ISSUE BACKGROUNDER

Why NAFTA Modernization Should Preserve Benefits for the Paint & Coatings Industry

The North American Free Trade Agreement (NAFTA) entered force on Jan. 1, 1994, following approval by Congress on Nov. 20, 1993. Enhanced trade facilitated by NAFTA for more than two decades has been quite beneficial to the U.S. paint and coatings industry, whose exports range from consumer paints to those used in industrial settings and in manufacturing operations. The U.S. coatings manufacturing base exports a significant portion of its production to Mexico and Canada — $1.5 billion in 2016, accounting for ***two-thirds of the industry's exports*** — and the United States benefits from a consistently strong trade surplus with both countries.

The U.S. paint and coatings industry is a modern, globally competitive industry that supports a significant number of high-paying jobs in the United States, many of which are supported by exports. The American Coatings Association (ACA) represents the nearly $30 billion U.S. paint and coatings industry, operating in all 50 states, and employing over 287,000 people engaged in the manufacture, application, and distribution of its products.

NAFTA renegotiation led by the Office of the U.S. Trade Representative (USTR) under Trade Promotion Authority (TPA) is currently underway. Considering the strong American trade position, ACA would like to reinforce with Congress what it has already expressed to the House Ways & Means Committee's Subcommittee on Trade and the USTR: that NAFTA negotiations be accomplished in a "do no harm" approach that preserves the very real benefits that the coatings industry has seen from this trade agreement over the past two decades. ACA encourages Congress to work with the current Administration in a bilateral manner to promote U.S. exports, remove tariff and non-tariff barriers to U.S. goods and services, and increase access to markets through free trade agreements and other bilateral and multilateral agreements. When it eventually considers the work of the USTR here, ACA hopes Congress will keep these principles in mind during its deliberations.

In this *Issue Backgrounder*, ACA outlines the positive impact NAFTA has borne the U.S. coatings industry, and highlights a few areas for improvement as part of the renegotiation process with respect to re-importation of coatings products, as well as other inefficiencies.

The Coatings Industry and NAFTA

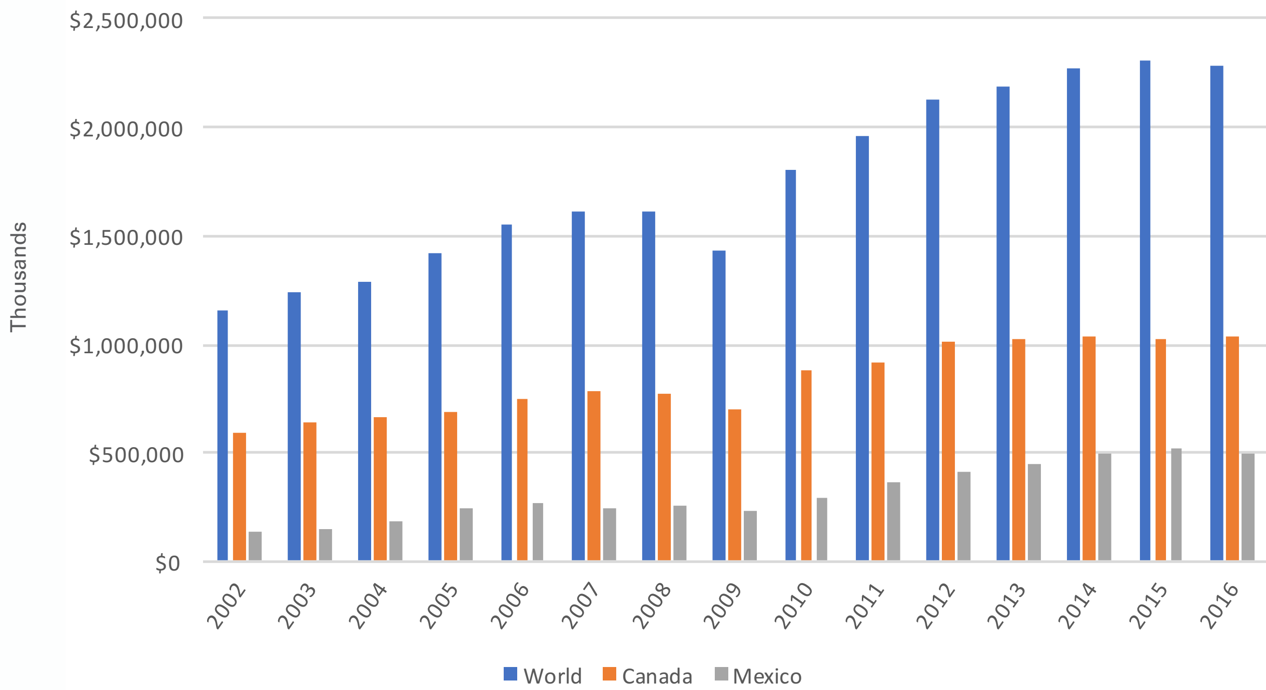
The U.S. coatings industry (NAICS 32551) is a highly efficient, internationally competitive industry that features not only many key global market leaders, but many small and medium-sized enterprises (SMEs) that compete in a variety of market sectors. The U.S. market is roughly evenly divided between architectural (decorative) coatings, along with industrial coatings, most of which are sold for original equipment manufacture (OEM) applications, but some of which are categorized as special purpose coatings, such as automotive refinish coatings. Per the Census, the U.S. coatings manufacturing industry had a total value of shipments and receipts for services of $27.7 billion, and it employs approximately 33,933 persons (manufacturing), and has an annual payroll of $2.231 billion, along with $612 million in fringe benefits.[1]

The U.S. coatings industry also enjoys a strong trade position, both within NAFTA and globally. In 2016, the U.S. exported coatings products valued at $1,531,842,275 to U.S. NAFTA partners Canada and Mexico, with $1,040,857,987 of that total going to Canada and $490,984,288 to Mexico. These figures are comprised of a mix of waterborne[2], solventborne[3], and miscellaneous coatings products[4] that are sold to both Canadian and Mexican consumers, as well as industrial and commercial users and manufacturers. While the U.S. market did import coatings products from NAFTA partners as well, trade in coatings products resulted in a positive trade balance of $1,146,662,347 in transactions within the NAFTA framework (these include a positive trade balance of $734,324,057 with Canada and $412,338,290 with Mexico).[5]

SEPTEMBER 2017

American Coatings ASSOCIATION™

U.S. Coatings Exports, 2002-2016



Source: International Trade Administration

As noted, the coatings products traded in the NAFTA region include both decorative paints used by consumers or painting contractors, along with coatings that are used as intermediate goods within in the manufacturing setting. Particularly important to the paint and coatings industry is the North American market for the manufacturing of motor vehicles. U.S. manufacturers, along with their global competitors, assemble cars, light trucks, and heavy vehicles at multiple locations in the United States, Canada, and Mexico. The complex supply chains that support this manufacturing activity involve Tier 1 and Tier 2 suppliers within NAFTA and elsewhere. This trade in intermediate goods works in both directions, with U.S. suppliers selling to Canadian and Mexican manufacturing plants, and vice versa. This North American interdependence was illustrated recently by the Brookings Institute, which observed that, "advanced manufacturing in many states greatly depends on imports of parts and components from Canada and Mexico. Michigan's automotive industry has long relied on suppliers in Canada and Mexico who provide 61 percent of Michigan's total intermediate imports."[6]

From the perspective of the U.S. coatings industry, NAFTA has proven highly beneficial. U.S. coatings producers have been successful in exporting into the Canadian and Mexican markets, to both Canadian and Mexican manufacturers and consumers, with the NAFTA area accounting for ***two-thirds of the industry's exports***. As such, ACA believes that the ongoing NAFTA negotiations should avoid producing an outcome that leads to either Canada or Mexico erecting new trade barriers that hinder these currently beneficial trade flows, particularly those involving coatings as an input into the manufacturing process. Specifically, renegotiation of any of the existing trade agreement positions that affect the listed categories of coatings could result in increased import duty rates into Canada and Mexico. This will adversely affect American manufacturing operations, considering the large coatings export volumes to Canada and Mexico, and the resulting positive trade balances.

Room for Improvement

Prior to entering trade negation talks, USTR solicited stakeholder feedback, specifically regarding areas in which NAFTA could be improved. ACA, along with other stakeholders, provided suggestions that are summarized here.

Reimportation of Goods

The re-importation of goods often arises in the context of exported merchandise that is deemed defective or obsolete, which would ordinarily result in the return of the merchandise to the producer. In the case of products of U.S.- origin, the process of re-importation into the United States is straightforward, with U.S. import procedures permitting duty-free re-importation. In contrast, the procedure for returning Canadian goods back to their Canadian manufacturer duty-free is very cumbersome in practice.

The complexities here result in some companies deciding not to return defective or obsolete Canadian merchandise to Canada, and U.S. customers holding those goods having to find a market, such as a salvage outlet, or having to liquidate or dispose of those goods in the United States. ACA urged the USTR to seek simplification of Canadian goods return procedures by Canadian Customs. This will result in U.S. customers being able to successfully ship NAFTA-origin products back to their producers on the same basis as they would with domestic suppliers.

Customs and Trade Facilitation

Generally, import and export administrative procedures between Canada and the United States are currently well streamlined. In practice, the routine exchange of substantial trade information between Canada and the United States results in the waiver of certain procedures (e.g., U.S. export declarations), which simplifies and facilitates the border-crossing process considerably. In contrast, the import and export administrative procedures between Mexico and the United States are more cumbersome and require more paperwork. These extra steps result in longer clearance and border-crossing times. ACA urged that eliminating this divergence in customs procedures can be a negotiating point.

Rules of Origin or Origin Procedures for NAFTA Qualifying Goods

While they are themselves not specifically coatings, key raw material inputs classified, for example, under HS 3907[7] are used in coatings, and in some cases, are also manufactured by coatings producers as inputs into coatings formulations. In practice, importing these products requires producers to apply (1) tariff shift rules, and (2) regional value content calculations. This requirement places a considerable administrative burden on manufacturers, who must solicit supporting NAFTA certificates from suppliers of raw materials. Simplifying this procedure and allowing importers to apply either tariff shift rules *or* regional value content calculations rather than both could considerably simplify the overall process of importation.

Harmonization of Standards for Transport of Dangerous Goods

It is widely understood that harmonized regulations enhance the safety and efficiency of cross-border shipments of dangerous goods. Typically, these standards are discussed and debated at the United Nations' Sub-Committee of Experts on the Transport of Dangerous Goods (UN SCE TDG) with the participation of countries and non-governmental organizations, including the International Paint and Printing Ink Council (IPPIC), for which ACA serves as the Secretariat. The UN SCE TDG issues revisions to its model regulations every two years and participating countries may then adopt these changes into their own regulations for transport of dangerous goods. While NAFTA already contains international harmonization standards under Article 906, these principles have not been embraced by Mexico, nor applied to cross-border traffic in dangerous goods between the United States and Mexico. Consequently, ACA member companies experience delays at the southern border related to differing regulatory structures. ACA encourages the USTR and Congress to pay special attention to the issue of harmonization of standards to alleviate these unnecessary delays that result in confusion and interrupted shipments.

Conclusion

While there are clearly areas in which NAFTA could be improved and modernized, ACA has urged the USTR to approach these negotiations with a "do no harm" approach. The current arrangement is largely beneficial to U.S. consumers, the U.S. manufacturing sector and workforce, and the U.S.-based coatings industry. We believe Congress shares industry's view that maintaining this beneficial agreement in a trilateral form is the best outcome, and urge Congress to continue working to ensure a level playing field for U.S. exports. The U.S. market is largely open to imports from around the world, but some countries continue to levy tariffs on U.S. exports that, in some cases, are extremely high. Foreign governments have also erected other barriers against U.S. goods and services. America's trade agreements, however, work to create a level playing field; and by tearing down foreign barriers to U.S. products, these agreements, including NAFTA, have a proven ability to make big markets even out of small economies.

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[1] U.S. Census Bureau, 2015 Annual Survey of Manufactures.

[2] These are represented by HS Code 3209, "Paints and varnishes (including enamels and lacquers) based on synthetic or chemically modified natural polymers, dispersed or dissolved in an aqueous medium."

[3] These are represented by HS Code 3208, "Paints, varnishes; (enamels and lacquers) based on synthetic polymers or chemically modified natural polymers, dispersed or dissolved in a non-aqueous medium."

[4] These are represented by HS Code 3210, "Paints and varnishes (including enamels, lacquers and distempers), excluding those of heading no. 3209, prepared water pigments of a kind used for finishing leather."

[5] The comparable global numbers are total exports of $2,284,383,233, with a net trade surplus of $1,453,069,036. Source: International Trade Administration.

[6] "How US states rely on the NAFTA supply chain," Joseph Parilla, The Brookings Institute, March 30, 2017

[7] HS 3907 is defined as "polyacetals, other polyethers and epoxide resins, in primary forms; polycarbonates, alkyd resins, polyallyl esters and other polyesters, in primary forms."