



TaxNewsFlash Canada

Canada and U.S. Reach Agreement on Trade Deal

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Many Canadian importers and exporters will welcome news that Canada has reached a tentative trade deal with the United States and Mexico. The new deal, to be known as United States-Mexico-Canada Agreement (USMCA), is reported to take effect in late 2019 or 2020. The agreement follows extensive negotiations to revise the North American Free Trade Agreement (NAFTA).

The new USMCA provides some clarity on contentious trade issues, particularly for the dairy and automotive industries. Specifically, the agreement allows U.S. dairy producers additional access to Canada's market while limiting the effects of Canada's existing supply management system. The USMCA also exempts Canadian-made autos and auto parts under a specific quota from U.S. tariffs, among other consequential changes.

The 25% tariff on steel, and 10% tariff on aluminum and other specified products that were recently introduced by Canada and the United States will remain in place. However, the parties are continuing to discuss this matter separately.

Now that Canada has agreed to sign onto the USMCA, it will have to receive approval from Canada's Parliament as part of the ratification process. However, since the text of the USMCA is not expected to change, Canadian businesses should start to carefully determine the effect of the new agreement and make adjustments in advance of the effective date. Some of the highlights of the USMCA are discussed below.

Background

Canada, Mexico and the United States have decided to enter into a trilateral trade agreement after more than a year of talks and negotiations to update NAFTA, which came into effect in 1994. During the negotiations, the United States also imposed a 25% tariff on steel and a 10% tariff on aluminum imports that applies to a wide range of products imported into the United States from most of its trading partners, including Canada and Mexico. In response, Canada and Mexico imposed their own countermeasures on U.S. imports.

For details, see [TaxNewsFlash-Canada 2018-25, “Canada Announces Surtaxes in Response to U.S. Tariffs”](#) and [TaxNewsFlash-Canada 2018-29, “Canadian Trade Surtaxes Start July 1”](#).

Dairy industry

The United States will expand its ability to import certain dairy products into Canada, under the USMCA. The agreement provides the United States with a level of access to Canada’s market that is expected to be slightly greater than the access that Canada recently provided under the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The USMCA will also end Canada’s special pricing for Milk Class 6 and 7 (i.e., diafiltered or ultrafiltered milk) so that prices will be more consistent with their U.S. equivalents.

Automotive industry

The USMCA includes new automotive rules of origin that require 75% of a vehicle's parts to be made in Canada, Mexico or the United States, a significant rise from the current 62.5% requirement. This change will be implemented over a five-year transition period after the agreement enters into force. Further, the new rules require 30% of the work performed on the vehicle to be done by workers earning \$16 per hour, with a gradual increase to 40% of the work performed by 2023 (or three years after the date that the agreement enters into force, whichever is later).

Canada will be afforded exemptions from potential U.S. tariffs on automotive goods, up to specified limits. In particular, pursuant to a side letter, Canada will be excluded from tariffs on 2.6 million passenger vehicles, light trucks, and USD\$32.4 billion of auto parts imported from Canada.

Duty-free shopping limits

The USMCA raises the minimum purchase price for duties and taxes to apply to goods shipped into the country, such as by online shopping (i.e., the de minimis threshold). Under the USMCA, all items shipped into Canada worth more than CDN\$40 will be subject to GST/HST, and duties will be applied to goods worth more than CDN\$150. Previously, duty and GST/HST applied to goods valued more than CDN\$20.

Other trade issues

Among other changes, the USMCA contains additional provisions to:

- Preserve the existing trade dispute settlement mechanism on anti-dumping and countervailing duty decisions (formerly in Chapter 19, now in Chapter 31)
- Phase-out the investor–state dispute settlement mechanism that allowed corporation to sue governments for interfering in their business (formerly in Chapter 11)
- Increase intellectual property protections (i.e., more stringent patents and trademarks for biotech, financial services and other industries).

The USMCA is also accompanied by 12 side letters tackling additional issues such as the treatment of wine, water, and cheese.

KPMG observations

At first glance, it might look like only modest modifications were made to the original NAFTA. However, upon a closer look, the USMCA is much more complex. It's a brand new agreement and must be approached that way. Businesses will have to carefully review the complicated details included in the USMCA to understand and assess its potential impact, including identifying specific opportunities and risks.

We can help

KPMG's Trade & Customs team are well-positioned to help you analyze the impact of these trade-related measures and strategize the most effective ways to minimize the effects on your business. Please contact a KPMG's Trade & Customs professional in Canada:

Bob Sacco
GTA Trade and Customs Leader
416 777 3693
bobsacco@kpmg.ca

Angelos Xilinas
Partner, Trade and Customs
604 691 3479
axilinas@kpmg.ca

Lisa Zajko
Partner, Trade and Customs
416 224 4210
lzajko@kpmg.ca

Joy Nott
Partner, Trade and Customs
416 228 7175
jnott@kpmg.ca

kpmg.ca



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