 visit to Canada, former President Clinton declared that the United States valued its relations with “a strong, united and democratic Canada.” If, at some future date, Québec eventually *does* leave the confederation, the U.S. government will be faced with difficult political and economic questions.¹⁸

Security and Foreign Policy Issues

Canadian Security Issues. Canadians are proud of their active role 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 nearly every U.N. peacekeeping operation, from Cyprus and the Sinai, to Bosnia, Rwanda and Somalia. As of April 24, 2006, over 2,700 Canadian Forces personnel were participating in international operations in Afghanistan, the Balkans, the Middle East, and Africa.¹⁹

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

¹⁷ “54% In Québec Back Sovereignty.” By Rhéal Séguin. *Globe and Mail*. Apr. 27, 2005. “Survey Numbers Corrected But Poll Still Shows Drop In Sovereignty Support.” *The Canadian Press*. Feb. 2, 2006.

¹⁸ “Albright Says U.S. Prefers United Canada.” *Ottawa Citizen*. Mar. 11, 1998. “President Clinton Meets with Chrétien, Opens New U.S. Embassy.” *Canada Quarterly*. Oct., 1999.

¹⁹ *Canada and International Peacekeeping*. By Joseph T. Jockel. Center for Strategic and International Studies/Canadian Institute of Strategic Studies. Washington, D.C., and Toronto, Ontario. 1994. Current Operations. Available from the Canadian National Defence web page at [http://www.forces.gc.ca/site/operations/current_ops_e.asp].

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) spend a lower percentage. Canada's meager military budget has irked some within the alliance, particularly the United States; former U.S. Ambassador Paul Cellucci repeatedly urged the Canadian government to devote greater resources to its military.²⁰

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 — the 56th largest in the world. The Canadian forces have also been strapped for resources to replace aging equipment.²¹ This trend has disturbed many in the military, and may be affecting morale. There have been numerous warnings in recent years. In February 1996, the Canadian Chief of Defence Staff stated that his troops would be unprepared for "high intensity" combat. More than two years later, Canada's Auditor General cautioned that an equipment budget shortfall might result in "reduced capabilities." 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." Finally, in September 2005 the Senate published yet another report, which called for a doubling of spending on defense.²²

Some analysts have charged that continued low levels of defense spending may hamper Canada's international reputation by creating a "commitment-capability gap." A Canadian editorialist declared that "[w]e have effectively signed over responsibility for our national defence to the United States by allowing our own military to become so diminished in size and the quality of its equipment."²³

Canada's defense spending has been trending upward in recent years. The budget tabled in February 2005 contained the largest military spending increase in two decades: C\$12.8 billion — roughly equal to one year's military budget — spread over five years. Highlights of the budget include \$3 billion for additional troops, \$3

²⁰ "Spend More On Military, U.S. Envoy Urges Ottawa." *Toronto Star*. Feb. 25, 2004.

²¹ "Canada's Flying Coffins." Peter Newman. *Maclean's*. Feb. 3, 2003.

²² "A Shot Across the Bow: The Chief Says His Forces Are Unfit For War." By Luke Fisher. *Maclean's*. Feb. 26, 1996. "Canada's Security At Risk." By Jim Bronskill. *Ottawa Citizen*. Mar. 2, 2002. "Pull Troops From Overseas, Senators Say." By Allison Dunfield. *Globe and Mail*. Nov. 12, 2002. "Armed Forces Hobbled, Report Says." By Daniel LeBlanc. *Globe and Mail*. Dec. 3, 2003. "Senators Sounding Alarm On Defence." *The Gazette*. Oct. 3, 2005.

²³ "Military Criticized For Rhetoric On Peace: Canada Accused of 'Speaking Loudly and Carrying a Bent Twig.'" By Mike Blanchfield. *Ottawa Citizen*. Mar. 23, 2001. "Afghanistan In the Wake Of Death." Anthony Wilson-Smith. *Maclean's*. Apr. 29, 2002.

billion for operations and maintenance, and \$2.5 billion for new equipment and capabilities. Although the Conservative government has not yet tabled its budget, Harper pledged during the midwinter campaign to add C\$5.3 billion in military spending.²⁴

In April 2005, the Martin government released its long-anticipated International Policy Statement, of which defense is one part (the last such defense policy overhaul took place in 1994.) The new security plan aims to make Canada's military "more effective, relevant and responsive." Among other things, it calls for a change in the command structure; the addition of 5,000 regular troops and 3,000 reserves; the expansion of Canada's special forces, including tactical support equipment; the creation of an anti-nuclear, biological, and chemical weapons unit and a rapid-reaction force; and the acquisition of a wide range of materiel, particularly of air, land, and sea transport. The Harper government reportedly plans to procure both tactical as well as strategic transport aircraft.²⁵

U.S.-Canada Security Issues. According to the U.S. State Department, "U.S. defense arrangements with Canada are more extensive than with any other country." In a valedictory speech, former Canadian Ambassador Michael Kergin referred to the defense relationship as being "intermestic" in nature.²⁶

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

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; its most recent five-year renewal took effect in May 2001. 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

²⁴ Defence and Budget 2005 — Highlights. Canadian Department of National Defence web page. [http://www.forces.gc.ca/site/reports/budget05/summ05_e.asp] "Harper Pledges Boost To Military Spending." *Globe and Mail*. By Michael Den Tandt. Dec. 14, 2005.

²⁵ Defence and Budget 2005 — Highlights. Canadian Department of National Defence web page. [http://www.forces.gc.ca/site/reports/budget05/summ05_e.asp] "Harper Settles Feud Over Military Hardware." By James Travers. *The Toronto Star*. April 25, 2006.

²⁶ United States Department of State. Bureau of Western Hemisphere Affairs. *Background Note: Canada*. April, 2006. "Remarks to the Center for Strategic and International Studies." Feb. 28, 2005.

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. NORAD is scheduled for renewal in May 2006; Ottawa and Washington have reportedly agreed to expand the scope of the agreement to encompass nautical surveillance.²⁷

Ottawa also long debated whether it should participate in the U.S. missile defense (MD) 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.²⁸

On February 24, 2005, the Canadian government said that it would not participate in MD. 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. MD commands. U.S. officials expressed puzzlement and disappointment with the announcement, noting that Canada had sent signals that it would likely sign on. Some analysts suggest that domestic political pressures — polls showed that a majority of Canadians, particularly Québeckers, opposed MD — may have guided the decision. In late February 2006, newly-named Defense Minister Gordon O'Connor 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.²⁹

²⁷ "Continental Divides." By Sydney J. Freedberg, Jr. *National Journal*. Mar. 23, 2002. "Leading academics Examine Risks Inherent In Closer Military Co-operation With the United States." *Canada NewsWire*. Apr. 26, 2002. "Canada Won't Join Norad-Like Land-Sea Force. By Rick Mofina." *Ottawa Citizen*. Aug. 15, 2002. "All For One?" By Luiza Ch. Savage. *Maclean's*. Sept. 12, 2005. "Revised NORAD To Guard Costs: Pact Ready In May." *Montreal Gazette*. Feb. 21, 2006. Binational Planning Group. Final Report. March 13, 2006. [<http://www.canadianally.com/BPGFinalReport.pdf>]

²⁸ "Shoot Down Defence Dreamers." By Paul Koring. *Globe and Mail*. June 25, 2003.

²⁹ "Canada and the U.S. Missile Defense System." Dwight M. Mason. *CSIS Hemisphere Focus*. Jan. 9, 2004. "Martin and the Politics of Missile Defense." *Globe and Mail*. May 1, 2004. "Missile Defence Won't Work." *Ottawa Citizen*. Dec. 15, 2004. "Martin's Move Irritates U.S." By Sean Gordon. *Toronto Star*. Feb. 24, 2005. "Minister Backs U.S. Missile Plan." *Toronto Star*. Feb. 24, 2006.

In February 2002, Canada agreed to participate in the further development of the U.S.-led Joint Strike Fighter program, contributing \$150 million over a 10-year period. Canada is apparently already reaping rewards from its participation; on May 26, 2004, *Jane's Defence Weekly* noted that Canada "has been particularly successful in acquiring JSF contracts." More recently, it was announced that Canadian firms so far had won 147 contracts worth about \$130 million. Canada may eventually purchase JSF to replace its own fleet of CF-118 fighters.³⁰

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 and 500 troops to maintain stability in Haiti. Canada also supplied 200 troops to NATO's mission in Macedonia, and 600 to the initial U.N. peacekeeping mission in East Timor. In addition, 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 1500 troops each to KFOR. Canada also provided 844 personnel to assist in the post-Hurricane Katrina relief activities in New Orleans. Canada currently has hundreds of peacekeepers stationed in Afghanistan, the Balkans, Africa and the Middle East.³¹

Canada has been engaged in the debate over NATO's future. It supported enlargement and has announced that it will participate in the NATO Response Force, which the alliance agreed to at its November 2002 Prague summit. In April 2003, Foreign Minister Graham, along with the Dutch and German governments, requested that NATO take over command of ISAF in Afghanistan; in February 2004, a Canadian general took over command of the peacekeepers in Kabul.³²

Canada has also made military contributions to the war on terrorism. It was one of the first countries to join the military operation in Afghanistan. In October, 2001 the government launched *Operation Apollo*, in support of U.S. *Operation Enduring Freedom*. Nearly 900 infantry troops and approximately 40 members of Canada's special forces unit, Joint Task Force 2, served in Afghanistan. Their main task was to provide airbase security, but they were also involved in delivering humanitarian aid and in combat missions, including *Operation Anaconda*, to root out remaining elements of the Taliban and Al Qaeda. Other Canadian military assets supporting *Operation Enduring Freedom* have included a naval task force group, consisting of 4 frigates, a destroyer, and a replenishment ship, all serving in the Arabian Sea, and a half-dozen transport and surveillance aircraft. In August 2005, a Canadian Provincial Reconstruction team began an 18-month mission in Kandahar. As of April 18, 2006, Canada had 2,300 troops in the country. Ottawa has provided humanitarian and reconstruction assistance to Afghanistan, with total allocations of

³⁰ "Canadian Firms Big Winners In U.S. Jet Project." *National Post*. April 21, 2006.

³¹ Current Operations. Apr. 26, 2006. Canadian Department of National Defence web page: [http://www.forces.gc.ca/site/operations/current_ops_e.asp].

³² "NATO Umbrella Sought." By Allan Thompson. *Toronto Star*. Apr. 4, 2003. "NATO Sees Key Role For Canada In Afghan Security." *Reuters*. May 6, 2003.

C\$616.5 million for the period 2001-2009.³³ A total of 16 Canadians — including one diplomat — have died in Afghanistan, and 48 have been wounded. The most recent casualties occurred on April 22, 2006, when an improvised explosive device killed 4 Canadians.

Foreign Policy Background and Issues. After Chrétien became prime minister in 1993, some analysts concluded that he had “tilted Canada’s foreign policy towards the more explicit pursuit of economic self-interest and away from concerns about human rights abroad.”³⁴ Under Lloyd Axworthy’s leadership beginning in 1996, however, many observers detected a swing in attitude at the Foreign Affairs Ministry back toward Canada assuming the role of “soft power,” relying on its reputation as an honest broker to help effect consensus through negotiation and moral suasion rather than military force or economic sanctions.³⁵ In the most significant example of this approach, Axworthy launched the “Ottawa process” to reach agreement on a treaty banning the manufacture, trade, and use of antipersonnel land mines; the effort culminated in a December 1997 conference at which more than 100 nations signed the accord. Axworthy also sought to launch a similar ban on small arms, and attempted to generate interest among other countries in promoting an international “humanitarian agenda.”³⁶ The United States did not sign the pact.

John Manley replaced Axworthy in 2000; in January 2002, when Manley became Deputy Prime Minister, Bill Graham, chairman of the parliamentary committee on foreign affairs and international trade, took over. According to one writer, Graham “can often sound like Axworthy.”³⁷ Others, however, believe he placed more emphasis on pragmatism. In July 2004, Martin reshuffled his cabinet, moving Graham to Defense and replacing him with Pierre Pettigrew, a Québecker. In February 2006, Prime Minister Harper named Nova Scotian Peter MacKay Foreign Minister.

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, and the Asia-Pacific Economic Cooperation forum. From 1998-2006, Canadian diplomat Louise Frechette served as Deputy Secretary General of the United Nations. Also, the Organization for Economic Cooperation

³³ Backgrounder: Canadian Forces Operations in Afghanistan. Apr. 18, 2006. DND web page: [http://www.forces.gc.ca/site/newsroom/view_news_e.asp?id=1703]. Afghanistan Overview. July 22, 2005. Available online from the Canadian International Development Agency web page at [<http://www.canada-afghanistan.gc.ca/menu-en.asp>].

³⁴ “Canada Bows Out As ‘Boy Scout’ To the World.” By Jeffrey Simpson. *Hemisfile: Perspectives on Political and Economic Trends in the America*. July/Aug. 1995.

³⁵ “Canada to Play Global Role as ‘Soft Power.’” By Mike Trickey. *Ottawa Citizen*. Mar. 3, 1998. “Ottawa’s New-Age Diplomacy Ruffles Many Feathers in Washington.” By Steven Pearlstein. *International Herald Tribune*. Feb. 22, 1999.

³⁶ See Canadian Department of Foreign Affairs and International Trade. *Human Security: Safety for People in a Changing World*. Ottawa. Apr. 1999.

³⁷ “Out of Africa: The Perils For A PM.” By Anthony Wilson-Smith. *Maclean’s*. Mar. 25, 2002. p. 4.

and Development is led by a Canadian (former cabinet minister Donald Johnston), and the first head of the U.N. War Crimes Tribunal was Canadian Louise Arbour. In June 2005, Canadian Air Force General Ray Henault was named head of NATO's military committee.

Canada and the United States have worked closely together in a number of troubled regions. One example of such cooperation over the past decade was 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 6 helicopters and nearly 500 troops. Ottawa also said it would provide C\$1 million in emergency aid to flood victims in Haiti and the Dominican Republic.

U.S.-Canada Agenda. Canada was disinclined to expand the war on terrorism beyond Afghanistan to Iraq. In February 2002, Foreign Affairs Minister Graham stated that Ottawa would oppose U.S. unilateral action against Iraq unless Baghdad were linked to terrorism, or it were “shown that they are amassing their weapons of mass destruction with a vision of using them against someone in the immediate future....” Later, when asked whether Canada would require “tangible proof” of a connection between terrorists and the Iraqi government before Canada would consider joining a military action against Iraq, Graham replied “Yes, absolutely.”³⁸

In September 2002, during a brief meeting in Detroit with President Bush, Chrétien reaffirmed Canada's preference for a U.N. mandate, a stance that strongly reflected Canadian public opinion. Two months later, Washington 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.”³⁹ One week later in Toronto, U.S. Ambassador Cellucci delivered a speech in which he expressed the Bush Administration's disappointment with the Canadian government's decision. The remarks raised strong concerns in Canada over the state of bilateral relations, particularly after the White House postponed a state visit by President Bush to Ottawa. In April, seeking to repair the apparent rift,

³⁸ “Canada Won't Back War On Iraq.” By Mike Trickey and Hilary Mackenzie. *Ottawa Citizen*. Feb. 15, 2002. p. A1. “Canada FM Requires Proof Of Terror Links For War Beyond Afg.hanistan.” *Agence France-Presse*. Mar. 11, 2002.

³⁹ “Well, Maybe” *Economist*. Sept. 28, 2002. “PM Scolds McCallum On Canada's Role In Iraq.” By Shawn McCarthy and Daniel Leblanc. *Globe and Mail*. Jan. 16, 2003. “Bravos Greet Chrétien.” By Tim Harper. *Toronto Star*. Mar. 18, 2003.

Secretary of State Powell acknowledged that “differences will come along,” and declared the two countries to be “inseparable.”⁴⁰

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. Since then, Canada has provided funding in a number of areas, including humanitarian and reconstruction aid, support for elections, and police training. Altogether, the Canadian International Development Agency has pledged C\$300 million in assistance to Iraq. In January 2004, Canada announced that it would cancel Iraq’s \$564 million debt.

Cuba has been another issue where the two countries have not seen eye-to-eye. For decades, Canada and Cuba have enjoyed relatively extensive business links. Because of this ongoing commercial relationship, Canadian government officials have 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-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 April 2003, after the Castro government handed down Draconian prison terms to several political dissidents, Foreign Minister Graham expressed official disapproval to the Cuban ambassador.⁴¹

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, Foreign Minister 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.”⁴²

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

⁴⁰ “Powell Says Canada and US ‘Inseparable’ Friends Despite Iraq Tiff.” By Robert Russo. Canadian Press. Apr. 15, 2003.

⁴¹ “Chrétien Admits Having ‘A Problem’ With Cuba, But Will Maintain Pressure.” *Agence France-Presse*. Apr. 10, 2003.

⁴² “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*. Sept. 10, 2002.

attempting to smuggle explosives into the United States; it was later discovered that Ressay 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. 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.”⁴³

Some American policymakers pointed to the Ressay 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 terrorists and criminals would at best be inconvenienced, not stopped, in traversing the two countries’ 5,500-mile border. About 70% 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.⁴⁴ 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 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, which will permit coordination of refugee and asylum policy.

Ottawa and Washington are currently working to resolve issues surrounding the Western Hemisphere Travel Initiative, a provision of a 2004 U.S. law that will require travelers passing between the two countries to present a passport, or an equivalent document, at the border. Travel-dependent businesses particularly in Canada, are concerned that the cost of acquiring either a passport (only about 25% of Americans and 40% of Canadians hold passports) or similar ID would inhibit travel; other critics are worried that the requirement could indirectly discourage Asian and European investment in both countries.⁴⁵

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

⁴³ “Al-Qaida In Canada?” CBSNEWS.com. Apr. 25, 2002. “Canada Alters Security Policy To Ease Concerns of U.S.” By Clifford Krauss. *New York Times*. Feb. 18, 2002.

⁴⁴ “Delays at the Canadian Border Eat Up Trade.” By John Stark. *AP*. Feb. 1, 2003.

⁴⁵ “A Tightening Border Has Canadians Worried.” By Ian Austen. *New York Times*. Apr. 15, 2006.

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.

The Martin government in December 2004 created a Department of Public Safety and Emergency Preparedness, a counterpart to the U.S. Department of Security (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. The 2005 budget, for example, contains funding for the addition of 270 border officers over the next five years.

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 Royal Canadian Mounted Police, and increasing outlays for countering nuclear, biological, and chemical weapons attacks.

In March 2004, reports by the Canadian Senate and the Auditor General faulted Ottawa's emergency preparedness efforts, chiefly for lack of coordination among government agencies and between federal and provincial governments. In April 2005, the Auditor General delivered a second report that characterized progress as "uneven." Nevertheless, in a speech one month later in Toronto, former U.S. Secretary of Homeland Security Tom Ridge praised Canada's border security actions, declaring that he did not "accept the thesis that Canada is lenient or hasn't done what it needs to do...."⁴⁶

During a March 2005 summit meeting in Texas, President Bush, Mexican President Vicente Fox, and Prime Minister Martin agreed to a Security and Prosperity Partnership of North America. The initiative is intended to provide security for the continent, while easing the flow of goods and travelers who cross the borders between the three countries. It also aims to improve prosperity in all three countries through promoting cooperation in a number of areas, including health, food safety, environmental protection, transportation, energy, and financial services. Presidents Bush and Fox, joined by Harper, met again in March 2006 to review progress to date and to plan the next phase of cooperation.

Economic and Trade Issues

Canada's economy over the past three years has proven itself to be resilient. Despite afflictions caused by what the *Globe and Mail* referred to as "the Four Horsemen of the Apocalypse — BSE, forest fires/hurricane, SARS, and a massive blackout," Canada's GDP grew by 2.0% in 2003 and by 2.9% in 2004 and 2005. In

⁴⁶ "Canada Unprepared for National Emergencies." Darren Yourk. *Globe and Mail*. Mar. 31, 2004. "Big Gaps In Emergency Plans." Sean Gordon. *Toronto Star*. Apr. 6, 2005. "Ridge Defends Canadian Security." Andrew Davidson. *Globe and Mail*. May 12, 2005.

April 2005, inflation stood at 2.2%, buoyed up in part by higher petroleum and natural gas prices. The March 2006 unemployment rate was 6.3% — the lowest rate in 30 years.⁴⁷

Although the Canadian economy overall is in healthy condition, prosperity has been somewhat uneven over the past decade. British Columbia suffered from Asia's financial turmoil, and the prairie provinces from the loss of livestock export revenues caused by the BSE scare. In addition to SARS, Ontario was pummeled by the August 2003 blackout. The economy of oil-rich Alberta, on the other hand, has benefitted significantly from higher petroleum prices.⁴⁸ U.S.-Canadian interest rate gaps, along with strong oil prices and sound fiscal policies, boosted the value of the Canadian dollar (known as the "loonie") 20% against the U.S. dollar after 2003. Some economists are concerned that this may affect Canada's export sector, which over the past two decades has increasingly represented a significant share of the economy. In 2005, Canada enjoyed a current account surplus of \$24.9 billion.

On February 11, 2003, Chinese officials announced the outbreak of the severe acute respiratory syndrome (SARS) and in March, it was discovered that a traveler had carried the disease to Toronto. Eventually, about 150 Canadians contracted the illness, and 23 died. Canadian health authorities made strenuous efforts to contain the sickness, and on April 30, the World Health Organization lifted the travel advisory it had placed on Toronto. But the appearance, however brief, of the virus is expected to have significant longer-term effects upon the regional and national economy; the impact on travel-related industries has been particularly severe.⁴⁹ The Martin government announced the establishment of a Canadian Public Health Agency, which will play a role similar to that of the U.S. Centers for Disease Control and Prevention. Many public health officials on both sides of the border are worried over the possible spread of avian influenza. Bird flu has a much higher mortality rate and is a matter of serious concern to epidemiologists. The security of the two countries' food supplies is another area that policymakers continue to monitor.

Canada is the United States' largest supplier of energy — oil, natural gas, and electricity — and the energy relationship has been growing. Canada is the world's seventh largest petroleum producer, and its reserves are believed by some to be secondly only to those of Saudi Arabia; Canada's sources include traditional and offshore wells and, increasingly, Alberta's tar sands. Canada provides 17% of U.S. oil imports and supplies 18% of U.S. natural gas demand. Canada is particularly valued because it is a reliable source of energy, a key factor contributing to U.S. economic security. The two sides are cooperating on the development of pipeline construction projects. China recently has begun to show increasing interest in

⁴⁷ "Federal Budget 2004." *Globe and Mail*. Mar. 24, 2004. Economic data are from wire service reports and from "Canada: 5-Year Forecast Table." *Economist Intelligence Unit (EIU)*. Apr. 13, 2006.

⁴⁸ "Alberta Gallops Ahead, As Eastern Canada Struggles." By Clifford Krauss. *New York Times*. Mar. 28, 2006.

⁴⁹ "A Model of Epidemic Control." David Brown. *Washington Post*. May 3, 2003. "SARS: Fear and Loathing in Toronto." Jonathon Gatehouse. *Macleans*. May 5, 2003. "Canada Says SARS Has Infected Its Economy." Gilbert Le Gras. *Reuters*. Apr. 29, 2003.

Canada's oil sector, a development that is believed to have "caused some consternation in Washington." Canada also a net exporter of electricity to the United States, and the North American electricity grid is closely interconnected. Following the August 2003 blackout, the two sides have worked to develop improved standards for electricity transmission reliability.⁵⁰

Bilateral Trade Issues. The United States and Canada enjoy the largest bilateral commercial relationship in the world; the U.S. State Department estimates total two-way trade at \$1.2 billion *per day*. Many analysts believe that the sharp differences of the past, over diverse items ranging from automobiles to peanut butter, are not as prominent today. A likely reason for this is the conclusion of two important bilateral treaties: the 1988 U.S.-Canada Free Trade Agreement and the 1993 North American Free Trade Agreement. These documents, along with major revisions in the Uruguay Round of the General Agreement on Tariffs and Trade and the creation of the World Trade Organization (WTO), contained mutual concessions on commercial trade barriers, and, more importantly perhaps, established or improved upon mechanisms for resolving disputes.⁵¹

Nevertheless, 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.

In particular, the long-running dispute over softwood lumber continued to fester. 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 to 21%) duties on Canadian softwood. Canada challenged the agency decisions under NAFTA and in the WTO. In August 2005, NAFTA affirmed earlier NAFTA decisions resulting in an ITC "no threat" determination. Canadians asserted that the United States should lift its tariffs on softwood and refund some C\$5 billion in estimated lumber duties, which might otherwise be distributed to U.S. lumber producers under the Byrd Amendment. The Bush Administration maintained, however, that the ITC "no threat" determination (issued in September 2004) was superseded by a November 2004 "threat of injury" determination issued by the ITC in response to a separate WTO decision. Further

⁵⁰ "Canada — Natural Resources." *Jane's Sentinel Security Assessment*. June 13, 2005. "Canada: Challenges Remain In Oil Sector." *Oxford Analytica*. Feb. 16, 2005. The Canada-U.S. Energy Relationship. Updated Apr. 12, 2006. Canadian Embassy website: [http://www.dfait-maeci.gc.ca/can-am/washington/trade_and_investment/energy-en.asp].

U.S. Energy Information Administration. Country Analysis Briefs: Canada. Available online at [<http://www.eia.doe.gov/emeu/cabs/Canada/Background.html>].

⁵¹ "Current State of U.S.-Canada Economic Relations." By Sidney Weintraub. *American Review of Canadian Studies*.

complications arose later in August when a WTO panel preliminarily ruled that the November threat determination was not in violation of WTO rules. Canada has challenged implementation of the November ITC determination in U.S. court. Finally, on April 26, 2006, the two sides announced that they had struck a tentative seven-year agreement on softwood. 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. In addition, the United States will return to Canada a large majority of the duties it had collected.⁵²

In May 2003, a cow in the Canadian province of Alberta was discovered to be infected with bovine spongiform encephalopathy (BSE, or “mad cow” disease). The United States banned importation of Canadian cattle or cattle products. The Canadians quarantined several ranches and destroyed and tested several thousand animals. In September 2003, the United States began permitting importation of live animals young enough to be at low risk of having the disease. In December, however, a Canadian-born cow in Washington State was discovered to have BSE, and most countries banned imports of U.S. beef. In January 2005, two new BSE-infected animals were found in Canada. In early March, a U.S. federal judge blocked a USDA ruling that would have permitted more Canadian cattle to enter the United States, and the Senate approved a White House-opposed resolution that would overturn the rule. A U.S. appeals court reversed the blocked ruling in July, permitting Canadian cattle to enter the United States. The two countries have been cooperating bilaterally and in international organizations to develop consistent approaches to animal health and food safety regulations. On April 16, 2006, a fifth Canadian animal was discovered to be infected with BSE.⁵³

Regardless of the occasional rancor of U.S.-Canadian trade disputes, there is little danger that such conflicts would ever escalate into a full-blown trade war. The Canadians in particular have a strong incentive to resolve feuds and maintain close trade ties with the United States. The Canadian economy is heavily export-oriented, and its largest trading partner by far is the United States, takes more than 80% of Canada’s exports and is the source of nearly two-thirds of its imports. And although sharp disputes still plague the enormous bilateral trade relationship, it is important to bear in mind that such disputes normally affect only 2% of trade.

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,

⁵² “U.S. Gets a Lift In Lumber Fight With Canada.” By Ian Austen and Clifford Krauss. *New York Times*. Aug. 31, 2005. “Conservative Government Wins Softwood Truce.” *Globe and Mail*. Apr. 28, 2006.

⁵³ For further information, see CRS Report RS22345. *BSE (“Mad Cow Disease”): A Brief Overview*. By Geoffrey S. Becker. “Mad Cow Case Is Found In Canada.” *New York Times*. Apr. 17, 2006.

especially the Great Lakes. In 1978, the two signed the Great Lakes Water Quality Agreement.

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 and with sound conservation practices. Talks resumed in 1997, and the two sides finally reached an accord in 1999; both countries are monitoring implementation of the agreement.⁵⁴

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 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 governments, the United States agreed to install a permanent filtration system at the Devils Lake outlet.⁵⁵

Other environmental problems the two countries have dealt with in recent years include secondary wastewater treatment, control of predator fish introduced into the 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. 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.

⁵⁴ CRS Report RL30234. *The Pacific Salmon Treaty: The 1999 Agreement In Historical Perspective*, by Daniel A. Waldeck and Eugene H. Buck. Updated Oct. 18, 1999.

⁵⁵ "Devil Down South." *The Economist*. July 16, 2005. "Little-Known White House Office Negotiates Devils Lake Dispute." *AP*. Sept. 5, 2005. "U.S. Promises Devils Lake Filter, But Water May Flow Before Installation." *Canadian Press*. Apr. 25, 2006.

Border Security Issues⁵⁶

Issue Definition. Border security has emerged as an area of public concern, particularly after the September 11, 2001 terrorist attacks. Since the terrorist attacks, the United States and Canada have been striving to balance adequate border security with the facilitation of legitimate cross-border travel and commerce. As Congress passes legislation to enhance border security and the Administration puts into place procedures to tighten border enforcement, concerns continue to persist with respect to the potential for terrorists to exploit the border. Congress previously passed significant border security-related legislation as discussed below, and issues pertaining to the oversight of such legislation and their possible policy implications for U.S.-Canada border relations continue to be of interest to Congress. These issues include (1) the new requirement that Canadian nationals, along with other foreign nationals from countries in the Western Hemisphere, will soon need a travel document to enter the United States; and (2) improvements to infrastructure at the border and ports of entry (POE).

Background and Analysis. Both the United States and Canada have taken various measures to better secure the shared border while simultaneously preventing disruption to the flow of people and trade. While such efforts date back to 1995, recent efforts include a 30-point plan, commonly referred to as the “Smart Border Accord” (signed on December 12, 2001). The declaration includes a 30-point (now 32-point) plan to secure the border and facilitate the flow of low-risk travelers and goods through coordinated law enforcement operations, intelligence sharing, infrastructure improvements, improvement of compatible immigration databases, visa policy coordination, common biometric identifiers in travel documents, prescreening of air passengers, joint passenger analysis units, and improved processing of refugee and asylum claims, among other things. Previously, on December 3, 2001 the two countries signed a joint statement of cooperation on border security and migration that focuses on detection and prosecution of security threats, the disruption of illegal migration, and the efficient management of legitimate travel. Other efforts to increase border security between the U.S. and Canadian government include the 1999 *Canada-U.S. Partnership Forum* (CUSP) and the February 24, 1995, joint accord, *Our Shared Border*.

Congress also took action to better secure the border by passing the USA PATRIOT Act (P.L. 107-56). The act authorized the Attorney General to triple the number of border patrol personnel and immigration inspectors along the northern border and authorized \$50 million for the former INS to make technological improvements and to acquire additional equipment for the northern border. The Enhanced Border Security and Visa Reform Act of 2002 (the Border Security Act; P.L. 107-173) similarly authorized additional personnel and technological and infrastructure improvements at the borders. The Border Security Act contained a provision that required the development of technology to track the entry and exit of foreign nationals (referred to as the US-VISIT program). Both the USA PATRIOT

⁵⁶ Prepared by Blas Nuñez-Neto, Analyst in Domestic Security, Domestic Social Policy Division of CRS.

Act and the Border Security Act required travel documents to be tamper resistant and contain a biometric identifier that is unique to the card holder.

More recently, Congress passed legislation that requires the Secretary of Homeland Security, in consultation with the Secretary of State, to develop and implement a plan as expeditiously as possible to require a passport or other document, or combination of documents, “deemed by the Secretary of Homeland Security to be sufficient to denote identity and citizenship,” for all travelers entering the United States. Commonly referred to as the Western Hemisphere Travel Initiative (WHTI), this provision in the Intelligence Reform and Terrorism Prevention Act of 2004 (P.L. 108-458) will require Canadian nationals (and other foreign nationals) to present some form of approved travel document to enter the United States by January 1, 2008. The WHTI has fostered much debate in Canada as well as the United States. According to published reports, only about 23% of Americans and 40% of Canadians own passports. These statistics lead some observers to voice concerns that the increased documentation that will be required at the border may suppress travel between the two nations. The Department of Homeland Security (DHS) and the Department of State (DOS) recently announced that the vehicle for WHTI documentation would be known as the People Access Security Service (PASS). The PASS card would be credit card sized, cost less than a passport, contain a biometric, and provide documentation of citizenship. According to DHS and DOS, the WHTI will become effective in two phases: by December 31, 2006, all air and sea travel to or from Canada, Mexico, Central and South America, the Caribbean, and Bermuda will fall under the WHTI requirements; by December 31, 2007, all land border crossings as well as air and sea travel will fall under the WHTI requirements.

Many bills have been introduced in the 109th Congress (and one such measure has been enacted into law) that would authorize appropriations to further increase personnel and improve infrastructure at the border. Legislation has also been introduced that would require the Secretary of Homeland Security to conduct a vulnerability assessment study at land ports of entry. Other pieces of legislation would (1) establish a northern border coordinator in DHS to serve as a liaison to the Canadian government on border security-related issues, among other things; (2) require the Secretary of Homeland Security to submit a border security strategy and a report on progress toward implementing the Smart Border Accords; (3) require the Secretary of Homeland Security to establish a North American security initiative; and (4) require DHS to conduct a study concerning the erection of border fencing. For more information concerning these and other proposals affecting the northern border, please refer to CRS Report RL33181, *Immigration Related Border Security Legislation in the 109th Congress*, by Blas Nunez-Neto and Cheryl Beaver.

Current Coordination Between the Two Countries. The U.S. and Canadian governments continue to implement the provisions in the Smart Border Accord. For example, both countries have expanded the NEXUS program to eleven land border crossings. Both countries continue to explore the feasibility of creating additional joint facilities at agreed upon ports of entry and sharing of information through interoperable technology. Additionally, both countries have begun to take steps to share passenger information on high-risk travelers en route to either country

through a risk-scoring scheme that was jointly developed; and in 2004, an automated process to share “lookout” data between both countries was developed.

Questions.

1. When fully implemented, the WHTI will make significant changes to the current documentary requirements needed to enter the United States. What steps will the Canadian government be taking to ensure that Canadian citizens are aware of these changes? Will the Canadian government consider imposing similar requirements on American citizens entering Canada?

2. In recent years, a number of different technologies, including the US-VISIT program, have been implemented at northern POE. With the advent of the WHTI, the demand for improved infrastructure will continue to be critical. What measures have been taken by the Canadian government to mitigate the impact of such a demand at its border crossings?

3. The Smart Border Accord calls on the two countries to develop approaches to move customs and immigration inspection activities away from the border. While such an approach is already present at Canadian airports, there has been interest in expanding it to areas away from land ports of entry. What is the Canadian government doing to facilitate this objective?

Border Security: Trade and Commercial Concerns⁵⁷

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. 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 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. Today, the United States and Canada have the largest trading relationship in the world with over \$1 billion per day in goods and services crossing the border in 2005. Canada purchases 23% of U.S. exports, a share larger than Japan and slightly less than the entire European Union. The United States purchases 84% of Canadian goods exports in 2005, a sum that represents approximately 27% of Canadian gross domestic product. The Ambassador Bridge that links Detroit, Michigan and Windsor, Ontario is the largest trade link in the world with more than 7,000 daily truck crossings totaling more than \$120 billion per year.

Action Programs and Initiatives. New initiatives to increase security of the border without impeding the flow of commerce are being developed under the Security and Prosperity Partnership (SPP), which was launched by the leaders of the United States, Canada, and Mexico in March 2005. Many of these initiatives expand upon previous bilateral efforts by the United States and Canada, including the Smart Border Action Plan of December 2001 consisting of 4 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

⁵⁷ Prepared by Ian F. Fergusson, Analyst in International Trade and Finance; Foreign Affairs, Defense, and Trade Division of CRS.

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 SPP calls for the two programs to be harmonized within two years.

The *Free and Secure Trade (FAST)* is a joint harmonized commercial processing initiative at 21 border locations (as of April 2006), 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.

Status. 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 calls 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).

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 aging and adequacy of the border infrastructure may affect trade flows if crossing becomes more difficult in terms of time and money. A binational partnership to construct additional crossing capacity at the Detroit-Windsor gateway is engaged in technical and environmental assessments of potential new crossing sites; however, the opening of new bridge or tunnel capacity is not envisioned before 2013.

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. Is Canadian sovereignty threatened by having U.S. customs agents with enforcement powers active on Canadian soil? Is this a factor in the negotiations on land preclearance? What are the elements of sovereignty that most concern you? Is legislative action necessary to permit this cooperation?
3. 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?
4. Who should pay for the replacement or improvement of aging border infrastructure? Should business pick up part of the tab?

Immigration and Refugee Policies⁵⁸

Issue Definition. Should the United States be concerned that Canada's immigration and refugee laws and policies pose a threat to its national security? If so, what has been the impact of the implementation at the beginning of 2005 of the 2002 Agreement designed to require many potential refugees to present their claims in their first safe country of entry?

Background and Analysis. Although Canada does not have country or worldwide quotas, the government does establish annual targets. The annual global targets for 2004 and 2005 were set between 220,000 and 245,000 persons. In 2004, 236,000 persons were accepted as permanent residents. The government has maintained that it would like to eventually increase the annual total to approximately 300,000. That figure would represent almost 1% of the total Canadian population and is subject to Canada's absorptive capacity. Asian countries, such as China, India, Pakistan, and the Philippines, are heavily represented at the top of the list of countries from which Canada's immigrants come, but no one nation dominates. Iran is the country closest to the Middle East that recently has been in the top ten. Immigrating to Canada is usually difficult and time-consuming. Security checks are conducted by federal authorities. However, since Quebec has an agreement with the federal government that allows it to select immigrants intending to settle in that province, Quebec's system adds a second screening process for its applicants. Quebec also has addressed security concerns by adjusting its programs for recruiting immigrants. The federal government uses a points system for assessing independent applicants that recently was changed to attract more highly skilled and educated immigrants. Canada already accepts a much higher percentage of independent immigrants and a much lower percentage of family class immigrants than does the United States.

One notable feature of Canadian immigration is that nearly three-quarters of the persons accepted settle in the three largest cities: Toronto, Montreal, and Vancouver. This tendency, combined with the high rate of immigration, has raised some concerns about destructive "diaspora nationalism" emerging in these concentrated communities. The 2005 bombings in London, which apparently were conducted by persons who had lived most of their lives in the United Kingdom, and reports of possible politically violent tendencies in some young persons raised in Canada by immigrant parents have heightened this concern. However, this problem is not unique to Canada and opposition to immigration has not been voiced nearly as loudly or as forcefully as it recently has been in parts of Western Europe. In fact, immigration still generally is viewed as an opportunity for growth in what would otherwise be a declining population.

Canadian policy for asylum applicants is a far more contentious issue within the country than immigration, not so much for its negative effects within Canada, but because it generally is believed to invite fraud and abuse. Between 1989 and 2004, an average of about 30,000 refugees claims were presented annually. In 2001, this number rose to about 45,000 before falling back to approximately 39,000 in 2002.

⁵⁸ Prepared by Stephen F. Clarke, Senior Foreign Law Specialist, Western Law Division, Law Library of Congress.

An average of about 44% of the applications were accepted. This number is higher than the corresponding figure in the United States. Of particular concern to Canadian officials prior to 2005 was the fact that approximately 40% of the overall total claimants and some 70% of port-of-entry claimants had entered Canada through the United States. There was significant evidence that illegal migrants were abusing the U.S. Non-Immigrant Visa system to access North America and the Canadian asylum system to stay in Canada. Canada is attractive to these persons because it detains few undocumented refugee claimants pending independent identification and the federal and provincial governments grant immediate assistance to applicants who have yet to substantiate their claims. The result has been that the majority of Canada's refugee claimants arrive in Canada without any documents and are allowed free entry into the country even though it is clear that many disposed of the documents they had before coming to Canada. While Canadian officials do not routinely detain undocumented arrivals, Canada has increased the use of detention for persons who may be viewed as posing a security or flight risk. New holding facilities are being prepared, but opposition critics have contended that even stronger action needs to be taken.

The Canadian refugee system has been portrayed as extremely liberal on a number of American television programs that have received considerable attention in Canada. Most of these segments have mentioned four high profile cases of terrorists from the Middle East who entered Canada as refugees with the intention of launching attacks against U.S. targets. Among these examples was the case of Ahmed Ressam who was arrested four years ago while crossing the border with explosives that he planned to set off at Los Angeles International Airport. Also highlighted have been the cases of suspected terrorists who have remained in the country for many years while fighting their way through a very lengthy appeal process. In 2002, the Supreme Court of Canada ruled that two persons linked to terrorist organizations could be deported to countries where they might face torture when security concerns so require. One of these individuals was returned to Iran, but the other has continued fighting his extradition to Sri Lanka.

American media coverage of the Canadian refugee system has elicited a wide range of responses. While a number of commentators agree that the United States has good reason to fear that Canada's refugee policies can be easily employed by terrorists to enter North America, others contend that terrorists are more likely to use other means to enter both Canada and the United States. Many analysts point out that there is no evidence that any of the September 11 hijackers had a Canadian connection, and that the refugee system essentially has been used for "queue jumping" by enterprising persons who might not qualify under Canada's immigration laws. Proponents of this view question how great the security risk to the United States can be if a significant number of claimants are coming to Canada from this country.

In December 2002, the United States and Canada signed a Safe Third Country Agreement to allow immigration officials in both countries to require most persons seeking asylum at a border crossing to go back and present the claims in their respective country. This type of Agreement had been called for in the Action Plan to the Smart Border Declaration signed in the aftermath of the September eleventh attacks in the United States. Implementation of the Agreement was delayed by the

lengthy and complicated process for drafting and approving appropriate regulations in the United States, but it finally went into force at the beginning of 2005.

Although the Safe Third Country Agreement aims to limit asylum shopping and the filing of multiple claims, it is limited in scope and subject to several major exceptions. One major limitation is that it only covers the presentation of claims at land border crossings. Airport and marine facilities are not covered because, as the drafters of the Agreement have explained, authorities know that persons are in the other country only in instances where they are seen crossing the border. However, critics contend that this will simply encourage would-be refugee claimants to sneak into their country of choice illegally or fly into their country of choice in order to present a claim. The Agreement also contains very broad exceptions for relatives, including relatives of other asylum seekers and it allows the parties to “examine any refugee status claim made to that party where it determines that it is in the public interest to do so.” Since the Safe Third Country Agreement generally is opposed by refugee groups in both countries, it is likely that internal pressure will be put on both countries to invoke this reserved right in particular cases.

Statistics show that the number of refugee claims presented at border crossings in Canada declined by approximately 40% in the first half of 2005, and fewer than 20,000 total claims were filed for the entire year. Although this data would suggest that the Safe Third Country Agreement has had a dramatic impact, it also has been noted that claims presented at airports, which are not subject to the Agreement, initially were down to about 25%. Thus, the Safe Third Country Agreement appears to have gone into effect during a period in which the number of refugee claims already was declining.

Status of the Issue. In recent years, Canada’s courts have extended many rights and protections to refugee claimants, frustrating some attempts by the government and quasi-judicial officers to eliminate abuses. Several refugee organizations have brought suit against the government, contending that the Safe Third Country Agreement violates the constitutional guarantees to security of the person. These organizations also are pushing for reforms to weaken the law and are pointing to the steep decline in refugee claims as an indication that the law goes too far in closing off Canada to persons fearing political and other forms of persecution.

Questions.

1. Could the Safe Third Country Agreement have had a broader application and will it withstand judicial scrutiny on both legal and constitutional grounds in Canada and the United States?
2. Are the well-reported cases of terrorists and potential terrorists entering North America through legal means be a sign of a potentially much greater threat?
3. Why do Canadian and United States officials maintain different detention policies in the case of undocumented refugee claimants?

Canada and the WTO Doha Development Agenda⁵⁹

Issue Definition. A signatory to the Havana Treaty in 1947, Canada was one of the founding members of the General Agreement on Tariffs and Trade (GATT). Over the intervening half-century, Canada has become a leading trading economy and has become increasingly involved in shaping the world trading system through several rounds of GATT and, since 1994, World Trade Organization (WTO) negotiations. Canada played a key role in facilitating the 2001 launch of the Doha Development Round. The Doha Ministerial Declaration set forth objectives in several negotiating areas such as agriculture, industrial tariffs, services, and the special needs of developing countries in the international trading system.

Background and Analysis. Canada's interest in the world trading system can be partly attributed to its dependence on it. In the half-century since the signing of the GATT, Canada has developed an export driven economy. In 1947, Canada exported approximately 2% of its GDP; that figure was 32% of GDP in 2005. Imports of goods represent 27.9% of GDP. It was recently estimated that one-third of Canadian employment is directly dependent on international trade. The United States is Canada's largest trading partner, buying 84% of its merchandise exports and supplying 56.6% of Canada's goods imports in 2005. It must be noted, however, that much of this trade relationship is due more to the Canada-U.S. Free Trade Agreement of 1988 (which was incorporated into the North American Free Trade Agreement in 1994), than to multilateral trade liberalization. Recently, some commentators have questioned the influence that Canada has on the WTO negotiations as well as the relevance of those negotiations to Canadian trade flows.

The Doha Round negotiations are currently stalled. Four years into the negotiations and after a string of missed deadlines for conclusion of the talks, agreement on modalities — methodologies such as formulas for tariff reductions by which negotiations are conducted — still elude the agriculture, industrial market access, services, and other negotiating groups. Although the December 2005 Hong Kong Ministerial made limited progress on moving the negotiations forward, the deadline it set for negotiating modalities for agriculture and industrial market access, April 30, 2006, will not be reached. The July 2007 expiration of U.S. trade promotion authority looms as the *de facto* deadline for approval of an agreement.

Agriculture. Canada and the United States broadly share common objectives concerning agricultural negotiations begun in early 2000. As the fourth largest agricultural exporter, Canada seeks to maximize reductions or elimination of trade distorting domestic support and to improve market access for agricultural products. Canada also supports the total elimination of export subsidies, which was agreed to at the Hong Kong Ministerial in 2005. However, Canadian negotiators have resisted attempts to include state trading enterprises (such as the Canadian Wheat Board) in

⁵⁹ Prepared by Ian F. Fergusson, Analyst in International Trade and Finance; Foreign Affairs, Defense, and Trade Division of CRS.

parallel negotiations on other trade-distorting export practices. Disciplines on these entities are a priority for the United States.

Non-Agricultural Market Access (NAMA). The United States and Canada have similar goals for the NAMA talks. Canada's main objectives in tariff negotiations are to seek broad-based market access opportunities, especially among developing countries where tariffs on non-agricultural products remain high. It favors the reduction of tariff rates through a Swiss formula approach, one adopted at the Hong Kong Ministerial. However, it has not advocated specific coefficients in the talks. It has favored the negotiation of non-tariff barriers and, with the United States, expanding the use of sectoral tariff elimination agreements, specifically on chemicals, forestry products, non-ferrous metals, fisheries, fertilizers and energy equipment.

Services. Negotiations on amending the General Agreement on Trade in Services (GATS) have been in progress since early 2000. Canada's stated objective is to target sector requests to maximize the opportunities of Canadian service exporters, especially small and medium enterprises (SMEs). Canada also is interested in providing additional labor mobility for its service professionals overseas. Conversely, Canada is committed not to negotiate on liberalizing the provision of services relating to its health care, education, or social services. Canada has also declared that its cultural identity policies (including Canadian content restrictions and media subsidies) will not be subject to the GATS, but instead it has proposed the negotiation of a "New International Instrument on Cultural Diversity" that would govern regulations concerning cultural industries.

Trade Remedies. The launch of negotiations at Doha to discipline, to clarify, and to provide transparency in the use anti-dumping, subsidies, and countervailing measures is a key priority for Canada. The government's position in these negotiations is to separate legitimate uses of trade remedy legislation from what it considers disguised attempts at protectionism and has sought to impose more specific disciplines and increased transparency in the use of trade remedy measures. In addition, Canada has objected to the use of these remedies by the United States and has been engaged in anti-dumping and countervailing duty disputes at the WTO over softwood lumber and wheat, and the Byrd amendment. The U.S. position has sought to reflect the negotiating mandate of trade promotion authority, i.e. not to undermine U.S. trade remedy laws. The United States has focused on promoting transparency in the administration of trade remedy laws, adherence to appropriate standards of review in dispute settlement panels, and addressing underlying trade distorting practices.

Questions.

1. What is the legislative process in Canada for approving trade agreements? Are there legislative procedures analogous to Trade Promotion Authority, or fast-track procedures, approved by the U.S. Congress in 2002?
2. Have recent U.S. antidumping and countervailing duty cases against Canadian softwood lumber and wheat stiffened Canada's resolve to press for additional disciplines on trade remedies in the WTO negotiations? Given the general

opposition of Members of Congress to changes in U.S. trade remedy laws, what types of disciplines can be agreed upon?

3. One of the themes of the Doha Development Agenda is the integration of developing and least-developed countries into the world trading system. While this is a laudable goal, many key exports of developing countries, such as textiles and apparels, face high tariffs from developed countries. How does Canadian trade policy seek to resolve this conundrum? Should developed country trade policy allow for non-reciprocal tariff concessions as a spur to development? How important is it that developing countries lower their own generally high tariff rates?

4. Given that 80% of Canadian exports of goods and services go to the United States, and are thus covered by NAFTA, how important are the WTO negotiations to the Canadian government, and to the Canadian people? Do the WTO talks present Canada with the opportunity to remedy perceived weaknesses in NAFTA? If so, in what areas?

North American Integration⁶⁰

Issue Definition. The terrorist attacks of 2001 fueled a wide-ranging debate in Canada over its relationship with the United States, including the feasibility or desirability of furthering the process of North American integration. While concerns in the United States over the U.S.-Canada border are focused primarily on border security and immigration issues, the debate in Canada has become much broader, encompassing such issues as sovereignty, the desirability and feasibility of further economic integration with the United States, and even the adoption of the U.S. dollar. This discourse is not unusual in Canada; questions concerning its relationship with the United States continually loom large in policy discussions. Recent initiatives, however, may spur the process of economic integration.

Security and Prosperity Partnership (SPP). On March 23, 2005, the leaders of the United States, Canada, and Mexico signed the Security and Prosperity Partnership (SPP), a pledge to develop a series of security and economic cooperation measures among the three countries of the North American Free Trade Agreement (NAFTA). Ministerial working groups were established to develop concrete proposals, the first set of which were announced in June 2005. Additional measures were announced at the trilateral Cancun summit between Presidents Bush and Fox and Prime Minister Harper in March 2006. The impetus for the establishment of the SPP has been the effect on trade from the increase in security along the border following the 2001 terror attacks as well as the growing perception among some that NAFTA needs to be reinvigorated in order to compete with the growing economic power of Asia. Many of the security planks expand on the Smart Border Action Plan of 2001 (see *Border Security: Trade and Commercial Concerns*).

The “prosperity” rubric consists of a series of measures designed to enhance the competitiveness of North American business to better meet the pressures of globalization. Some of the goals include cooperation on regulatory harmonization with the establishment of a trilateral Regulatory Cooperation Framework by 2007; the reduction of redundant and duplicative testing (what Canadian International Trade minister David Emerson called “the tyranny of small differences”); sectoral cooperation on steel, energy, autos, and air transportation, protection of intellectual property, and detection and deterrence against counterfeit and pirated goods.

Many of these initiatives reportedly were chosen because they could be undertaken through the regulatory process and would not require legislation. Some initiatives will be developed by institutional structures that already exist, such as the North American Steel Trade Committee. Business groups in the United States and Canada have generally supported this effort, and some have called for its expansion. However, other groups have decried what they consider the undemocratic nature of implementing regulatory changes without legislative approval and what they consider the business-driven agenda of the initiatives. Some Canadians also fear that regulatory harmonization, given the wide disparity in population and economic

⁶⁰ Prepared by Ian F. Fergusson, Analyst in International Trade and Finance; Foreign Affairs, Defense, and Trade Division of CRS.

power of the two nations, would inevitably lead Canada to adopt U.S. standards and, implicitly, the policies behind them.

More generally, some in Canada believe the lesson from September 11 is that increased cooperation with the United States is both necessary and inevitable, given the reality of Canadian trade flows and economic interdependence. Several long-term economic options have received renewed attention, including a *customs union*, a *common market*, or a *monetary union*. These concepts are not new; they have been discussed in conjunction with “deepening” NAFTA. Consequently, these discussions often involve Mexico as well.

Customs Union. The first step usually discussed regarding the further integration of the North American economy is the creation of a *customs union*. Members of a customs union commonly eliminate tariffs among themselves, and erect common barriers against the rest of the world. Both the U.S. and Canada have already eliminated all tariffs between each other under NAFTA, and have similar, though not identical, tariff schedules with third countries. However, the continued use of trade remedy laws against each other would be called into doubt. Although customs duties would be paid at ports of entry at the perimeter of the customs union, border agents would still enforce immigration, sanitary and phytosanitary, and environmental laws, as a customs union does not imply a harmonization or mutual recognition of each nation’s regulations.

Common Market or Economic Union. In addition to a common tariff policy and free trade in goods and services, a common market would imply free movement of capital and labor. At this point, harmonization of certain investment and immigration issues would need to be agreed upon. A type of economic union approaching that of the European Union would also require harmonized or mutually recognized standards and regulations and perhaps some supranational institutions. Although the United States and Canada share many developed country level standards, this form of integration would require regulatory harmonization or mutual standards recognition. For example, would the United States adopt the metric system to fulfill its obligations to harmonize standards? Could the two nations adopt common forestry practices and management policies that have been at the heart of the softwood lumber dispute? These questions illustrate the extent to which North American economic integration may affect the governance of the United States, Canada, and possibly Mexico.

Monetary Union. The concept of monetary union took hold in Canada during the 1990s and early 2000s when the Canadian dollar steadily depreciated against the U.S. dollar. However, since 2003 the loonie (named after the bird on the C1\$ coin) has risen over 40% from 2002 levels to US\$0.88 by April 2006. The loonie is benefitting from record high prices for energy and other primary products. Hence, talk of the desirability of monetary union has been muted. However, those who support monetary union argue that it would force Canada to make the necessary structural adjustments that would make it more competitive with the United States. In addition, business would also reap significant savings in transaction costs associated with the huge volume of bilateral trade. Opponents of monetary union contend that it would lead to an unacceptable loss of political and economic

sovereignty. According to them, monetary policy would be dependent on (or tied to) actions of the U.S. Federal Reserve, with which Canada would have little influence.

Status of the Issue. The active pursuit of North American integration is not a front-burner issue for either the United States or Canadian government. However, the adoption of the SPP indicates that the three NAFTA countries are beginning to think about the parameters of economic integration, and may be taking the first steps towards the creation of a North American economic space.

Questions.

1. Does the dispute over softwood lumber and the U.S. dismissal of the NAFTA Extraordinary Challenge Committee ruling cloud your perception of further economic integration between the two (three) countries?
2. Has the loonie's appreciation since 2002 hurt the Canadian manufacturing sector that previously relied on a weak currency to maintain competitiveness?
3. How does the Canadian public feel about closer economic ties with the United States? Is there a perceptible difference on this issue among Canadian political parties?

U.S. Imports of Canadian Softwood Lumber⁶¹

Issue Definition. The U.S. lumber industry has long argued that imports of subsidized Canadian lumber were injuring U.S. producers. A 1996 agreement with a fee on lumber imports above a specified level expired on March 31, 2001, and the U.S. lumber industry filed antidumping and countervailing petitions to restrict imports. In May 2002, determinations of Canadian subsidies, of dumping, and of injury to the U.S. industry led to a duty of 29% on most Canadian softwood lumber imported into the United States. Canada has challenged these findings under NAFTA and before the WTO. Negotiations have apparently led to an agreement that would result in the United States revoking the countervailing and antidumping orders and Canada imposing export charges.

Background and Analysis. U.S. lumber producers have long expressed concerns about imports of subsidized Canadian lumber. The Department of Commerce (DOC) has investigated the imports several times over the past two decades. In 1981, it found that Canadian subsidies were *de minimis* (insignificant). In 1986, its preliminary finding was subsidies of 15% of sale values; the expected duty was supplanted by a Memorandum of Understanding (MOU), with Canada imposing a 15% export tax on softwood lumber. Canada withdrew from the MOU in 1991, arguing that the provinces had responded to the previous concerns. The next investigation led to a 6.51% duty in 1992, but this duty was successfully challenged under the U.S.-Canada Free Trade Agreement. In 1996, the United States and Canada reached a five-year softwood lumber agreement which established a fee on lumber imports from four Canadian provinces in excess of a specified level.

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. 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.

U.S. lumber producers assert they have been injured by subsidies that 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,

⁶¹ Prepared by Ross W. Gorte, Natural Resource Economist and Senior Policy Specialist; Resources, Science, and Industry Division of CRS, and Jeanne J. Grimmer, Legislative Attorney, American Law Division of CRS.

and grades; in measurement systems; in requirements on harvesters; in environmental protection; and in other factors.

Log export restrictions in British Columbia are also said to be subsidies, 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 35% 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. The 1996 U.S.-Canada softwood lumber agreement expired on March 31, 2001. On April 2, the U.S. Coalition for Fair Lumber Imports filed countervailing duty and antidumping petitions, asking the DOC to investigate Canadian imports again. After negotiations for a solution collapsed, DOC issued final determinations on March 22, 2002, that subsidies were 19.34% of sale value and average dumping margins were 9.67%. On May 3, the ITC determined that the U.S. lumber industry was threatened with material injured by dumped and subsidized softwood lumber imports from Canada. An import duty averaging 27% was imposed on May 22, 2002.

Canada challenged each of the final agency determinations under the North America 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, some supporting the United States and some adverse to the United States. Canada is also concerned that some C\$5 billion in estimated duties on softwood lumber collected by the United States may eventually be available for distribution to U.S. lumber producers under the Continued Dumping and Subsidy Offset Act ("Byrd Amendment"); however, on April 7, 2006, the U.S. Court of International Trade ruled that the Byrd Amendment does not apply to imports from Canada.

On April 26, 2006, a tentative agreement between Canada and the United States resolving the dispute was announced. The United States would revoke the countervailing and antidumping duty orders and would return the greater of US\$4 billion or 80% of the deposits (with interest) to the importers of record. The remaining deposits (20%, up to US\$1 billion) would be split evenly between the members of the Coalition for Fair Lumber Imports and jointly agreed-upon initiatives. Canada would collect 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 by more than 10%. Lumber from logs harvested in the Atlantic Provinces, Yukon, Northwest Territories, or Nunavut is exempt from the export changes. Disputes would be resolved through a binding settlement process, using

non-North American arbitrators. The agreement is for seven years, with an optional two-year renewal.

Questions.

1. The dispute over U.S. imports of Canadian lumber has persisted for more than 20 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. The new seven-year agreement would terminate the current duties, return most of the money collected, and establish price-dependent export charges on Canadian lumber. Will all the relevant parties (U.S. and Canadian lumber companies and litigants; Canadian provinces) accept the agreement? What changes are needed in the next seven years to assure that the recent countervailing and antidumping duty process — with NAFTA and WTO challenges and litigation — is not repeated when the agreement expires? What happens if some of the provinces make appropriate changes and others do not?

Wheat Trade⁶²

Issue Definition. U.S. trade officials and northern-tier wheat producers have long expressed concerns that Canadian wheat trading practices — both import and export — are inconsistent with Canada’s international trade obligations. U.S. concerns have been exacerbated by the monopoly powers of the Canadian Wheat Board (CWB). In accordance with Canadian law, the CWB has the exclusive right to purchase and sell western Canadian wheat (durum and nondurum) and barley for domestic human consumption and for export. U.S. trade officials and wheat producer groups contended that Canadian wheat trading practices, particularly the export practices of the CWB, were inconsistent with Canada’s WTO obligations and disadvantage U.S. wheat exporters in Canadian and international markets. U.S. trade officials also contended that Canadian wheat entering the U.S. market was being supported by various subsidies and that these wheat imports have been harmful to U.S. producers and that the Canadian government had certain rules and regulations in place that discriminated against imported grains at grain elevators and within Canada’s rail transportation system.

Canadian officials have countered that the CWB operates as a valid state trading enterprise (STE) under WTO rules. Furthermore, Canada maintained that its import practices and the CWB wheat export practices comply fully with international trade rules and its WTO obligations, and that Canada does not subsidize its wheat exports. In addition, U.S. wheat millers and pasta manufacturers have expressed a strong interest in maintaining their access to Canadian grain and oppose trade restrictions that might limit their access.

U.S. allegations against Canadian wheat trading practices have led to two major investigations by U.S. agriculture and international trade authorities against wheat imports from Canada, as well as the trading practices of the CWB. First, the charges that Canadian wheat entering the U.S. market was being supported by various government subsidies and that these wheat imports have had a large negative impact on local grain prices were investigated under anti-dumping (AD) and countervailing (CV) duty investigations by the U.S. International Trade Commission (ITC) starting in 2001. Second, U.S. charges concerning the trading practices of the CWB and the treatment of wheat imports by Canada were pursued under a WTO Dispute Settlement Case (DS276) that was initiated in December 2002. In response to the U.S. trade actions, Canada brought its own charges against U.S. claims within the NAFTA dispute settlement framework.

Background and Analysis. The United States and Canada are both important producers, traders, and consumers of major grain crops, including wheat. The United States is the world’s leading exporter of wheat (totaled across the major wheat classes), while Canada is the world’s leading exporter of hard red spring (HRS) and durum wheat. HRS is a crucial ingredient in the production of leavened bread, while durum wheat is used to make pasta.

⁶² Prepared by Randy Schnepf, Specialist in Agricultural Policy, Resources, Science and Industry Division of CRS.

U.S. imports of wheat and wheat flour are historically small, averaging about 3% of total U.S. supplies each year, and are generally related to specific end-use needs. About 70% of U.S. wheat imports originate from Canada — mostly of durum and HRS wheat. Despite their small volume relative to total supply, unexpected growth in U.S. imports of spring and durum wheat from Canada in the early 1990s — with import growth from about 611,000 metric tons (mt) in 1989 to 3 million mt in 1993/94, and an average of over 2.2 million mt since — has been viewed as problematic by producers in U.S. border states, especially when U.S. prices are low, as during the 1998-2001 period. Trade liberalization following the 1989 FTA (subsequently incorporated into NAFTA) has undoubtedly contributed to the expanded wheat trade. However, not all of the change in U.S.-Canadian agricultural trade can be attributed to the FTA or to any other single factor. Weather, policy changes, and world supply and demand conditions are some of the influential factors. Exchange rates have also been important. Prevailing exchange rates between the Canadian and U.S. dollars for most of the 1990s made Canadian imports cheaper for U.S. buyers and U.S. farm products more expensive for Canadian buyers.

On October 3, 2003, the ITC announced a positive injury finding and imposed punitive duties on Canadian HRS wheat imports of 14.16% (5.29% CV and 8.87% AD duties), but no duties were imposed on Canadian durum imports. Canada appealed the ITC's findings under NAFTA dispute settlement provisions. On March 10, 2005, the NAFTA panel recommended removal of the AD portion of the punitive duty. On June 7, 2005, the NAFTA panel ordered the ITC to revisit its material injury findings. Finally, in October 2005, the ITC, pursuant to the NAFTA panel's review remand, reversed its earlier finding and issued a new determination that there was no injury or threat of injury. This decision was upheld on appeal to the NAFTA panel by the North Dakota Wheat Commission, and both the AD and CV duties were removed in March 2006. As a result, Canadian Durum and HRS may freely enter U.S. markets.

U.S. charges concerning the trading practices of the CWB and the treatment of wheat imports by Canada were also pursued under a WTO Dispute Settlement Case (DS276) that was initiated in December 2002. On April 4, 2004, a WTO dispute settlement panel issued a mixed final ruling. Contrary to U.S. charges, the Panel concluded that the CWB's trading practices did not violate WTO rules for State Trading Enterprises (STEs). However, the Panel found that certain Canadian grain marketing practices were not in compliance with WTO rules. A Canadian government spokesman claimed that the ruling upheld the Canadian position that the CWB operates as a valid STE under WTO rules. This initial panel ruling regarding the CWB was upheld under appeal by the United States (August 30, 2004). With respect to the WTO ruling on Canada's treatment of imported grains, Canada was obligated to remove regulatory hurdles on imports of U.S. wheat. As a result, Canada passed legislation (May 19, 2005) that rectified its grain import and marketing system practices (effective August 1, 2005) to bring them into compliance with the WTO Panel's recommendations.

Status of the Issues. Presently, Canadian HRS and durum wheat may freely enter the United States. Meanwhile, the changes effected upon the Canadian grain marketing system pursuant to the WTO recommendations could result in increased marketing opportunities for U.S. wheat into niche markets in Canada. In addition,

some analysts suggest that the ruling will be helpful to American farmers and elevators that may at times want to ship wheat west on the Canadian rail system since now Canadian railways will have to haul U.S. wheat for the same price as Canadian wheat. U.S. wheat producer groups and the USTR remain very disappointed in the WTO Panel's ruling with respect to the CWB and are likely to aggressively pursue the elaboration of greater disciplines on STEs like the CWB in on-going and future WTO trade negotiations.

Questions.

1. How will the government of Canada respond to the growing list of external, as well as internal, charges being leveled against the CWB? Are there ways in which the CWB could become more transparent in its operations so as to reduce informational uncertainties about its operations?
2. How flexible will Canada be in negotiating greater discipline and more transparency in the operations of STE's such as the CWB in on-going WTO trade negotiations, particularly if the quid pro quo is reduced use of export subsidies by grain-export competitor nations?

Corn Trade⁶³

Issue Definition. Since 2000, U.S. corn exports to Canada have risen dramatically from previous levels. The surge in imports of U.S. corn occurred at a time when U.S. government program payments to the corn sector were also growing. The increases in both U.S. corn program payments and imports of U.S. corn drew the attention and ire of Canada's corn producing sector, which claims that U.S. corn exports were being facilitated by large U.S. government payments and being sold into Canada at below the cost of production. The Canadian Corn Producers — a coalition comprised of the Ontario Corn Producer's Association, the Fédération des producteurs de cultures commerciales du Québec, and the Manitoba Corn Growers Association — filed a domestic trade remedy complaint under Canada's Special Import Measures Act (SIMA) for the alleged "injurious subsidization and dumping of imports of U.S. corn."

On September 16, 2005, the Canadian Border Services Agency (CBSA) announced that it was beginning an investigation into alleged dumping and subsidizing of U.S. grain corn in Canadian markets in response to pressure from Canadian corn producer groups. At the same time that CBSA was conducting its investigation, Canada's International Trade Tribunal (CITT) began a parallel investigation to determine whether imports of U.S. corn were harming Canadian producers. U.S. producer groups and trade officials have argued that Canada's case is based on weak, circumstantial evidence; that it ignores several important economic factors that have contributed to growing Canadian corn imports; and that Canada's corn imports have actually fallen off since 2003. In addition, twenty Canadian corn users from the livestock, food processors, and ethanol sectors have voiced their disagreement with the Canadian Corn Producers' accusation that imports of U.S. corn are either dumped or subsidized and have expressed their opposition to this case moving forward.

Background and Analysis. The United States is the world's leading producer and exporter of corn. Since 1980, U.S. corn production has accounted for over 40% of world production, while U.S. corn exports have represented over two-thirds of world corn trade. Canada is also an important producer and consumer of corn. However, Canada's average annual corn production of 8.7 million metric tons (mt) since 2000 is substantially smaller than U.S. average production of nearly 260 million mt. Although grown widely throughout the world, corn grows best in temperate conditions with deep, fertile soils such as in the U.S. Corn Belt. Corn's agroclimatic requirements, coupled with Canada's northerly latitudes, limit Canada's corn planting to the more southerly regions of Ontario and Quebec. As a result, growth in Canada's corn production has been limited almost entirely to yield growth. In contrast, strong steady domestic demand for corn — driven by the livestock (dairy, swine, and poultry) and ethanol sectors — has outpaced domestic production and made Canada a net importer of corn, primarily from the United States, since the early 1990s.

⁶³ Prepared by Randy Schnepf, Specialist in Agricultural Policy, Resources, Science and Industry Division of CRS.

The elimination of tariffs on corn trade between the United States and Canada, first under the U.S.-Canada Free Trade Agreement (FTA) and later under NAFTA, has facilitated corn imports into Canada from the United States and strengthened the integration of the North American livestock feeding industry. Since 1989, over 99% of Canada's corn imports have come from the United States. During the 1990s, U.S. corn exports to Canada averaged less than 1 million mt per year; since 2000, they have averaged almost 2.8 million mt per year. The surge in imports of U.S. corn occurred at a time when U.S. government program payments to the corn sector were also growing. During the 1990s, U.S. corn program payments averaged \$2.7 billion per year; since 2000, they have averaged nearly \$5 billion per year. In light of these circumstances, Canadian corn growers have claimed that the United States is subsidizing and dumping corn into the Canadian market.

On November 15, 2005, the CITT announced that there was reasonable evidence that the dumping and subsidizing of unprocessed U.S. grain corn caused injury to Canada's domestic industry. A month later, the CBSA announced its preliminary determination of dumping and subsidizing of U.S. grain corn. As a result, provisional duties of \$1.65 per bushel were imposed payable on imports of U.S. corn at any time on or after December 15, 2005, including a provisional AD duty of \$0.58 per bushel and a provisional CV duty of \$1.07 per bushel. (All amounts are in U.S. dollars.) On March 15, 2006, the CBSA announced a final determination concurring with its earlier decision to impose the \$1.65 per bushel punitive tariff on imports of U.S. corn until the CITT concluded its investigation of injury to Canadian producers.

Shortly thereafter, on March 17, 2006, the United States requested WTO dispute settlement consultations with Canada concerning Canada's imposition of provisional AD/CV duties on unprocessed U.S. grain corn. In its WTO request, the United States' arguments included an accusation that Canada's CITT had relied on weak causality between imports and injury, while ignoring other more likely candidates causing injury such as exchange rate movements and unusually large world corn harvests leading to weak international corn prices.

On April 18, 2006, the CITT announced its final determination, reversing its earlier position, by issuing a finding of no injury regarding the importation of U.S. grain corn. Pursuant to this final finding, the preliminary AD/CV duties of \$1.65 per bushel were removed and all duties already assessed will be returned. Similarly, the United States' motivation for pursuing its WTO case against Canadian AD/CV duties was ended.

Status of the Issues. Presently, U.S. corn may freely enter Canada. However, the Canadian Corn Producers have announced that they are reviewing their options for pursuing further legal action against imports of U.S. corn. Such options include requesting a NAFTA bi-national panel review or possibly encouraging the Canadian government to pursue a WTO dispute settlement case. However, such actions would likely have to be based on a new line of reasoning that was not a part of the AD/CV duty case, which focused on the presence of injury to Canadian corn growers. A NAFTA panel review would involve a review of whether Canadian trade authorities (in this case, the CITT) had correctly interpreted and applied existing Canadian law in reaching their determination of no injury. In contrast, a WTO case — which can only be brought by the Canadian government, not the Canadian Corn

Producers — would likely be pursued under the Agreement on Subsidies and Countervailing Measures and would involve an investigation of whether “serious prejudice” occurred in the marketplace as a result of U.S. domestic corn program payments. Brazil’s recent success in such a WTO dispute settlement case against U.S. cotton subsidies could provide both an encouragement and a template for future action against U.S. corn subsidies.

Questions.

1. How will the government of Canada respond to continued demands from Canadian corn growers to limit imports of U.S. corn in the face of escalating U.S. program payments to U.S. corn growers?
2. If the ongoing Doha Round continues to drag on with no resolution in sight or proves entirely unsuccessful, will Canada consider bringing a dispute settlement case against the U.S. corn sector based on “serious prejudice” related to large U.S. program payments?

Cattle and Beef Trade⁶⁴

Issue Definition. The U.S. and Canadian cattle and beef industries continue to be affected by discoveries of Bovine Spongiform Encephalopathy (BSE or “mad cow” disease) in both Canada and the United States, the most recent in British Columbia in April 2006. Before this and subsequent incidents, the United States exported about 10% by value of its beef primarily to Japan, Korea, Mexico, and Canada, while Canada exported about a third of its slaughter cattle and 90% of its beef to the United States. While some U.S. producers have endeavored to keep the border closed to Canadian cattle and beef, U.S. feedlot owners and meat packers pressured USDA to readmit cattle imports from Canada. Some restrictions on Canadian imports have been lifted, and the United States is importing beef from cattle under 30 months old as well as younger live animals. The United States continues its focus on reopening foreign markets, especially Japan, to U.S. beef; after months of negotiation, Japan reopened its market to U.S. beef from young animals in December 2005. That market closed abruptly in January 2006 upon the discovery of vertical column bones in a U.S. shipment of veal. In Canada, policy-makers are supporting Canadian industry aims to become less reliant on U.S. live cattle markets by increasing Canadian slaughter capacity and diversifying export markets for beef.

Background and Analysis. Canada’s exports of live cattle to the United States averaged 1.3 million head in 2000-2002 according to USDA reports. The immediate closure of the U.S. border to Canadian live cattle on May 20, 2003, however, dealt a blow to the Canadian industry as prices for live cattle declined sharply resulting in substantial income loss to the cattle/beef industry. The price of Alberta fed steers, for example, which averaged C\$110.89/cwt (live) during the first five months of 2003 dropped to \$C37.80 by July of that year. The border was reopened in August 2003 to imports of boneless beef from younger animals, but remained closed to live cattle imports. A Minimal Risk Rule for BSE, first proposed by USDA in November 2003, would have restored most of the live cattle trade, but implementation of the rule was delayed when a Montana judge issued a temporary restraining order to halt the Canadian imports. The rule finally went into effect on July 18, 2005 and live cattle imports resumed. Since publication of the rule, 562,000 Canadian animals have crossed the border (July 2005-February 2006). In 2002, the last full year before the first Canadian case, there were 1.7 million cattle exports from Canada.

The Canadian government responded to the closure of the U.S. border to live cattle by introducing financial assistance programs for ranchers while the Canadian industry (meat processors) invested in increased slaughter capacity to relieve pressure from the build-up of the cattle inventory. Canadian government initiatives have included establishing a loan loss reserve to encourage lenders to support projects to increase slaughter capacity; streamlining inspections of new slaughter facilities by the Canadian Food Inspection Agency (CFIA); providing additional resources for CFIA inspection activities; and establishing set-aside programs for fed and feeder

⁶⁴ Prepared by Charles E. Hanrahan, Senior Specialist in Agricultural Policy, Congressional Research Service.

cattle to help maintain cattle prices before additional meat processing capacity becomes available. Private investment to increase slaughter capacity includes new facilities in Alberta, Manitoba, and Quebec. These investments include the purchase of a modular U.S. packing plant and its installation in Manitoba. A Canadian subsidiary of Cargill, Inc. also has invested in increased slaughter capacity in Canada. One consequence of these investments, according to industry analysts, is that some of the employment and value-added associated with meat processing of Canadian cattle has shifted from the United States to Canada.

For the United States, the major industry and policy concern has been the effort to re-open the export market for beef, with Japan being the major focus of attention. The value of total U.S. beef exports in 2003 was \$3.1 billion according to USDA. Japan imported about 37% of that total. South Korea was the second largest market with 24%; Mexico and Canada accounted for 20% and 10%, respectively. Canada, by contrast, exported more than a third of its slaughter weight live cattle and nearly 50% of its beef. In both cases, about 90% of these exports went to the United States. The world's second largest exporter of beef in 2002, the United States is forecast to be eighth in global exports in 2006. Canada, which was the world's fourth largest exporter in 2002, fell to seventh place in 2004, but is forecast to rise to fifth place in 2005, partly as a result of the resumption of boneless beef imports by the United States.

In late 2003, prior to the first BSE event in the United States, U.S. domestic cattle prices were at record high levels. Prices for live cattle declined right after the first BSE case but had substantially recovered by January 2004. A decline in cattle inventories, in part because of drought in cattle country, strong domestic demand for beef, and, according to some industry analysts, the prohibition of live cattle imports from Canada, kept prices relatively high during much of 2004. In contrast to Canada, where economic losses have been concentrated in live cattle markets, most of the economic losses in the United States are due to the closing of world markets to U.S. beef exports. Estimates of U.S. beef export losses range from the U.S. Meat Export Federation's figure of \$2.8 billion annually to Kansas State University's high of \$4.7 billion.

Status of the Issue. Uncertainty affects the future of beef and live cattle trade between Canada and the United States. Industry analysts identify several factors that could preclude live cattle imports from reaching pre-BSE levels. These include current lack of shipping capacity by Canada's trucking industry, hit hard during the U.S. import ban; high fuel prices that increase the cost of truck transport; a stronger Canadian dollar that could reduce incentives to sell into the U.S. market; increased Canadian slaughter capacity; reduced U.S. demand for slaughter cattle due to closure of U.S. plants that relied on Canadian cattle; and continued pursuit of legal avenues by some U.S. cattlemen to block cattle imports from Canada. The resumption of beef imports from the United States at pre-BSE levels if Japan re-opens its market could be complicated by competition from other suppliers, such as Australia and New Zealand, whose beef exports to Japan have increased substantially. Industry analysts expect, for example, that even with resumption of Japanese imports of U.S. beef, exports of Australian beef to Japan would remain at record high levels.

Questions.

1. What is the outlook for the Canadian strategy of increasing slaughter and meat processing capacity and diversifying beef export markets away from the United States? What are the economic implications of this strategy for the U.S. cattle and beef industry?
2. What are the prospects that U.S. beef exports to Japan and other Asian markets would attain pre-BSE levels if and when Japan opens its markets to U.S. beef?

Potato Trade⁶⁵

Issue Definition. Although tariffs on potatoes are zero under the North American Free Trade Agreement (NAFTA), Canada has imposed certain non-tariff barriers to trade in potatoes and other fresh vegetables.

Background and Analysis. According to the U.S. Trade Representative's (USTR's) annual report on foreign trade barriers (2006), access to the Canadian market for fresh fruits and vegetables is impeded because Canada prohibits imports of such products in packages exceeding certain standard package sizes unless the government of Canada grants a ministerial easement or exemption. To obtain such an easement, Canadian importers must demonstrate that there is an insufficient supply of the product in the Canadian market. These restrictions apply to all fresh and processed produce imports in bulk containers and have a particularly negative impact, USTR says, on U.S. potatoes, apples, and blueberries. The restrictions, however, do not apply to inter-provincial commerce. In addition, USTR points out that Canadian regulations on fresh fruit and vegetable imports prohibit consignment sales of such products in the absence of a pre-arranged buyer.

Status of the Issue. USTR has reported on these non-tariff barriers for a number of years. In the 2005 annual report on foreign trade barriers, USTR noted that the United States entered into negotiations with Canada in 2004 in an attempt to remove these trade restrictions. No progress was noted in the 2006 annual report from USTR.

Questions.

1. What is the current status of Canadian packaging requirements with respect to potatoes and other fresh vegetables?
2. What is Canada's position with respect to altering its non-tariff regulations governing trans-border shipments of bulk potatoes?

⁶⁵ Prepared by Charles E. Hanrahan, Senior Specialist in Agricultural Policy, Resources, Science and Industry Division of CRS.

Country of Origin Labeling⁶⁶

Issue Definition. Section 10816 of the Farm Security and Rural Investment Act of 2002 (P.L. 107-171) as amended requires many retailers to provide country-of-origin labeling (COOL) for fresh produce, red meats, seafood, and peanuts. Although seafood COOL began September 30, 2004, Congress delayed the implementation date for the other covered commodities until September 30, 2008. Some in Congress continue to strongly support mandatory COOL, especially after discoveries since 2003 of “mad cow” disease in five Canadian-born and two U.S.-born cattle. Others counter that COOL is a marketing, not an animal or human health, concern and should be voluntary.

Background and Analysis. Under the Tariff Act of 1930, as amended, most unprocessed agricultural commodities have long been exempt from requirements that every import be clearly marked to indicate country of origin for the “ultimate purchaser.” The 2002 farm bill required those retailers covered by the Perishable Agricultural Commodities Act, i.e., those which deal in at least \$230,000 per year in produce (fresh and fresh-frozen fruits and vegetables), to begin providing such information. Specifically covered commodities are: ground and muscle cuts of beef, lamb and pork; seafood; peanuts; and produce. These commodities are exempt if they are ingredients in processed foods, or if they are sold in dining out settings.

Passage of the law has not ended debate over the value and efficacy of mandatory COOL, particularly with regard to meats. COOL opponents continue to argue 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 there is little evidence consumers actually want labeling; and that COOL is a protectionist policy that undermines free trade. Supporters counter that compliance would not be nearly as burdensome as some large industry groups and USDA have attempted to portray 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 point out that five of seven North American cases of “mad cow” disease (bovine spongiform encephalopathy, or BSE) occurred in Canadian-born cattle, yet the United States is permitting the importation 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.)

The Canadian government’s views generally parallel those held by other opponents of mandatory COOL. Canadian officials had earlier stated that they would challenge the COOL law as trade distorting under the North American Free Trade Agreement (NAFTA) and the World Trade Organization (WTO) Agreements.

Status of the Issue. The 2002 farm bill had called for mandatory COOL to be implemented by September 30, 2004. However, Congress has twice postponed

⁶⁶ Prepared by Geoffrey S. Becker, Specialist in Agricultural Policy, Resources, Science and Industry Division of CRS.

the requirement. P.L. 108-199 (the omnibus FY2004 appropriations law) delayed this date for all covered commodities, except farmed fish and wild fish, until September 30, 2006. The FY2006 USDA appropriation (P.L. 109-97; H.R. 2744) postponed the date for two more years, until September 30, 2008.

Pending in the House Agriculture Committee is legislation (H.R. 2068) introduced by its chairman that would replace the mandatory program for meats with a voluntary program. The Senate companion bill is S. 1333; another Senate bill (S. 1300) would make COOL voluntary for all of the covered commodities. COOL debate was fueled partly by a USDA rule, published January 4, 2005, permitting younger live cattle to enter the United States from Canada. Among pending bills to modify this rule are bills (H.R. 384, S. 108) that would have prohibited implementation of the Canada rule in any year unless retail COOL for meat was in effect.

Questions.

1. Does Canada have country of origin labeling programs, and how do they compare to those for which implementation is pending in the United States?
2. Does Canada still intend to challenge the COOL law as trade distorting under the WTO and NAFTA, and if so, what, specifically, are its arguments?
3. What is the relationship if any between COOL and Canada's animal identification program?

Waste Issues⁶⁷

Issue Definition. Since 1991, the Canadian province of Ontario has shipped substantial amounts of solid waste to the United States for disposal. The issue has received additional attention since late 2002, when Toronto announced it would close its last landfill and begin shipping all of its waste to Michigan. Some of the communities on the receiving end of such waste have pressured Congress for legislation to allow them to restrict out-of-state and out-of-country waste from disposal, thus far without success. Should such waste flows be limited or subject to regulation?

Background and Analysis. Canada and the United States have open borders for waste shipments, and in general, waste has flowed across the border in both directions without incident. The United States does not report data regarding such shipments on a regular basis, but information is available from Environment Canada and from some U.S. states. Available data distinguish hazardous waste from other solid waste. The United States appears to be a net exporter to Canada of hazardous waste, but is a net importer of non-hazardous solid waste.

Hazardous Waste. According to Environment Canada, Canada imported 416,000 metric tons of hazardous waste and hazardous recyclable materials in 2004, almost entirely from the United States. Exports of hazardous waste and hazardous recyclable materials from Canada (mostly to the United States) were 308,357 metric tons. Canada's imports of hazardous waste have exceeded its exports in each of the last seven years for which data were available. Michigan, New York, and Ohio were among the leading sources of U.S. hazardous waste exports.

Since 1985, the Solid Waste Disposal Act (at 42 U.S.C. 6938) has required exporters of hazardous waste to notify the Environmental Protection Agency and the receiving country. Exporters are required to provide information concerning the types and quantities of waste to be exported, and to report annually the total amount of waste exported to any country. Since 1986, Canada and the United States have also had a bilateral agreement governing hazardous waste exports. This agreement requires both countries to notify each other and provide information concerning the types and quantities of waste to be exported. Environment Canada and the U.S. Environmental Protection Agency are the agencies charged with implementing the agreement.

Non-Hazardous Solid Waste. There are no federal notification or reporting requirements for shipments of *non*-hazardous waste, including municipal solid waste (MSW), construction and demolition (C&D) waste, medical waste, and non-hazardous industrial waste, nor is there any administrative authority to restrict imports. (The bilateral hazardous waste agreement was amended in 1992 to require notification prior to shipments of municipal solid waste, but, for lack of legislative authority, the amendment was never implemented.) It is the shipments of municipal solid waste that have proven controversial.

⁶⁷ Prepared by Jim McCarthy, Specialist in Environmental Policy; Resources, Science, and Industry Division of CRS.

Although there are no notification or reporting requirements for these wastes at the federal level, many state governments do require the operators of solid waste management facilities to report the origin of waste received for disposal. According to these data, the Canadian province of Ontario has shipped major quantities of such waste (principally MSW and C&D waste) to the United States (particularly Michigan) in recent years. In FY2005 (October 2004 - September 2005), Michigan reported that it received 3.6 million tons of non-hazardous waste from Canada, an increase of 2.8% from the previous year. Imports from Canada to Michigan have increased 80% since fiscal 2002. In January 2003, the City of Toronto closed its last remaining landfill and began shipping all of its solid waste to Michigan. As a result, waste imports from Canada have become a controversial issue.

Although Canadian waste imports continue to grow, the City of Toronto has implemented a number of recycling/diversion programs that have reduced its shipments to Michigan and has committed to the elimination of such shipments by 2012. The city says that it has already made substantial progress in reaching its goal and now sends fewer than 100 trucks of waste per day, down from a peak of 142 in 2003. According to the city, Canada's shipments to Michigan are growing because private haulers have increased their shipments from industrial, commercial, and institutional sources. Private haulers account for 75% of the shipments to Michigan, according to the city.

Status of the Issue. In the present Congress, several bills have been introduced concerning interstate and international shipments of waste. The most prominent of these, H.R. 2491 (Gillmor), was reported by the House Energy and Commerce Committee on September 27, 2005. The bill would implement the bilateral Agreement Concerning the Transboundary Movement of Hazardous Waste between the United States and Canada, as amended in 1992 to deal with municipal solid waste shipments between the two countries. It would also authorize states to restrict imports of foreign MSW if they do so prior to the bilateral agreement's implementation. Under the latter provision, states would have a window of up to 24 months after the bill were enacted to impose restrictions of their choosing on the receipt of foreign MSW, and those regulations could remain in effect as long as the state desires.

H.R. 2360, the Department of Homeland Security Appropriations bill, could also have affected Canadian waste imports. The Senate version of the bill would have required the Bureau of Customs and Border Protection (CBP) to report to Congress within 90 days after enactment (1) whether methodologies and technologies used to screen for and detect chemical, nuclear, biological, and radiological weapons in municipal solid waste are as effective as those used to screen for such materials in other items of commerce entering the United States; and (2) what actions CBP will take to achieve comparability, if such methodologies and technologies are less effective. If CBP failed to fully implement actions in the report to achieve comparability within six months, then the Secretary of Homeland Security would have been required to deny entry into the United States to commercial motor vehicles carrying municipal solid waste until the Secretary certified to Congress that screening of such waste comparable to that used to screen other items of commerce had been achieved. These provisions were not included in the enacted bill.

Questions.

1. Given the concerns in receiving states over shipments of waste from Canada to the United States, would Canada be willing to work with the United States to develop a bilateral reporting and inspection system to measure exports and imports of all kinds of waste between the two countries and assure the safety of such shipments?
2. Many landfill operators have reached what are called “host community agreements” with local governments, under which the local government receives financial benefits or agreed services in return for accepting out-of-area waste. Should waste imports be limited to communities in which the landfill owner or operator has negotiated a host community agreement with the local government? If so, should the agreement meet some minimum standards (e.g., specifically authorizing waste imports, setting minimum requirements for host community fees, etc.)?

Electric Reliability⁶⁸

Issue Definition. Reliability of electricity supply is a significant concern in both Canada and the United States. As was shown during the 2003 blackout, both countries are interconnected and operational control issues in one country can affect the electric system in both countries. The North American Electric Reliability Council (NERC) is an industry organization whose membership has been voluntary. Its mission is to ensure that the bulk power system is reliable, adequate, and secure. The ten regional reliability councils of NERC account for virtually all the electricity supplied and used in the United States, Canada, and a portion of Baja California Norte, Mexico. Among its responsibilities, NERC develops reliability guidelines for its member utilities. The Energy Policy Act of 2005 (P.L. 109-58) requires the formation of an Electric Reliability Organization (ERO) with enforceable standards. At issue is whether the provincial and federal government of Canada will enforce Federal Energy Regulatory Commission (FERC) approved reliability standards.

Background and Analysis. There are three components to electric power delivery: generation, transmission, and distribution. Electric generators need to move their power to their ultimate customers through the transmission system, crossing state and international borders. The current system allows for power transfers within, but not between, three major regions of the United States, Canada, and parts of Mexico: the area west of the Rockies (Western Interconnection), Texas, and the Eastern Interconnection. Because of these international interconnections, operational control issues in one country may affect the reliability of the power supply in the neighboring country.

The United States is a net importer of electricity from Canada. On average, 60% of total Canadian generation is produced in hydroelectric plants. Canada began 2004 with drought conditions, resulting in greater electricity imports from the United States. As the year progressed, water levels in Canada improved, resulting in a 62% net increase in exports to the United States compared to 2003. In 2004, net imports of electricity from Canada were 10.7 terawatt-hours. During the same period, total sales to ultimate consumers of electricity in the United States were 3,717 terawatt-hours.

Transmission Constraints. Power transfers between the United States and Canada are limited by the physical infrastructure of the system and its operation. One method to improve reliability is to increase transmission capacity (see CRS Report RL32075, *Electric Reliability: Options for Electric Transmission Infrastructure Improvements*, by Amy Abel). In May 2003, the National Energy Board of Canada conditionally approved New Brunswick Power's application for a new 345-kilovolt international power line that will cross at the Maine border. Bangor Hydro has received the required permits and has begun clearing the right-of-way within the United States.

⁶⁸ Prepared by Amy Abel, Specialist in Energy Policy, Resources, Science, and Industry Division of CRS.

Three types of constraints limit the transfer capability within the existing transmission system: thermal constraints, voltage constraints, and system operating constraints. Thermal constraints limit the capability of a transmission line or transformer to carry power because the resistance created by the movement of electrons causes heat to be produced. Overheating can lead to two possible problems: The transmission line loses strength, which can reduce the expected life of the line, and the transmission line expands and sags between the supporting towers. This presents safety issues as the lines approach the ground as well as reliability concerns.

Voltage can be likened to the pressure inside the transmission system. Constraints on the maximum voltage levels are set by the design of the transmission line. If voltage levels exceed the maximum, short-circuits, radio interference, and noise may occur. Low voltages are also a problem and can cause customers' equipment to malfunction and can damage motors.

System operating constraints refer to reliability and security. Maintaining synchronization among generators on the system as well as preventing the collapse of voltages are major aspects of the role for transmission operators. NERC guidelines require utilities to be able to handle any single outage through redundancy in the system. When practical, NERC recommends the ability to handle multiple outages within a system. Reducing the constraints on the system through technology improvements is one way to increase the transfer capability over existing lines.

The Blackout of 2003. On August 14, 2003, operational errors by FirstEnergy in Ohio caused an estimated 50 million people in the Midwest, the Northeast United States, and Ontario to lose power. NERC identified seven violations of NERC standards by FirstEnergy and the Midwest Independent System Operator (MISO) and PJM interconnection. In addition to several violations of system control, FirstEnergy failed to have an adequate tree trimming program to prevent the blackout. However, there is currently no NERC vegetation management standard for utilities. The U.S.-Canada Power System Outage Task Force identified institutional problems with NERC reliability standards. In particular, it noted that NERC has no structural independence from the electric utility industry it represents and has no authority to develop strong reliability standards and to enforce compliance with those standards.

Status of the Issue. The Energy Policy Act of 2005 provides for an Electric Reliability Organization (ERO) to develop and enforce mandatory reliability standards. FERC issued a final rule on the certification of the ERO on February 2, 2006. The rulemaking included provisions for the approval and enforcement of mandatory electric reliability standards. On April 4, 2006, NERC filed its application to become the ERO in both the United States and Canada. NERC plans to begin operations as the ERO on January 1, 2007.

Questions.

1. NERC has applied to be the ERO to the provinces of British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Quebec, New Brunswick, and Nova Scotia as well as to the National Energy Board. Will Canadian regulators approve and enforce

identical standards? Without identical standards and enforcement, the reliability of the electric power system could be reduced.

2. Encouraging investment to improve reliability has not been a goal of electric regulatory restructuring. In a more competitive electric market, utilities minimize unnecessary expenses. For example, FirstEnergy implemented cost saving measures by reducing the frequency of tree trimming activities, contributing to the blackout of 2003. Compliance with reliability standards may involve new capital investment and/or expenses. Will regulators in both the U.S. and Canada approve recovery of these costs?

Natural Gas Pipeline from Alaska⁶⁹

Issue Definition. In October 2004, Congress approved the Alaska Natural Gas Pipeline Act, which authorizes, in principle, a pipeline to carry natural gas from Alaska's North Slope, establishes rules governing its construction, and authorizes federal guarantees on pipeline project loans. In early March 2006, the three North Slope oil producers and the state of Alaska agreed on a contract to build the pipeline. The destination of the gas is expected to be markets in the lower 48 states. A proviso of the act effectively prevents the pipeline from passing through or near the Mackenzie Delta gas fields in northwest Canada. This prohibition appears likely to limit the potential gas throughput inasmuch as Canada is moving to construct its own pipeline from the Mackenzie Delta fields. Thus, the two partly competing projects may diminish each other's economic viability.

Background and Analysis. Alaskan natural gas is a major potential U.S. energy resource that has been hardly tapped. The Alaska Department of Natural Resources estimates recoverable gas reserves in the North Slope oil fields at about 30 trillion cubic feet (tcf), which is the energy equivalent of about 5.3 billion barrels of oil. Natural gas is believed to be under the Arctic National Wildlife Refuge (ANWR) as well, although seemingly not as much as already discovered in the rest of the North Slope. The already discovered natural gas resource has not been developed because of a lack of a cost-effective means of transportation to major markets; estimated costs of construction have precluded serious consideration of transporting the gas by pipeline. Most of the gas produced so far on Alaska's North Slope — 80% of the 8-9 billion cubic feet produced annually — has been reinjected into the ground. The small amounts produced are used for operations in conjunction with oil production and transportation, such as powering oil through pipelines.

Construction of a pipeline to transport natural gas to North American markets and/or a warm-water port for shipping liquefied natural gas (LNG) could enhance North Slope oil and gas economics and the commercial promise of ANWR. Recent steep increases in gas prices and projections of continued high prices have suggested improvement in the relationship between market prices and the combined cost of known North Slope gas resources and of pipeline transportation. Potential profitability of the authorized pipeline is enhanced by the \$18 billion in loan guarantees for the \$20 billion project.

Congress created a statutory framework for an Alaska natural gas pipeline in the mid-1970s. Legislative authority for designation of the route, and for the U.S. role in the approval, construction and operation of such a pipeline, was established in the Alaska Natural Gas Transportation Act of 1976 (15 USC 719 *et seq.*). Under that authority, still in force, a gas pipeline would parallel the existing Alaska oil pipeline from the North Slope to Fairbanks, then head southeastward along the Alaska Highway and into Canada via the Yukon Territory, British Columbia, and Alberta. This, the Alaska Natural Gas Transportation System (ANGTS), was approved by the U.S. and Canadian governments. Phase I of the ANGTS pipeline was completed in

⁶⁹ Prepared by Bernard A. Gelb, Specialist in Industry Economics, Resources, Science, and Industry Division of CRS.

the early 1980s and is in operation. Its two legs, stretching from a collecting point in Alberta in the directions of the U.S. West Coast and the Midwest, respectively, deliver one-third of Canada's total annual gas exports to the United States. The third leg, connecting North Slope to the "prebuilt" network, has never been started.

Alaska has enacted legislation that bans construction of a gas pipeline in northern state waters, while supporting a pipeline to the south. Under the shorter, less costly, northern route, wellhead prices (determined by subtracting transportation cost from market price) would be higher, and royalties to the state would be higher (the gas resources are state-owned). But state officials see greater gain through the income multiplier effect of construction within the state and Alaskan communities' greater access to the gas supplies. There are some questions concerning who will construct and operate the Canadian portion of the pipeline originating in Alaska, but the Canadian government has promised that these issues will not impede completion of the project. The 3,400-mile U.S.-authorized pipeline likely would not enter service until at least 2014.

Canada supported a natural gas pipeline that would travel from the North Slope through Canada and opposed any unilateral selection of routes by the United States. The Canadian government believes that the private sector is best suited to decide the route, subject to regulatory and environmental review procedures. Canada has an interest in selling more oil and natural gas to meet U.S. energy needs. Among pipeline routes receiving less attention than those described above, the most prominent is one entirely in Alaska, which would parallel the existing oil pipeline and terminate at a yet-to-be built tanker port, at either Valdez or Cook Inlet, that would liquefy the gas.

A consortium of four companies and a group representing aboriginal peoples plan to build the Mackenzie Valley gas pipeline, which is intended to carry natural gas from inside the Arctic Circle to northern Alberta, where it would flow into the existing natural gas transportation system. There also would be a parallel pipeline to carry natural gas liquids (NGL). The first stage of regulatory public hearings began in January 2006. Inasmuch as the multistage U.S. regulatory process has not begun, it appears that the Canadian project is somewhat ahead of the U.S. project.

Status of the Issue. Both the United States and Canada are moving toward the construction of natural gas pipelines built from their respective Arctic regions that will partly compete with each other for markets in the Lower 48 states and in southern Canada.

Questions.

1. Will the Canadian project begin construction long enough before the U.S. project begins so as to minimize competition between the projects for inputs such as labor and steel?
2. To what extent might the partly competing natural gas pipelines, once completed, diminish the economic viability of each other?

Northern Energy Development⁷⁰

Issue Definition. Should the United States proceed to develop energy resources thought to be in the coastal plain of the Arctic National Wildlife Refuge (ANWR)? And if it chooses to do so, how would Canadian interests, especially those of the Gwich'in people who live on both sides of the Alaska/Yukon boundary, be affected? Canada opposes ANWR development, arguing a need to protect the calving grounds of a caribou herd heavily used by Gwich'in in both countries. (See also *Natural Gas Pipeline* above, a closely related issue.)

Background and Analysis. A major element of the energy debate in the 109th Congress has been whether to approve energy development in the Arctic National Wildlife Refuge (ANWR) in northeastern Alaska, and if so, under what restrictions, or whether to continue to prohibit development to protect the area's biological resources. ANWR is an area rich in fauna, flora, and oil potential. Development proponents argue that ANWR oil would reduce U.S. energy markets' exposure to recurring crises in the Middle East, create many jobs in Alaska and elsewhere, boost North Slope oil production, and extend the economic life of the Trans Alaska Pipeline System. They maintain that ANWR oil could be developed with minimal environmental harm, with a footprint limited to 2,000 acres of the 19 million acre Refuge. Opponents argue that intrusion on this ecosystem cannot be justified on any terms; that it should be designated as wilderness; that oil found (if any) would provide little energy security and could be replaced by cost-effective alternatives; and that job claims are exaggerated.

Canada opposes energy development in ANWR primarily because it might disturb calving of the Porcupine Caribou Herd (PCH). The PCH is covered under the Agreement Between the United States of America and Canada on the Conservation of the Porcupine Caribou Herd, which entered into force on July 17, 1987. The objective of the agreement is to conserve the herd for customary, traditional uses by peoples on both sides of the international boundary, with disputes to be settled by consultation between the parties. Since it was an executive agreement, no implementing legislation was required. The U.S. agency primarily responsible for implementing the agreement is the Fish and Wildlife Service.

The range of the PCH is centered on the Porcupine River in the United States and Canada; the herd winters south of the Brooks Range in both nations. The herd of about 130,000 animals provides the staple diet of Gwich'in hunters in Alaska, the Yukon, and the Northwest Territories. It is also the source of cultural tradition and a focus of religious ceremonies. Fearing that oil development in the herd's most frequent calving ground in ANWR's coastal plain area might jeopardize their livelihood and even their culture, the Gwich'in on both sides of the border have vigorously opposed development. Indeed, the concern over the PCH has invigorated cross-border contacts between Gwich'in for more than a decade.

⁷⁰ Prepared by M. Lynne Corn, Specialist in Natural Resources Policy; Resources, Science, and Industry Division of CRS.

Under current law, Alaskan Gwich'in would receive relatively little economic benefit from development, successful or otherwise. (Canadian Gwich'in would receive no direct economic benefit; there are no known reports of indirect benefits.) In contrast, Inuit Natives (primarily from Barrow and Kaktovik) along Alaska's North Slope would receive tax revenues, as well as bonus, royalty, and rent payments if successful development took place on Native-owned subsurface lands within ANWR. As a result of their experience with Prudhoe Bay development, and of its effects on the smaller Central Arctic Herd (CAH), many Inuit feel that ANWR development can proceed without significant risk to the PCH. Other Alaskan Inuit are more cautious, with villagers such as some in Nuiqsut, west of ANWR, arguing that a nearby existing development has not generated expected levels of employment or dividends, while exacerbating social problems or driving a local caribou herd farther away.

The Canadian portion of the PCH calving ground is protected in Ivvavik National Park. While some energy exploration has taken place in the Canadian portion of the calving area, Canadians argue that that activity occurred only before the government was aware of the importance of the area to the PCH. Indeed, some Canadian industry officials have complained of government hostility to development in the northern areas of the country, based on what they perceive as overzealous environmental concerns. Critics note that the Canadian part of the calving area was protected not only after the area's importance to caribou was known, but also after it was known to lack commercial energy resources. Canada is proceeding with development plans farther east, in the Mackenzie River Delta.

Status of the Issue. Canadian Prime Ministers have raised the issue of development in the PCH calving range on several occasions over the years, and their government has sent numerous position papers to various U.S. agencies and departments. In first session of the 109th Congress, several attempts were made to pass ANWR development legislation, but none succeeded. It remains to be seen whether a final FY2007 budget resolution will contain assumptions concerning ANWR revenues. If it does, and a reconciliation measure is considered by the House and Senate, it is expected to be a vehicle for ANWR legislation, since reconciliation is not subject to a filibuster. The Alaska delegation and the Bush Administration remain strong proponents of ANWR development.

Questions.

1. How can one reconcile the opposition of the Canadian government to energy development in ANWR (where the PCH calves in most years) to its support of an "over-the-top" natural gas pipeline? Would the pipeline be sited to avoid the areas that the PCH tends to use for calving in the years when it does not reach ANWR in time for calving?
2. What energy activities are going on currently in the northern Yukon and the Northwest Territories? What activities have occurred in the last two years? How do these activities affect calving grounds, migration routes, and wintering areas in Canada? Are there any known effects on the PCH?

3. If Congress were to decide to open ANWR to development, are there specific mitigation practices that Canada is seeking for the protection of caribou? For the protection of other marine or terrestrial species?

Status of Polar Bears⁷¹

Issue Definition. To what extent is the polar bear, *Ursus maritimus*, threatened by changing conditions in the Arctic? What, if any, are the responsibilities of signatory nations to the 1973 Agreement on the Conservation of Polar Bears in relation to environmental change? Are any new activities or programs warranted to address changes in the Arctic that affect polar bears?

Background and Analysis. Polar bears are circumpolar carnivores, requiring ice-covered waters to find and prey upon seals. The goal of the 1973 international agreement is to protect ecosystems of the bears, particularly their denning and feeding areas and migration routes.

An October 2003 article in the journal *Nature* reported that, in recent decades, the extent of Arctic sea ice has declined significantly as a response to climate warming; ice break-up in many areas is occurring earlier and freeze-up later.⁷² The polar bear, which relies on sea ice to hunt for seals, could find its habitat under increasing threat. Longer ice-free periods during the Arctic summer leave polar bears stranded onshore for longer periods. A delay in freeze-up causes polar bears to lose critical fat reserves, affecting reproduction and the ability of pregnant females to produce enough milk for their cubs. In addition, a reduction in the extent and thickness of the sea ice will likely encourage the development of increased commercial and tourist ship traffic in areas inhabited by polar bears. Such increased ship traffic could exacerbate poor sea ice conditions for polar bears and disturb these bears such that they avoid high traffic areas.

On December 15, 2005, the Center for Biological Diversity, along with Greenpeace and the Natural Resources Defense Council, filed suit against Secretary of the Interior Gale Norton and the U.S. Fish and Wildlife Service to force the Bush administration to respond to a petition to list polar bears under the Endangered Species Act (ESA). On February 8, 2006, the Fish and Wildlife Service announced that a petition to list the polar bear as threatened under the ESA presented substantial scientific and commercial information indicating that listing the polar bear may be warranted. As a result, FWS has initiated a status review of the polar bear to determine if the species should be proposed for listing. Polar bears currently are listed in Appendix II of the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES); Appendix II identifies species whose trade must be controlled to avoid use incompatible with their survival.

Status of the Issue. This is an emerging issue; aspects of this issue are not fully developed.

⁷¹ Prepared by Eugene H. Buck, Specialist in Natural Resources Policy; Resources, Science, and Industry Division of CRS.

⁷² Seymour Laxon, Neil Peacock and Doug Smith, "High Interannual Variability of Sea Ice Thickness in the Arctic Region," *Nature*, v. 425 (Oct. 30, 2003): 947-950.

Questions.

1. What cooperative efforts might be required to address concerns for polar bear survival?
2. How might the United States and Canada approach the prospect of increased maritime transport through the Arctic so as to minimize the disturbance to polar bears?
3. What is the role of the Canadian federal government versus provincial and territorial governments in managing polar bears?