

Brief to the Standing Committee on International Trade

Bill C-4, An Act to Implement the Agreement Between Canada, The United States of America and The United Mexican States

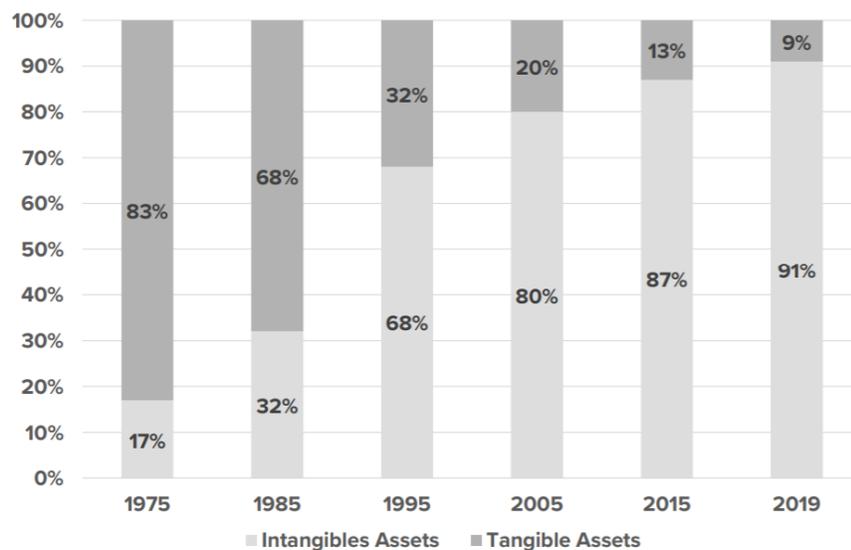
Summary

Canada has focused substantial resources and effort on new trade deals (e.g. CETA, CPTPP and CUSMA) to reinforce the rules of the game for international trade. And rightly so. Trade is at the heart of our prosperity and new trade agreements are necessary to open up new markets and opportunities and preserve old ones; revised rules are necessary as economies change and to minimize trade frictions. The new agreements have many benefits for Canada particularly in the areas of preserving and/or opening markets in regions of primary interest (the US, EU and parts of Asia) while updating arrangements in agriculture and pharmaceuticals. Nevertheless, Canada has made commitments related to data and intellectual property (IP) that may inhibit Canada’s ability to innovate. In particular, these latest agreements fail to consider the implications of how the nature of trade is changing, moving from scale and cost efficiencies to:

- IP creation and extraction;
- the rise of (big) data as an economic and social asset; and
- the resulting imperative of asset protection.

As Canada embarks on new trade agreements, including the forthcoming WTO e-commerce negotiations, it needs to be mindful of these changes, which are further explained in this brief. What Canada agrees to in these areas has very wide-ranging repercussions for Canada in many forward-looking areas, including our ability to harness data in new technologies such as artificial intelligence (AI), as well as fundamental domestic policies related to privacy, security, IP, investment, competition and innovation.

Figure 1: Shift from tangibles to intangibles. Components of S&P 500 Market Value



Source: Ocean Tomo: Intangibles Asset Market Value Study, 2015.

Background

While globalization has raised global living standards, the globalization of the last two to three decades has been “unbalanced”—high in movement of finance and the spread of information and communications technologies; slower in the liberalization of trade in goods and services; and lagging in the movement of people and the development of regulatory and other policy responses at the national and supranational levels.

Technological change is both a driver and product of globalization. The digital/intangibles era is characterized by high upfront costs, and very low reproduction costs. It conveys a great advantage to first movers, particularly if the technology becomes an industry standard. This also means that primacy in this matter is a global geopolitical game and Canada has not been the leader. And economies of agglomeration are inherent in the production of intellectual property (IP), so existing innovation clusters have a head start over others still in the formative stage.

Against this background, regional trade agreements have focused on opening up markets and driving scale economies, which result in lower prices and a welfare gain to consumers. Countries are thus better off through the comparative advantage that trade brings (though distributional issues persist). In the data-driven economy (DDE), the opposite is true. Increased market access tends to eliminate competition as firms use their intellectual property to extract rents from trading partners. Indeed, successful companies now principally compete on staking positions in value chains of intangibles rather than by only lowering costs in production supply chains. Additional product enhancements and services based on IP and data have low or even zero marginal production costs, which results in “winner take all” economics. Those that want to prosper in the intangible economy are accumulating valuable IP assets because it’s a precondition to commercialization.¹ Not surprisingly, some countries are strategically growing and protecting their IP assets and using trade agreements to benefit their firms.

In the DDE, to state the obvious, data is thus an extremely valuable resource. Data feeds the algorithms that drive new forms of decision making that has disrupted existing industries and led to the creation of new ones. In essence, data is an extremely valuable factor of production (Statistics Canada has produced estimates in the range of CAD \$200 billion and roughly 2/3 the value of Canada’s oil assets) and one that firms seek, not surprisingly, to control: from a firm’s perspective, data is their intellectual property. From a national perspective, data drives innovation and economic prosperity and this is occurring across all sectors of the economy, including traditional sectors that have been the focus of trade agreements such as manufacturing, agriculture and more recently services. Moreover, both large amounts and large varieties of data are required for AI. This has led to calls for both open cross border data flows and data localization. On the one hand, cross border data flows allow the scaling of data resources; on the other data localization focuses on data as a national resource. Meanwhile, against these contrasting views, we have already seen the disruption that can result from data, and this disruption is only the beginning. The unfolding of the Internet of Things (IoT) on a grand scale with the advent of 5G telecommunications networks is looming.

¹ Report: Intellectual Property in Ontario’s Innovation Ecosystem Expert Panel on Intellectual Property Report to the Government of Ontario February 2020. https://files.ontario.ca/books/expert-panel-report-intellectual-property-in-ontarios-innovation-ecosystem_final_0.pdf

Moreover, data and associated technologies have led to the rise of new trading and geostrategic rivalry as evidenced by China and the US tech war.²

A plethora of data-related regulatory issues have been broached that impact global commerce, including data governance in general, privacy, misinformation and fake news, national security, the application of regulations to the gig economy and others. In addition, there are a host of competition policy issues especially related to the large digital platforms. Canada's new Digital Charter is unique in that it provides a comprehensive framework for these areas; however, these issues are also being raised in many other fora.

An illuminating example with respect to the social media platforms helps to clarify some of these points. Open data flows in CPTPP and CUSMA essentially imply that Canadian data will flow to US-based multi-national monopolies such as Google and Facebook that can use the data to further cement their market positions as the data are used to improve their AI technologies and platforms. Importantly, these platforms can then use their dominant positions to squeeze out Canadian firms in a number of ways: by hiring Canadian talent, by taking over Canadian firms (take out) using their treasure troves of cash (think of them as venture capital funds too), and by dominating the market place. This stifles Canadian innovation and ultimately hampers our prosperity.

Thus, Canada has agreed to provisions within CPTPP and CUSMA, whose implications bear further scrutiny. Canada appears to have followed the same logic on rules as we have for our past trade agreements with a primary focus on the tangibles economy, but which will limit our ability to grow in the data driven economy.

Some concrete provisions in recent trade agreements include:

- The treatment of data localization in the TPP and CUSMA.³ Where the TPP equivocated on the location of computing facilities the CUSMA provision on the matter (Article 19.12) is short and not so sweet, at least for those who read more into data localization policies than simply the enabling of trade: "No Party shall require a covered person to use or locate computing facilities in that Party's territory as a condition for conducting business in that territory." Once data is seen only through a commercial lens and not as an aspect of personal protection and privacy, the logic of ever more openness makes sense. But examples abound of the non-economic dimensions of data, lost when data is treated strictly through the trade agreement medium. A Canadian who legally purchases cannabis online with his credit card might be denied entry into the US for having bought a substance banned in the US, just because the "shadow" of the financial transaction was not localized. Or, if a smart city partnership in Toronto with Sidewalk Labs, a subsidiary of Alphabet, proceeds, Canadians may well desire the detailed data about their city and their lives in it remain in the country.⁴

² Ciuriak, D. World Trade Organization 2.0: Reforming Multilateral Trade Rules for the Digital Age CIGI Policy Brief No. 152. <https://www.cigionline.org/publications/world-trade-organization-20-reforming-multilateral-trade-rules-digital-age>

³ Hirsh, Jesse (2018), "CUSMA May Have Closed the Door on Data Localization Too Soon", Center for International Governance Innovation, October. <https://cis-india.org/internet-governance/resources/the-localisation-gambit.pdf>

⁴ Scassa, Teresa (2018), "Considerations for Canada's National Data Strategy" in Rohinton P. Medhora (editor), *Data Governance in the Digital Age*, Centre for International Governance Innovation. <https://www.cigionline.org/sites/default/files/documents/Data%20Series%20Special%20Reportweb.pdf>

- A Canadian request for algorithmic modification could be challenged under CUSMA as a protectionist measure discriminating against the American or Mexican producer of the software or application. Also, under CUSMA governments can only require organizations that collect, hold or process information to locate their computing facilities in the territory when these activities are undertaken for or on behalf of a government, which is in line with current practices. However, if, for example, data deemed critical for national security reasons were held by a private organization, then CUSMA would technically require a government to allow these data to be held and processed in the other two member states' territories. As a result, these data could become accessible to the other member-state governments (for example, through the USA PATRIOT Act in the United States).⁵
- The capacity of national authorities to hold multinational digital platforms accountable for the content they carry is unclear. The CUSMA uses the "safe harbor" provision to liberate digital platforms from responsibility for the content they carry. Free speech advocates see this as desirable.⁶ Others look at the "weaponization" of platforms like Facebook, Twitter and YouTube during recent votes such as the 2016 US Presidential election and the Brexit referendum and the livestreaming of the terror attacks in Christchurch, New Zealand in March 2019 as indications that the unwillingness and/or inability of digital platforms or governments to regulate content has important social and political consequences. Why is this a trade issue? These platforms gain their ability via the massive cross border data flows.
- Canada's CPTPP and CUSMA commitments could ultimately negate the effectiveness of future data protection policies that the federal government might want to adopt to create trust in the data-driven economy. It is not clear how much policy flexibility the CPTPP and CUSMA will ultimately allow the federal and provincial governments in adopting new laws and regulations to, among various objectives, protect people's privacy, prevent algorithmic bias, protect critical infrastructure, ensure national security or promote domestic innovation.⁷

Recommendations

1. Trade negotiators need to be more fully briefed on the wide-ranging implications of the data-driven economy and the implications arising both from existing measures implemented in CPTPP and CUSMA and more generally those that could arise in the ecommerce negotiations that are about to begin at the WTO. Data and IP issues are broader, and more profound, than ecommerce. What we agree to in trade negotiations can affect our ability to create domestic policy in many areas, including privacy, competition policy, cyber and IP. These spillover into foreign domestic investment and takeovers too. And there are broader geopolitical considerations to consider in any agreement, for example the US-China tech battle.
2. Be mindful of vested interests in the digital realm. Given that in the Western world the major platforms are US-based, and that they command attention in the political discourse in the country, the laissez-

⁵ Leblond, P (2019) Digital Trade at the WTO: The CPTPP and CUSMA Pose Challenges to Canadian Data Regulation CIGI Paper No. 227. <https://www.cigionline.org/publications/digital-trade-wto-cptpp-and-cusma-pose-challenges-canadian-data-regulation>

⁶ Geist, Michael (2018), "The CUSMA "safe harbor" provision reduces liability risks for business and provides Canadians with long-overdue safeguards for Internet free speech", *Policy Options*, October. <https://policyoptions.irpp.org/magazines/october-2018/why-the-CUSMA-will-enhance-online-free-speech-in-canada/>

⁷ Leblond, P (2019) Digital Trade at the WTO: The CPTPP and CUSMA Pose Challenges to Canadian Data Regulation CIGI Paper No. 227. <https://www.cigionline.org/publications/digital-trade-wto-cptpp-and-cusma-pose-challenges-canadian-data-regulation>

faire approach taken towards these companies in the US is understandable. The projection of this political economy, via Regional Trade Agreements (RTAs), into other countries removes their ability to view this situation differently. In effect, the RTA entry point is used to manage policy space for areas that go well beyond e-commerce.

3. More generally, we need new international rules of the game for trade, investment and intellectual property. Widespread concerns have, for some time, been raised about the fracturing of the global economy into walled-off and possibly warring data realms; and Canada could push to have a full-fledged negotiation round with the potential to facilitate agreement through trade-offs across issue areas. More generally, Canada could also push for the creation of a new global organization to set international governance for the data-driven economy. Drawing on the experience of the Financial Stability Board (FSB) created after the financial crisis of 2008-09, a proposal is to create a Digital Stability Board. Such an organization would develop standards, regulations and policies across the many realms that digital platforms touch; advise on best practices, and consideration of regulatory and policy actions needed to address vulnerabilities in a timely manner; assess vulnerabilities arising from these technologies, including their impact on civil society and the regulatory and policy actions needed to address them; and ensure that this work feeds into other international organizations.
4. Finally, use the 6-year review built into CUSMA to rectify some of these issues.

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