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# C.D. Howe Institute BACKGROUND

INTERNATIONAL ECONOMIC POLICY

## Beyond the Border and Back to the Future:

Seizing the Opportunity to Enhance Canadian  
and US Economic Growth and Security

Daniel Schwanen



### **In this issue...**

The ambitious Action Plan to be created by Canada and US leaders can avoid failure if mechanisms are put in place to ease flows of trade and people across the border – and protect individual rights.

# THE STUDY IN BRIEF

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The leaders of Canada and the United States have announced an ambitious vision for perimeter security and economic competitiveness between the two countries. They have charged a working group with producing a multi-year Action Plan that will turn this vision into reality. The vision is centered on the idea that performing inspection and other formalities well before shipments and people arrive at the busy bilateral border will ease costly delays there, and that this can be achieved while simultaneously enhancing security and reducing costs for secure trade and for individuals.

Given the high degree of personal and trade interaction between the two economies requiring frequent border crossings, the initiative makes sense. However, the Action Plan could be derailed if it does not pay attention to overarching considerations such as protecting individual rights and guarding against the misuse of confidential information. It may also suffer from insufficient momentum if left to the vagaries of political attention.

Given these considerations, the study proposes light joint mechanisms dedicated to making the vision a success. They include:

- a dedicated bilateral office, tasked with facilitating implementation of the plan, reporting to the two federal governments but working in close cooperation with communities, agencies, sub-federal levels of government, and legislators;
- an independent annual audit of security practices on both sides of the border, to provide joint, evidence-based assessment of mutually acceptable levels of security;
- an annual independent audit of border-related practices, aimed at informing governments on the effectiveness of resources dedicated to ensuring secure, efficient border passage;
- an ombudsperson with power to inquire about and prod agencies to redress misuse of information collected and shared for the purpose of border security clearance; and
- a “single window” of information and assistance for small businesses and others, to reduce costs of pre-clearance and traceability requirements.

The study concludes that these new mechanisms can draw inspiration from existing ones that help provide the mutual trust, dedication and expertise necessary to successfully manage water issues between Canada and the United States.

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## ESSENTIAL POLICY INTELLIGENCE

A rare window of opportunity exists for Canada and the United States to enhance their policies and procedures relating to their common border, to reduce security risks, and to foster more fruitful flows of commerce. This window was opened on February 4, 2011, by Prime Minister Stephen Harper and President Barack Obama when they issued a joint Declaration on a Shared Vision for Perimeter Security and Economic Competitiveness (United States 2011).

The two countries' strategic interests in border issues are strongly aligned. Both countries, of course, want to keep cross-border security risks as close to zero as possible, but since the 2008 recession, both have additional incentives to increase the efficiency with which secure trade and travellers can cross borders. For its part, the United States has launched a drive to promote exports, including through the removal of unnecessary border and regulatory obstacles to trade. Indeed, one of the surest signs that the United States is seriously predisposed to completing this initiative with Canada is that it has undertaken similarly motivated initiatives with other countries. Furthermore, Canada's relative economic strength makes it an attractive market for US-based businesses. At the same time, however, the fiscal discourse in both countries has shifted decisively toward austerity, albeit in combination with fierce resistance to increased taxes. This means that there is a sharp focus in

both countries on efficiencies and cost savings, including in border- and security-related agencies.

Canada must seize this opportunity. Its exports to the United States are tilted more toward manufactured goods than are its exports to other countries,<sup>1</sup> and Canada relies, in turn, on US inputs for many of these exports. Modern manufacturing requires secure, efficient, and rapid passage across the border for myriad components, often for the same good at different stages of fabrication, as well as for the people involved in making and selling these products. Easing the border crossing also would improve the ability of individuals to earn income by providing services as diverse as nursing or machinery repairs, for example, that might be needed in the neighbouring country.

The choice of the word "competitiveness" in the declaration appropriately underscores the reality that Canada and the United States make things together, and that the two countries therefore would derive enhanced value from being able to do so less impeded by border friction. This is especially relevant as trade barriers have been coming down in other regions of the world, in many cases enhancing their competitiveness relative to that of Canada and the United States. "Making things together" is also why, as the declaration emphasizes, the two countries need to secure their joint critical infrastructure and cyberspace, apart from their more direct contribution to Canadians' and Americans' standards of living.

The declaration evokes a "new long-term partnership" and sets up a "Beyond the Border Working Group," reporting directly to the two countries' leaders, to develop a joint Action Plan to realize the declaration's goals. The Working Group has been considering a long list of technical ideas submitted by various groups and experts for enhancing both security and ease of passage at the

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1 Excluding energy trade, which is overwhelmingly not affected by physical border inspection issues, Canada's exports to the United States by value are more likely to consist of finished manufactured goods than are Canada's exports to other countries. This is mostly, but far from exclusively, due to auto trade (Statistics Canada 2011, table 3-2, and author's calculations).

border. Many of these would build on or extend the use of currently available programs and processes. Nevertheless, the window of opportunity to enhance security, facilitate mutually beneficial trade, and reduce costs could close quickly in the run-up to the 2012 US presidential elections. Time is therefore of the essence.

For Canada, a major strategic objective must be not only to secure a one-off reduction in costs related to cross-border transactions, but also to reduce the likelihood that future actions by US administrations might increase those costs for unwarranted reasons. Therefore, the Action Plan needs to deal with the continued nurturing of a trusted relationship, without which a perimeter approach, inherently involving fewer checks made at the physical border, cannot work. This, presumably, is what the declaration means by a “new long-term partnership.” Accordingly, in this *Backgrounder*, I suggest that the partnership requires novel sustaining bilateral mechanisms dedicated to its success. To see what kind of mechanisms are needed, however, it is necessary to review the key substantive issues that should be addressed.

## What Needs to Be Done, in Short

Let me begin by drilling down from the strategic goals outlined above to some of the specifics of what needs to be accomplished, and the main sticking points associated with those specifics.

Ensuring that cross-border transactions occur at minimal risk, consistent with the goals of Canada and the United States, involves three types of measures. First, it is necessary to move security-related verification mechanisms and personnel away from the actual border (an essential feature of the “perimeter” concept), while simultaneously improving the two countries’ abilities to distinguish between secure and less secure shipments and individuals potentially headed for the border. Second, inspection at the border needs to focus more on potentially high-risk movement and less on secure shipments and individuals. This could be done, by, for example, reducing unnecessary

regulatory differences, agreeing mutually to recognize the result of each other’s inspections, or increasing limits on duty-free cross-border shopping. Third, infrastructure and the efficiency of inspection at the border itself need to be improved.

These three classes of measures are uncontroversial in principle, but need to be designed and implemented carefully if they are not to run afoul of overarching concerns such as the protection of individual rights and privacy – which the two countries’ leaders stressed in the declaration – as well as of confidential commercial information and the need for governments to raise revenues efficiently to cover program costs. More prosaically, such measures should not be permitted to run aground because of bureaucratic or other vested interests seeking to maintain the status quo.

### *Identifying Security Risks Away from the Border*

The reality of the perimeter concept embodied in the first class of measures is that the Canadian authorities will have to treat certain activities or persons that the United States considers risky, but that Canada might not, differently from those neither country considers as posing a risk. Ideally, this different treatment will affect “risky” activities or persons only insofar as they interact with US territory or persons, and not how they go about doing business in Canada with Canadians, or affect legal trade or movement of people between Canada and third countries.

In practice, however, given that the application of a “perimeter” concept necessarily involves each country’s authorities watching out for the security of the other in dealing with shipments or residents from third countries, Canada and the United States will have to assess jointly security risks attached to specific activities or individuals. And, from each country’s viewpoint, the acceptable level for risks coming from or through the other most likely cannot be lower than what it is prepared to tolerate, on its own, vis-à-vis third countries. Such exercises in joint risk assessment and joint action in the face of risks are fully in

keeping with a tradition in Canada-United States relations requiring the two neighbours to “watch each other’s backs” that dates at least to the 1940 Ogdensburg Declaration and the creation of a Permanent Joint Board on Defense. This tradition involves each country’s exercising its sovereignty in a way that maintains an agreed-upon common public good – security – which can best be obtained by their working together to minimize risks to one or the other, or to both countries.

This does not mean the two countries need to adopt the same security measures, but they must pass the grade in terms of each other’s security assessments, despite differences in their laws, institutions and procedures. Indeed, joint threat assessments should rely on risk analysis that is sophisticated enough to take into account that the two countries will not necessarily address risks in the same way. Where relevant, the two countries should also stress the compatibility of their joint threat assessment processes with multilateral processes, such as the United Nations’ “no-fly” list.

At the same time, Canada should take care that required restrictions on travellers and shipments rest on evidence-based, non-politically motivated assessments of risk and do not affect fundamentally Canada’s relations with third countries, with whose nationals Canadians might wish to interact in the normal course of business or personal matters. The two countries accordingly should reach an understanding that a restriction by one country, on national security grounds, on a third-party investor, does not automatically entail a similar restriction in the other country, but rather triggers an evaluation designed to ensure that an acceptably low level of risk ensues despite the two countries’ different stances.

Furthermore, long-term trust between the two countries ultimately requires trust not only between their two governments, but also on the part of legislators and the general public. In this

regard, it is important to reassure the US Congress, in particular, that the Canadian border is secure in order to avoid unexpected and unnecessary restrictions thrown at Canada based on poor information. A mechanism is also needed to query and, if necessary, adjust the other’s assessment of cross-board threats, with input from legislators, relevant agencies, sub-federal governments where appropriate, and the public.

An integral part of establishing a deeper level of trust between the two countries, so essential to the success of the perimeter concept, is that the public should trust that restrictions applied for security reasons do not trump individual rights, or rights to privacy or confidentiality, without due process, at least in non-emergency circumstances. Canada needs to be transparent about the type of information it intends to share, why it is relevant to addressing security concerns, and what assurances there are that the information shared will not exceed what is necessary or be misused.<sup>2</sup>

These considerations call for annual, independent audits of Canadian and US security programs, processes, personnel, and infrastructure to ensure that they meet both countries’ standards of risk tolerance. The audit reports, certifying the adequacy and equivalency of security measures – or, if not, identifying specific flaws – should be delivered to legislators in both countries and ideally be endorsed by them. In effect, the audits would act as a “security certificate” that should ensure that security is adequate and that it is seen as adequate. Legislators should have an opportunity to question the auditors and express any reservations or concerns about the report. In addition, the president and the prime minister should name an ombudsperson to whom individuals and firms mistakenly sanctioned can swiftly refer their cases for inquiry – and, if warranted, attempt to obtain reversal of unjustified decisions.

2 Authoritative views on how concerns about privacy and the misuse of information can best be handled, in the context of the collection and exchange of information required to ensure adequate border security, can be found in Callahan (2010) and Office of the Privacy Commissioner of Canada (2011).

Within this context of trust, it should be possible for Canada and the United States to proceed with cost-reducing measures at the border itself, such as an integrated entry-exit or “swipe once” system, whereby entry in Canada serves to document exit from the United States, and vice versa. The two countries also should be able to adopt or expand a range of preclearance measures away from the border, facilitated by technology, whereby, sometimes operating jointly, they enable the early detection of risk in the movement of people or goods, as well as risk in other areas, such as cyberspace, that originates within their jurisdictions or in other countries.<sup>3</sup>

### *Focus on Potential High Risks, Facilitate Secure Movements*

The concept of trust within the perimeter does not apply only to security issues, narrowly defined, or to criminal activities more broadly speaking. It is also embedded in the regulatory agenda through, for example, more frequent calls for requirements to make products and shipments traceable, to ensure conformity with existing safety, health, and other standards, thus intimately linking the first two classes of measures. To that end, the two governments have also set up a Regulatory Cooperation Council, to work toward reducing unnecessary differences between the two countries’ regulatory regimes (Canada 2011). If successful, this cooperation could spur trade by minimizing the need for firms to produce and ship goods that meet different standards for markets in the two countries. From the perspective of more efficient border management within a perimeter concept, the key is to reduce the number of inspections in areas where regulatory equivalence (or convergence), or at least equivalence in testing and inspection procedures, can be established. The relevant

agencies in each country then could accept more easily the results of the other country’s testing and inspection, which, in turn, would reduce costs to businesses and permit fewer inspections at the border.

Although the bilateral regulatory agenda is ambitious and focused on reducing the cost of doing business across the border, businesses will still have to meet an array of regulations for their products or services to be approved for sale in the other country. Indeed, the two countries’ security and regulatory agendas are evolving toward increasingly sophisticated traceability requirements involving the greater use of technology and the collection of information through the supply chain.

This risk reducing the benefits of the drive to simplification through “inspected once,” “tested once,” or “swipe once” systems. The next task, therefore, is to ensure that the regulatory costs of conducting cross-border transactions are not simply pushed away from the border and added to costs for businesses and travellers elsewhere within the perimeter. Thus, the overall burden of cross-border transactions should be reduced with a view to increasing the potential for small businesses – whose growth within continental and global value chains might well form the backbone of a North American manufacturing renaissance – to trade more easily across the border. Small businesses that are unable to piggyback on the security-related processes that larger suppliers or bulk or container transporters can afford more easily – allowing them swifter passage at the border – should have access to an alleviating mechanism that allows them to verify that they are meeting security and regulatory requirements, and that helps them meet those requirements. It makes sense to ensure that, for both small and large businesses, compliance costs do not outweigh the benefits of new initiatives.

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3 The concept of preclearance resonates well in both Canada and the United States, and offers a range of possibilities for significantly enhancing joint security, while reducing costs at the Canada-US border. For a detailed analysis of these possibilities, see Hart (2010).



A single “window” should be established through which smaller businesses on either side of the border could ascertain their compliance requirements, what steps they need to take to ensure compliance, to obtain preclearance for their shipments or people, and to ensure reasonably fast solutions to bureaucratic problems.<sup>4</sup> Such a window could use as its inspiration the model of integrated services for residents already provided in some US or Canadian jurisdictions, such as Service Ontario. Ideally, over time, the widespread application of one-time inspection, testing and swiping systems could lead to a single border form that provided for information that either country requires. A self-funding trade “accelerator” centre, within which smaller firms could pool resources and exchange views and experiences with government and larger firms on how to facilitate border passage, should also be encouraged. And, while governments should continue to push vigorously for harmonization of their external tariffs and simplification of rules of origin where this makes sense, they should also consider special rules for small businesses, shippers and shipments, based on the trustworthiness and security clearance of business owners and their employees, rather than on the filing of extensive paperwork to prove conformity with complex rules.

### *People Movement*

In economies in which trade and investment are able to flow as easily as they do between Canada and the United States, facilitating the temporary movement of business visitors, traders (including skilled workers) and investors, intra-company transferees, and professionals can generate additional value. Thus, the application of existing provisions under the North American Free Trade Agreement (NAFTA) should be reviewed as part of the overall modernization of the two countries’

border arrangements, with a view to ensuring smoother passage across their mutual border for legitimate business-related trade.

As the NAFTA spells out, the temporary movement of business people should not affect the two countries’ permanent immigration and labour market policies and arrangements or the need for letters of employment or work permits in the case of some temporary entrants. Instead, the two countries should review and improve the implementation of existing measures as they relate, for example, to business visitors who perform services directly related to cross-border trade, and streamline information and paperwork requirements more generally. A more ambitious measure would see the two countries revising the list of business visitors who are allowed temporary entry. The applicable provisions of the NAFTA, now almost 18 years old, date back to when, for example, a number of Internet-based occupations were in their infancy. The two countries thus should launch consultations – that include the provinces, states that trade heavily with Canada, and professional and certifying organizations – with a view to modernizing the list through, for example, a temporary short-term stay program for an additional set of professions.

### *Enhance at-the-Border Efficiency*

A third class of measures concerns the border itself. The basis of improvements in costs and waiting times at the border is embedded in the agenda of the first two classes of measures, which, when completed, will ensure that only inspections that must be made at the physical border take place there. Nevertheless, much remains to be done to ensure quicker passage at the border, including removing impediments to the take-up of existing preclearance programs, finding mechanisms to facilitate the building of

<sup>4</sup> A recent report from the Canadian Federation of Independent Business (CFIB 2011) suggests in a similar vein that border-related information relevant to small businesses be more accessible, that contacts be provided to respond to questions, and that a one-stop web portal be created that contains relevant information.

economically and environmentally sound transport infrastructure, and ensuring that border personnel focus on security and crime prevention rather than on the collection of taxes and fees. While it is reasonable for governments to collect fees for the services provided by agencies that administer the border, or taxes on cross-border purchases, a one-stop e-window – including perhaps a revenue-sharing formula between jurisdictions such as already exists for trucking licences – rather than collection at the border, should be contemplated as a means for doing so, including for individual cross-border purchases.

External auditing of border infrastructure and practices should prioritize, identify, and reduce key infrastructure and administrative bottlenecks. Such auditing would monitor the efficiency of border crossing and help governments, through public discussion of the auditors' reports, allocate resources and improve practices where this is most needed.

## Promoting Accountability and Continued Progress

Any program commensurate with the aspirations Prime Minister Harper and President Obama expressed in the February 4 declaration constitutes a tall order. Indeed, what is promised now is a multi-year Action Plan to be endorsed and put into motion by the two governments by the end of 2011. Experience, however – such as that of the Security and Prosperity partnership (SPP), launched by the three North American heads of government in 2005 but which became inactive in 2009 – shows that ambitious and detailed programs can wither on the vine from lack of ongoing political interest, not to mention public skepticism, which, in turn, can lead to administrative apathy for reform. This phenomenon has also affected the Canada-US Free Trade Agreement and NAFTA, both of which had embedded in them possibilities for evolution over time that were never fully exploited.

Political leadership is important in setting goals and launching the partnership, and ultimately will be responsible for measures taken under the Action Plan. Nevertheless, implementation of the plan and the management of the border in normal times should not be left to the vagaries of political attention. Furthermore, while agencies on both sides of the border have a long history of successful cooperation, there is a natural tendency for them to preserve their authorities and ways of doing things, and therefore they are not candidates for promoting change without external, authoritative prodding and monitoring.

While the Beyond the Border Working Group will continue to oversee through the implementation of the working plan over the next three years, a slim, dedicated bilateral office or commission should be set up to pursue the overarching commitment resolving coordination issues as they arise, in fulfillment of the leaders' declaration.

Indeed, the demise of the SPP showed that the process can be derailed by a combination of public hostility and indifference or misunderstanding. A mechanism to give the public a window on and a way to inform the process is necessary to the success of an enterprise that will rely as much on “bottom-up” cooperation between Canadian and US entities, communities and the public at large as on “top-down” plans by governments. A joint office or commission could perform this important consultative and informational role, in support of the responsibility ultimately exercised by governments and agencies on cross-border matters. Since the work of such an office or commission of necessity would involve the public and legislators from the northern US states, it could also be an important locus of political support in Congress for a secure, yet more open border.

Fortunately, experience with previous Canada-United States cooperation – in particular, the International Joint Commission and the recent Great Lakes-St. Lawrence River Basin Water Resources Compact – provides inspiring and workable models on how to go forward. These international agreements allow a role for local



government, agency, expert, and public input in providing evidence-based recommendations to government and agencies on complex cross-jurisdiction problems that also transcend the mandate of any one agency or department.

The success story of the Canada-United States relationship is steeped in these and other cross-border collaborative processes. A similar process

for managing and invigorating cross-border economic and security cooperation would provide the required input and evidence-based recommendations, as well as the credibility, transparency and accountability, that would cement the key element of the relationship at and beyond the border: trust.

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