August 6, 2014

Christine Lafrance
Clerk of the Standing Committee on Finance
Sixth Floor, 131 Queen Street
House of Commons
Ottawa, ON K1A 0A6

Re: 2014 Pre-Budget Consultations

Thank you for the opportunity to submit the comments of the Canadian Apparel Federation (CAF) as part of your committee's pre-Budget consultations. Our comments relate to the theme of *Improving Canada's taxation and regulatory regimes*.

Executive Summary

This submission outlines priorities and recommendations concerning import duties on apparel. In our remarks below we discuss three separate issues:

1. Tariff relief on finished apparel
2. Tariff relief on apparel products made from leather and silk impacted by 2013 changes to the General Preferential Tariff (GPT)
3. Proposed changes to the Least Developed Countries Tariff (LDCT)

The Government collects approximately $1.35 billion in duties on imported apparel annually. For this reason alone it is important to address these issues.

1 Tariff Liberalization: Apparel

The CAF testified before the Senate Standing Committee on National Finance in February 2012 on the issue of the consumer price gap between Canada and the United States. We argued that the Government should be able to make tariff policy based on a variety of factors and considerations – not only the impact on consumer prices relative to the US.

In the 2013 Budget duties on infants clothing were eliminated. Infants clothing was an ideal candidate for tariff relief as domestic production is virtually non-existent; the product is by nature a product used only by consumers, and there was a significant tariff disparity between Canadian and US duty rates (Canadian rates were over double the corresponding US rates).

The CAF supported this action, and had in fact recommended infants apparel as a candidate for tariff liberalization . The decision to eliminate duties on infants clothing has created a precedent for addressing tariffs on a case by case basis. We believe this is a positive way to approach the issue, and we want to encourage the government to continue reviewing individual products for possible tariff reductions or elimination. In determining whether individual products are appropriate for tariff liberalization considerations should include the following:

1. Whether there is a substantial disparity in tariffs for specific products between Canada and the United States;

2. Whether imports of specific products already benefit from trade preferences (duty free imports under free trade agreements etc.);

3. Whether tariff relief would impact Canadian manufacturers of the products,

4. Whether tariff relief be focused on consumer products (as opposed to other end users) and

5. Whether products in question represent important expenditures for Canadian families.

Budget 2013 also announced the creation of a research study to verify that the tariff savings would be passed along to the consumer. As the Budget stated, tariff liberalization measures "come with an expectation that wholesalers, distributors and retailers will pass these savings on to consumers."

While the results of this survey have not been released, we anticipate that the research will demonstrate that there are savings to consumers, but given the challenges of comparing specific fashion products over time (to establish clear pricing trends for discrete products) it will be extremely difficult to be as precise as the government might want.

It is our view that there is ample evidence to demonstrate that apparel prices have reflected reductions in import costs. Retail prices for clothing as measured by the Consumer Price Index (CPI), trail all other major commodities that make up the CPI basket of goods. With 2002 as the base year, the CPI shows that prices for clothes have declined by 10 per cent over the last decade, even as prices for other commodities have increased by 10 to 40 per cent.

As import quotas were eliminated and imports from countries such as Bangladesh and Cambodia were made duty free, prices declined. As a result we believe that the research currently being undertaken by the Department of Finance will simply confirm what is demonstrated by the consumer price index: as import costs go down, consumer prices also trend downward.

Given the importance of this issue many companies have presented their views to government and we mention several of these below.

Foundation Garments

Importers of foundation garments have requested tariff liberalization for their products. Submissions were made to the Senate national finance committee in 2012. Annually there are $200 million in foundation imports and approximately $27 million in duties paid. Tariff relief on brassieres would benefit nearly half of all Canadians and represent a progressive and meaningful approach to tariff policy.

Virtually the entire market for brassieres is supplied by imports. Given their sophisticated structure and complex designs, their production is heavily concentrated among specialized producers based primarily in the Asia Pacific region. Foundation garments have not benefitted from tariff relief secured under various Free Trade Agreements or other tariff concessions. By CAF's calculations less than 10% of imported brassieres enter Canada at preferential rates of duty.

Denim Apparel

Importers of denim apparel also testified before the Senate National Finance Committee to request tariff liberalization for their products. Denim is an extremely clear-cut example of a product which was once manufactured in Canada, but is no longer. Annually there are $235 million in imports of women's jeans alone, and approximately $20 million in duties paid.

Outerwear

In 2011 changes to certain tariff classifications were initiated by CBSA which had a significant impact on the classification and tariff treatment of winter outerwear. For many years a large volume of winter outerwear had been classified under chapter 39 of the Customs Tariff based on having a water resistant coating. This relatively arcane tariff classification allowed for imports of outerwear enter Canada at a very low rate of duty (as low as 3%).

The changes initiated by CBSA required importers to classify the same garments differently and pay much higher rates of duty (18%). Many importers of these products opposed the changes made by CBSA largely because the domestic manufacturing base was largely nonexistent. We urge the committee to consider a product such as winter outerwear especially outerwear for children as a potential item for tariff reductions or elimination.

Recommendation

We believe it is a legitimate public policy to review specific products for tariff relief. We have presented a full set of criteria which we feel should guide consideration of these applications

II Changes to the General Preferential Tariff

The 2013 Budget made substantial changes to the General Preferential Tariff (GPT), removing a number of countries from GPT eligibility, among them China and India. Changes to the GPT were undertaken to refocus the benefits of tariff preferences on less affluent developing countries. These changes will have a very negative impact on companies that source certain garments from these countries. The product categories most affected by these changes include silk and leather garments, classified under the following tariff numbers:

- HS 6204.49 - Womens/Girls Dresses - Woven - Textile not elsewhere specified
- HS 6206.10 - Womens/Girls Blouses, Shirts and Shirt-Blouses - Woven – Silk
- HS 4203.10 - Articles of apparel and clothing accessories, of leather

The proposed changes will increase duties payable on imports of garments that are either not produced in Canada (silk) or produced in very limited quantities (leather). Countries that will be removed from GPT eligibility (China in particular) are the dominant international sources of

supply for these products. China and other countries which will no longer be eligible for GPT treatment supply well over 50% of the Canadian market for each of these products. As an example 90% of all silk blouses imported into Canada are sourced from China alone.
The countries that remain eligible for the GPT will not replace China and India as suppliers of these products. For silk garments there are substantial production issues that make it very difficult to shift production out of China. For leather goods production is heavily reliant on the the tannery infrastructure in China and India. Similarly these products are not manufactured in countries that benefit from other tariff relief programs (i.e. the Least Developed Countries Tariff (LDCT).

- In simple terms the effective rate of duty on silk garments will rise from 10% (the current GPT rate) to 16% (the MFN rate) whereas the U.S. tariff rate on those products will remain at 6.9%. The spread between Canadian and U.S. duty rates will go from 3.1% to 9.1

- For leather apparel the effective rate of duty will rise from 8% (the current GPT rate) to 13% (the MFN rate). The spread between Canadian and U.S. duty rates will go from 3.1% to 9.1

The Canada-U.S. price gap will increase, as goods sold in the Canada will be subject to substantially higher duties than in the U.S, which is particularly important given the significance of cross border shopping.

Recommendation

We recommend consideration of two options.

1. Lower the MFN rate of duty on silk and leather apparel to the existing GPT rate.

or

2. Eliminate duties on silk and leather apparel. These products are produced in extremely limited quantities in Canada and there would be no impact on Canadian industry.

3 Least Developed Countries Tariff (LDCT) Rule of Origin

Apparel imports entering under preference programs are affected by customs compliance costs. In 2002 the Canadian government granted duty-free and quota free access to the Canadian market for goods produced in least developed countries (LDCs). In order to qualify goods must meet the LDCT rule of origin which requires that yarns and fibres originate in Canada, an LDC or a GPT country. In reality the vast majority of apparel manufactured in LDC's is made from GPT inputs. In 2013 following the changes announced in the federal budget the Canadian government amended regulations to add an additional category of qualifying inputs namely the 72 countries previously eligible for the GPT which had lost their eligibility.
In its current form the rule of origin creates a substantial compliance requirement, but it serves no purpose other than to create a paper burden for Canadian importers. In simple terms importers must work through their entire supply chain and continually monitor the origin of raw materials where the sole purpose seems to be to ensure that no raw material in inputs from Europe the United States or Taiwan factor into the production.
The benefits of these proposed changes would be:

1. Significant reduction in compliance costs (and risks associated with compliance) - consistent with the Government's Red Tape Reduction initiative, and especially beneficial to smaller importers;

2. It would reinforce LDC production, as it would allow for a wider range of textile inputs to be used in qualifying LDC apparel;

3. It would align the Rule of Origin with those found in recent Free Trade Agreements – (i.e. Canada-Jordan) and the proposed Canada-Korea FTA

4. It would align our program with other trading partners: bringing Canada's LDC Program into line with the revised rules under the European Union's Everything But Arms initiative.

Recommendation

We recommend the adoption of a single transformation rule of origin for LDC's, allowing textile inputs from all sources. This would bring Canada's LDC Program into line with the European Union's LDC initiative, which allows all fabric inputs regardless of origin to be used in qualifying LDC production.

The simplest mechanism to address this is to revise section 2.4 of the General Preferential Tariff and Least Developed Country Tariff Rules of Origin Regulations (SOR-98-34) by eliminating all restrictions in terms of raw material source.

Please do not hesitate to contact me if you need further information.

Sincerely yours,

Bob Kirke

Executive director