JOCK A. FINLAYSON*
J. CHRISTOPHER THOMAS†

The Elements of a Canada–United States Comprehensive Trade Agreement

I. Introduction

The last several months have witnessed important developments in the trading relationship between Canada and the United States. In September 1985, the Canadian government, after months of intensive study, announced that it wished to launch negotiations with the United States aimed at reaching a comprehensive, bilateral trade liberalization agreement. In early December, President Reagan formally responded to this Canadian request by informing Congress of his administration's intention to enter into wide-ranging trade discussions with Canada. The House of Representatives Ways and Means Committee and the Senate Finance Committee considered this question during the early months of 1986, and after an emotional set of hearings the latter split 10-10 when voting on whether to commence negotiations. This tie vote allowed the Administration to proceed with the trade talks. Formal negotiations began on May 21, 1986.

The Canadian-American trading relationship is the largest and most extensive in the world, with a two-way trade flow in excess of $110 billion (U.S.) in 1985. Each country is the other's most important trading partner, but there is a striking disparity in their relative dependence on bilateral trade. Canada sends some three-quarters of its exports to the United States, and purchases in excess of two-thirds of its imports from U.S. suppliers, whereas in the case of the United States the comparable figures are in the range of 19-20 percent.

* Mr. Finlayson was formerly Director of Policy Analysis and Research, Business Council on National Issues. He is currently attending the Yale School of Management.

† Mr. Thomas is on the Faculty of Law, University of British Columbia and an Associate of Ladner Downs, Barristers and Soliciters, Vancouver. He is currently an advisor to the Minister for International Trade of the Government of Canada. The views expressed herein are the authors' and do not necessarily reflect the position of the Government of Canada or the Business Council on National Issues.

Nonetheless, the United States trades more with a single Canadian province, Ontario, than with Japan, its second largest trading partner.[1]

Despite the magnitude and rapid growth of bilateral commerce, no formal bilateral legal or institutional framework has been developed to regulate Canada-United States trade. Instead, both countries have primarily relied on the rules and the legal framework provided by the General Agreement on Tariffs and Trade (GATT)[2] to govern their trade relationship, although a few bilateral arrangements have been put in place to deal with particular issues or problem areas. For example, Canadian objections to U.S. jurisdictional claims have led to a series of understandings in respect of antitrust enforcement.[3]

In light of the fact that serious trade negotiations between the two countries have now begun, this article will consider how the legal and institutional setting of Canada-United States trade may be altered as a consequence of a new trade agreement. Specifically, it will discuss the likely structure and content of a Canada-United States Comprehensive Trade Agreement (CTA). This is done partly by considering the stated negotiating objectives of the two countries, and partly by exploring the provisions that have been written into bilateral and plurilateral trade agreements reached by other countries. Many of these agreements can provide valuable clues as to how a Canada-United States trade agreement may be drafted. At the same time, however, it is argued here that certain unique features of the Canada-U.S. economic relationship—particularly the unusual degree of economic integration that has already occurred—suggest that the two countries may need to develop innovative approaches to address certain difficult trade issues.

It is not yet clear exactly what matters will be on the two countries' negotiating agendas. In general, tariffs, nontariff barriers at the federal and state/provincial levels, and subsidy policies appear to be recognized as important by both sides. In addition, the United States views obstacles to U.S. investment and exports of services as key issues, as noted by the United States Trade Representative, Clayton Yeutter, in his September 27th report to Pres-

1. The trading relationship is described in some detail in a Discussion Paper entitled, *How to Secure and Enhance Canadian Access to Export Markets*, released by the Honorable James Kelleher, Minister for International Trade (January 1985), at 4-6 [hereinafter cited as Discussion Paper].

2. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat. A3, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter cited as GATT]. GATT has been modified in several respects since 1947. The current version is contained in 4 GATT BASIC INSTRUMENTS AND SELECTED DOCUMENTS (BISD) (1969).

3. The Memorandum of Understanding as to Notification, Consultation and Cooperation with Respect to the Application of National Antitrust Laws of Mar. 9, 1984, *reprinted in* 23 I.L.M. 275 (1984), is the most recent agreement.

ident Reagan on the prospects for bilateral talks.[4] For its part, Canada views more secure and enhanced access to the U.S. market (i.e., the reduction or removal of the threat of contingency protection) as a central objective.[5] Thus, the elements of a possible CTA considered below address not only trade in goods and import relief protection, but also trade in services, investment, and investment-related trade issues.

The following discussion takes note of a number of existing bilateral and multilateral trade and investment treaties considered in the light of the special features of the Canada-United States relationship.[6] It reflects the view that Canada must offer a creative negotiating package to the United States if it is to succeed in attaining the central negotiating objective of more secure access. It also assumes that it probably will be impossible to obtain congressional support for modifications of U.S. import relief laws unless Canada is prepared to offer important safeguards to the United States. Finally, although the United States has just recently concluded a Free Trade Area Agreement with Israel,[7] this paper addresses a wider variety of issues than those canvassed in that agreement. The magnitude and complexity of our relationship makes it categorically different from the U.S.-Israel relationship. U.S. imports from Israel amount to only 0.05 percent of total U.S. imports whereas U.S. imports from Canada amount to approximately 19-20 percent.[8] Moreover, the much greater degree of transborder direct investment, as well as other factors, points to a significantly more complex relationship than the United States-Israeli one.[9]

4. Copy on file at THE INTERNATIONAL LAWYER.

5. Discussion Paper, *supra* note 1, at 17-18.

6. In particular, reference has been made to the Convention Establishing the European Free Trade Association, the Treaty of Rome, the Australia-New Zealand Closer Economic Relations Agreement, the Panama-United Kingdom Agreement for the Promotion and Protection of Investments and the Panama-United States Treaty Concerning the Treatment and Protection of Investment [hereinafter cited as Panama-United States Treaty]. The latter was done at Washington, Oct. 27, 1982, and is reproduced in 21 I.L.M. 1227 (1982).

7. Agreement on the Establishment of a Free Trade Area Between the Government of the United States of America and the Government of Israel, *done at* Washington, Apr. 22, 1985, *reprinted in* 24 I.L.M. 653 [hereinafter cited as United States-Israel Agreement]. The United States Trade Representative (USTR) drew up a summary of the Free Trade Area Agreement (copy on file at THE INTERNATIONAL LAWYER) [hereinafter cited as USTR Summary].

8. In 1982 the U.S. exported $1.5 billion worth of products to Israel; Israel exported $1.2 billion worth of products to the United States. USTR Summary, *supra* note 7, at 9.

9. Nevertheless, the U.S. is obliged to consult with Israel should it commence negotiations with a view to concluding a trade agreement with a third country. Art. 18 (1) (b) and (2) of the United States-Israel Agreement, *supra* note 7, provides:

> (b) Before either Party commits itself to take any action, unilaterally or by agreement, which would reduce the barriers to trade applicable to third countries, including those with whom that Party intends to enter into a customs union free trade area . . . it shall provide prior written notice to the other Party as far in advance as may be

II. Preliminary Considerations

Before discussing the likely elements of a CTA, a number of preliminary points should be noted. First, the type of agreement envisaged here would be a free trade area agreement as defined by article XXIV of the GATT, supplemented by rules on such matters as competition, services and investment.[10] Article XXIV states that the provisions of the General Agreement "shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free trade area or the adoption of an interim agreement" leading thereto.[11] However, there are certain conditions that must be fulfilled under article XXIV. First, duties and other regulations of commerce applicable to contracting parties that do not become members of the free trade area "shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing prior to the formation of the free trade area, or interim agreement."[12] Secondly, the parties to a free trade area are under a duty to "promptly notify" the contracting parties and "make available to them such information regarding the proposed union or area as will enable them to make such reports and recommendations to contracting parties as they may deem appropriate."[13]

It is unlikely that Canada and the United States would wish at present to create a customs union or a common market. A customs union requires the member states to have a uniform external tariff as against imports from other countries, whereas a free trade area does not. The logical consequence of this technical difference is that a customs union "must form a common commercial policy towards the outside world, unnecessary in the free trade area, which marks a more important difference between how the two arrangements then develop."[14] A common market would also require signatories to impose common external trade barriers

---

practicable.

2. If the Party affected by the proposed measure referred to in paragraph 1 requests consultations with regard to such measures, the Party proposing the measure shall afford adequate opportunity for consultations regarding the proposed measures.

10. Art. XXIV of the GATT, *supra* note 2, provides for an exemption from the application of the GATT's most-favored-nation rule for free trade areas and customs unions concluded by GATT members. On the importance of this GATT provision, *see* K. DAM, THE GATT—LAW AND INTERNATIONAL ECONOMIC ORGANIZATION 274-95 (1970). GATT does not presently address such issues as competition law, trade in services, or investment.

11. GATT, *supra* note 2, at art. XXIV: 5.

12. *Id.* at art. XXIV: 5 (b).

13. *Id.* at art. XXIV: 7 (a). The precise meaning of art. XXIV is difficult to discern due to drafting problems. *See* Dam, *Regional Economic Arrangements and the GATT: The Legacy of a Misconception*, 30 CHI. L. REV. 615 (1963); *see also* J. JACKSON, WORLD TRADE AND THE LAW OF GATT 587-88 (1969).

14. J. LAMBRINIDIS, THE STRUCTURE, FUNCTION, AND LAW OF A FREE TRADE AREA 6 (1965).

vis-à-vis the rest of the world and, in addition, would require the free movement of labor, capital and services.[15] In any bilateral trade pact, it is clear that both countries will want to maintain a significant latitude for independent policymaking in many areas. This suggests that an agreement broadly similar to a free trade area would be considered preferable.

Under GATT rules, countries wishing to establish a regional trade arrangement must either obtain a waiver from the GATT's most-favored-nation principle, or else negotiate a free trade area, customs union or an "interim agreement" leading thereto. It is assumed here that Canada and the United States would seek to negotiate an "interim agreement" leading to the subsequent establishment, over time, of a bilateral trade arrangement consistent with GATT rules. The most important requirement of article XXIV in this respect is that "substantially all trade" between the parties be freed under the terms of the regional agreement. Previous experience suggests that the freeing of trade in 80-90 percent of traded goods is sufficient to meet this test.[16]

A second preliminary point concerns whether a Canada-United States CTA should be open-ended and thus permit other countries to join at a later date. Both Ottawa and Washington may prefer that any future bilateral agreement be structured in such a way as to allow for subsequent accession by other trading nations prepared to abide by the terms of the agreement and to offer reciprocal concessions in exchange for free access to the Canadian and U.S. markets. This view is particularly likely to find favor in the two countries' other major trading partners in Europe and Asia.

Third, it is important to consider the method of implementation of a bilateral CTA under domestic law. Under U.S. law, there are basically two options—an executive agreement and a treaty. The first would be simpler to negotiate and possibly easier to get through Congress. As in the case of the various trade accords negotiated by the United States during the GATT Tokyo Round, a bilateral trade pact taking the form of an executive agreement under U.S. law could be legislated through the so-called "fast-track" procedure in Congress, whereby legislators would either accept or reject the agreement as is within a specified time period (i.e., no amendments are permissible). An alternative approach would be to have a formal treaty, which requires the consent of two-thirds of the Senate present.[17] This opens up the possibility that a CTA negotiated by

15. *See* B. HAWK, UNITED STATES COMMON MARKET AND INTERNATIONAL ANTITRUST, A COMPARATIVE GUIDE 423 (1st ed. 1979).

16. K. DAM, *supra* note 10, at 290-91; THE STANDING SENATE COMMITTEE ON FOREIGN AFFAIRS, III; CANADA-UNITED STATES RELATIONS: CANADA'S TRADE RELATIONS WITH THE UNITED STATES 32-33 (Mar. 1982) [hereinafter cited as Senate Committee Report].

17. U.S. CONST. art. II, § 2.

the two governments could be significantly altered as a result of opposition in the Senate. Because of this, a treaty is apt to be more difficult to negotiate and implement than an executive agreement. The U.S. administration, when seeking to negotiate a treaty, must take account of the views and priorities of key U.S. legislators, or else any agreement subsequently brought forward for Senate consideration may well be rejected. Canada experienced this problem in the case of the 1979 East Coast Fisheries Treaty, which failed to gain Senate consent owing to the determined lobbying of influential senators from the New England states.

Despite the probable difficulty of winning Senate approval for a Canada-United States trade treaty, a treaty would have certain advantages from Canada's perspective. The U.S. Constitution provides that all treaties entered into by the United States "shall be the Supreme Law of the Land."[18] Upon consent by the Senate and ratification by the President, a treaty assumes the force and effect of a U.S. federal statutory provision. Like federal statutes, treaties preempt all subsequent inconsistent state laws and regulations, provided they are "self executing."[19] Several U.S. Supreme Court cases have held that a valid, "self-executing" treaty overrides state laws on matters which, in the absence of the treaty, would ordinarily be within the powers reserved to the states.[20]

Among the three types of executive agreements possible under U.S. law,[21] the so-called congressional-executive agreement, which arises, for example, when Congress enacts legislation which for its execution requires or implies authority to conclude an international agreement on the part of the President, would probably be the most effective way to implement a Canada-United States trade pact. Any international agreement concluded as a congressional-executive agreement can also be concluded by treaty; the judgment as to which procedure should be used is generally a political one.[22] Agreements on tariffs and other trade matters are now often effected by congressional-executive agreement in recognition of the special role of the House of Representatives in regard to raising revenue. Either a treaty or a congressional-executive agreement would be preferable to a so-called sole-executive agreement, which is neither negotiated pursuant to congressional legislation nor authorized by an existing treaty, because there is uncertainty about whether such agreements are on an

18. *Id.* art. VI, § 2.

19. A "self-executing" treaty directly establishes a rule of law defining rights and duties, without the need for additional implementing statutes. *See* Foster v. Neilson, 27 U.S. (2 Pet.) 253 (1829); United States v. Percheman, 32 U.S. (7 Pet.) 51 (1833).

20. *See, e.g.*, Missouri v. Holland, 252 U.S. 416 (1920).

21. RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW OF THE UNITED STATES (revised) §§ 302, 306-08 (Tent. Draft No. 1, Apr. 1, 1980).

22. *Id.* § 307, Comment b.

equal footing with congressional statutes except in areas of express executive constitutional powers.[23]

Insofar as Canadian constitutional law is concerned, the question of domestic implementation of a trade agreement is considerably more complicated. This is due primarily to two factors. First, unlike the United States, Canada only gradually severed its colonial links, and its capacity to conclude international treaties emerged in like fashion. (Canada's emergence as a fully sovereign nation was formally recognized in the 1931 Statute of Westminster[24] but its international personality may have been acquired some eight years earlier.[25]) Secondly, Canadian constitutional jurisprudence has placed considerable emphasis on the notion of the exclusive legislative competence of the federal and provincial governments. As one commentator has pointed out, this has tended to restrict the applicability of a strong paramountcy doctrine,[26] so that in matters such as foreign relations, federal responsibility for international relations might be paramount to an otherwise recognized provincial jurisdiction. The development of jurisprudence dealing with the division of powers in the federal state prior to judicial consideration of the federal treaty-making power contributed to the present day conventional view of Canadian constitutional law, namely, that where the federal government concludes a treaty that would otherwise impinge on matters of provincial jurisdiction, provincial legislation implementing the international obligation is required.

Although consultations with the provinces have taken place during past GATT negotiating rounds, the federal government has traditionally exercised a relatively unfettered primacy in GATT negotiations and has not had to seek formal provincial legislative involvement. This is basically because the negotiations centered on matters that were clearly subject to federal jurisdiction. The widening scope of GATT, and of the Canada-United States discussions, into areas of provincial jurisdiction raises questions about provincial participation in the negotiating process. Indeed, in a "First Ministers Conference" held in late November of 1985, the principle of "full provincial participation" in trade discussions emerged. The

23. *Cf.* United States v. Guy W. Capps, Inc., 204 F.2d 655 (4th Cir. 1953) (holding that an executive agreement that conflicted with an act of Congress was invalid), *aff'd on other grounds*, 348 U.S. 296 (1955).

24. 22 Geo. V., c. 4 (U.K.)

25. *Reference Re: Amendment of the Constitution of Canada* (No. 1, 2, and 3), (1981), 1 S.C.R. 753, 125 D.L.R. (3rd) 1 at 44 (majority *per* Laskin C.J.C., Dickson, Beetz, Estey, McIntyre, Chouinard and Lamer J. J.).

26. H. Scott Fairley, Jurisdiction Over International Trade in Canada: The Constitutional Framework, Paper presented to the University of Windsor Conference on the Legal Framework for Canada/United States Trade, Sept. 20-21, 1985, to be published by Carswell Legal Publishers in a volume entitled THE LEGAL FRAMEWORK FOR CANADA/UNITED STATES TRADE. *See also* P. HOGG, CONSTITUTIONAL LAW OF CANADA 245-46 (2d ed. 1985).

precise meaning of the principle (the provinces claim it confers a provincial veto while the federal government claims it means full consultation only) has yet to be determined. It is representative, however, of the serious constitutional difficulties Canada presently faces in international trade negotiations.

III. An Overview of a Possible Comprehensive Trade Agreement

Given the size and complexity of the Canada-United States economic and trading relationship, it would be difficult to negotiate an agreement that addressed all of the main issues in a definitive fashion. Neither party, it is submitted, would or indeed should be willing to conclude an agreement that did not provide for flexibility as the new relationship evolved and for exceptions which in certain circumstances would permit the suspension of an obligation. Moreover, it is not possible to forecast accurately all new issues that might need to be resolved. Thus, in addition to the dispute settlement and consultation provisions that would necessarily be a part of an agreement, it would be prudent to create working groups pursuant to the treaty, to consider issues deserving of further negotiation and areas suitable for harmonization of domestic laws. In our view, therefore, the parties would benefit from an open-ended agreement. The major elements which we envisage as comprising a CTA are examined below.

IV. Major Elements of a Comprehensive Trade Agreement

A. Tariffs

The gradual phasing out of remaining tariffs in respect of most bilateral trade in goods would be the cornerstone of a bilateral CTA consistent with GATT rules. The Closer Economic Relations Trade Agreement recently negotiated between Australia and New Zealand calls for the immediate elimination of tariffs not exceeding 5 percent ad valorem; for the phasing out of tariffs of more than 5 percent, but not exceeding 30 percent ad valorem, by 5 percentage points per year; and for the phasing out of tariffs in excess of 30 percent ad valorem over a period of six years.[27] By 1987, most Canada-United States trade in goods will be largely tariff-free or subject to nuisance tariffs that have little protective effect. By that date, it is estimated that 80 percent of Canada's industrial exports to the United States will enter duty-free, and up to 95 percent will face tariffs of 5 percent or less. For U.S. industrial exports to Canada, the comparable

27. The Australia-New Zealand Closer Economic Relations Trade Agreement, art. 4:4 (a), (b), and (c), *reprinted in* 22 I.L.M. 946 (1983).

figures will be 65 and 91 percent, respectively.[28] Thus, to a substantial degree, Canada-United States trade in nonagricultural goods will already be tariff-free by 1987. However, it is important to note that tariffs maintained by both countries in the past have inhibited trade in certain sectors. Moreover, tariffs will still remain an important trade barrier in a number of sectors, particularly in Canada, which has higher tariffs than the United States. An eight to ten year transition period for the phasing out of bilateral tariffs would seem to be appropriate, but since the adjustment burden is likely to be more acute for Canada, it may be that different rates for phasing out tariffs could be negotiated by the two countries.

As noted above, article XXIV of GATT specifies that "substantially all" trade must be freed of tariffs and other restrictions in order for an agreement to be acceptable in GATT. In practice, this requirement has been interpreted quite flexibly. The European Free Trade Area (EFTA), for example, is basically limited to trade in industrial goods,[29] although special bilateral agreements with respect to trade in agriculture have been negotiated by some EFTA signatories. In general, Canada and the United States should not have much difficulty in convincing GATT that a bilateral agreement covering, say, 90 percent of bilateral trade in goods (with selected services as well) is acceptable under GATT rules and according to previous GATT jurisprudence.

Two approaches would be open to Canada and the United States. First, they could decide simply to issue a declaration that a free trade area as defined by GATT rules exists between them, and proceed to liberalize trade further in various products or sectors. Second, they could conclude an "interim agreement" leading to the eventual formation of a bilateral free trade area. The declaratory approach is weakened by the fact that only 65 percent of Canada's industrial imports from the United States will be tariff-free by 1987, and that nontariff barriers will still be potent trade impediments between the two countries. The interim agreement approach thus would be preferable. This would require Canada and the United States to adopt a clear plan and schedule for the removal of tariffs.

B. Exceptions

All trade agreements contain provisions which spell out exceptions to the general commitment to phase out tariffs (and other trade barriers). As noted previously, a CTA is likely to contain certain exceptions. One

28. Senate Committee Report, *supra* note 16, at 9.

29. Convention Establishing the European Free Trade Association, *signed at* Stockholm on Jan. 4, 1960; *entered into force* on May 3, 1960; 370 U.N.T.S. 3 [hereinafter cited as EFTA].

important type of exception could relate to certain products, or categories of products, that would be exempt from the elimination of tariffs or other kinds of trade barriers (e.g., quantitative restrictions). The number of such products must be kept small in order to ensure compliance with GATT rules regarding the commodity coverage of acceptable regional trade liberalization agreements. The idea of seeking exceptions from trade liberalization must be considered in terms of the danger that the number of sectors excluded could snowball. This suggests that exceptions should be kept to a minimum. It is important to recognize that vulnerable industries in both countries can be cushioned from the impact of trade liberalization through devices other than product exceptions. For example, tariffs can be removed more slowly in particularly sensitive sectors, and special assistance measures (such as certain kinds of permissible subsidies) can be used to ease the adjustment burden.

Having said this, it is possible that both countries may wish to exempt at least a few industries from a bilateral free trade agreement, including parts of agriculture and, perhaps in Canada, certain sensitive "cultural industries."[30] Other regional trade pacts have exempted the agricultural sector (e.g., the European Free Trade Area).[31] Exemptions would be acceptable provided that the total volume of bilateral trade represented by all these excluded sectors was kept relatively small. In order to ensure that the number of excluded sectors and products is kept small, it would be advisable for the two countries to start with the presumption that all sectors will be covered, at least with respect to tariff-removal, and then bargain over exceptions and exclusions.

C. Safeguards

Most trade agreements allow for trade restrictions in the event that sudden surges of imports disrupt, or threaten to disrupt, a particular domestic industry, and that such an import surge is attributable to previously implemented trade barrier reductions negotiated under the terms of the agreement. Article XIX, the key safeguard provision of the GATT, allows for the application of special protective measures to deal with situations of "serious injury" caused by increased imports of particular products as a result of what are termed "unforeseen developments."[32]

One of Canada's present concerns in its trade relations with the United States is the potential for "side-swipe" safeguard actions. Under GATT

30. R. Lipsey & M. Smith, Taking the Initiative: Canada's Trade Options in a Turbulent World 134-6, 143; & chap. 6, 94-102 (1985).
31. EFTA, *supra* note 29, at art. 21.
32. K. Dam, *supra* note 10, at 99-107.

article XIII, trade measures instituted to safeguard domestic producers are to be applied on a nondiscriminatory basis.[33] Thus, even though Canadian producers may not be the cause of injury to U.S. producers, they can be swept up by a safeguard action aimed at a third country. A CTA could address the "side-swipe" problem by disciplining safeguard action in respect of each party's products by restraining it to apply safeguards only where the serious injury or the threat thereof is substantially caused by the reduction or elimination of a duty as provided in the CTA. In addition, it could provide an exemption from safeguard actions aimed at third countries where, in the view of the importing party, the importation of a product from the other CTA signatory is not a significant cause of serious injury or the threat thereof. This would be similar to the approach taken in article 5 of the recent United States-Israel Agreement.[34]

A more difficult problem for Canada concerns the role that Congress plays in the import relief process. From the foreign perspective, there is a disturbing reluctance in the United States to accept a negative determination in an import relief case brought before the International Trade Administration (ITA) and the International Trade Commission (ITC). In recent years, although negative determinations have been made in several cases, nevertheless Canada has been under pressure to impose "voluntary restraints" on certain exports to the United States. The case of softwood lumber is a good example.[35]

In 1982, a section 332 fact-finding investigation was undertaken by the ITC to inquire into conditions relating to the importation of softwood into the U.S.[36] This was followed by a countervailing duty petition.[370] U.S. domestic producers alleged that Canadian softwood lumber received government subsidies and that the "stumpage" systems (or removal rights) conferred countervailable subsidies on lumber production. The ITA found that certain government programs in Canada did constitute subsidies, but they were de minimis, accounting for less than 2.5 percent of import value and hence were not countervailable. More importantly, the ITA found

33. Art. XIII, par. 1, of GATT, *supra* note 2, provides:

No prohibition or restriction shall be applied by any contracting party on the importation of any product of the territory of any other contracting party . . . unless the importation of the like product of all third countries . . . is similarly prohibited or restricted.

34. United States-Israel Agreement, *supra* note 7, at art. 5.

35. On the lumber dispute, *see* G. Jansen, Canada-United States Trade Relations: The Lessons of the Softwood Lumber Countervail Case (Conference Board of Canada 1984).

36. CONDITIONS RELATING TO THE IMPORTATION OF SOFTWOOD LUMBER INTO THE UNITED STATES, REPORT OF THE PRESIDENT OF INVESTIGATION NO. 332-125, USITC Pub. 1241, Apr. 1982 (conducted pursuant to section 332 of the Tariff Act of 1930, 19 U.S.C. § 1332 (1982)).

37. *Softwood Lumber from Canada,* Determination of the Commission in Investigation No. 701-TA-197 (Preliminary) Under Section 703 (a) of the Tariff Act of 1930, together with the information obtained in the investigation, USITC Pub. 1320, Nov. 1982.

that stumpage systems did not confer a subsidy, in the words of the Act, to a "specific enterprise or industry."[38]

Although it terminated the ITC proceedings, this negative determination did not complete the import relief process. Activity shifted to Congress, which was quite sympathetic to domestic producers' demands for relief. A number of legislative initiatives emerged, two of the more notable being Representative Weaver's Canadian Softwood Import Control Bill[39] and Representative Gibbons' Natural Resource Subsidy Bill.[40] Neither bill was enacted into law. Indeed, both encountered opposition from the Administration.[41] Nevertheless, they must be taken very seriously by foreign producers because they provide the Administration with clear evidence of strong congressional interest in an important trade problem. Congressional displeasure with Canadian softwood imports reached such a level that the United States Trade Representative (USTR) indicated to Canadian representatives that the issue needs to be dealt with before a bilateral trade pact could be concluded.[42] In 1985, the USTR requested an update of the 1982 section 332 investigation and a report was completed in October.[43] More recently, in June 1986, the Commerce Department announced that it would hear a new subsidy complaint being brought by U.S. lumber producers. And on October 16, 1986, a preliminary determination of subsidy (reversing the 1983 finding) was made by the ITA.

The point to note is that a 1982 ITA determination that a countervailable subsidy did not exist merely completed the first stage of a protracted trade dispute. Responding to the formal apparatus for the resolution of trade complaints and, in addition, to the Congress and the administration, requires close foreign attention and considerable resources in order to combat the threat of trade-restraining action. One of Canada's negotiating objectives, therefore, may be to make the remedies available under a CTA as exclusive as possible. This would inhibit Congress from responding to special interests and legislating special exceptions to the CTA. Thus, an Article dealing with "New Restrictions on Trade" (similar to that found in the United States-Israel Agreement[44] could provide:

38. *Id.*

39. H.R. 1088, 99th Cong. 1st Sess. (1985).

40. H.R. 2451, 99th Cong. 1st Sess. (1985).

41. For a discussion of Congress' treatment of Rep. Gibbon's proposed amendment to the trade laws, *see* Bello & Holmer, *Subsidies and Natural Resources: Congress Rejects a Lateral Attack on the Specificity Test*, 18 GEO. WASH. J. INT'L L. & ECON. 297 (1984).

42. Private confidential interview Dec. 12, 1985. The issue has also been discussed on a regular basis in Canada's financial newspapers. *See also, Vision Lacking in Reagan Push for Free Trade Pact*, Financial Post (Toronto), June 14, 1986 at 10.

43. CONDITIONS RELATING TO THE IMPORTATION OF SOFTWOOD LUMBER INTO THE UNITED STATES, REPORT TO THE PRESIDENT ON INVESTIGATION NO. 332-210 UNDER SECTION 332 OF THE TARIFF ACT OF 1930.

44. United States-Israel Agreement, *supra* note 7, at art. 4.

> New customs duties on imports or exports, or any charge having equivalent effect and new quantitative restrictions on imports or exports or any measure having equivalent effect, may be introduced in the trade between the Parties *only if permitted by this Agreement or by the GATT* as in effect on the date of entry into force of this Agreement, and as interpreted by the CONTRACTING PARTIES to the GATT, and insofar as not inconsistent with this Agreement.

Another kind of safeguard discussed in connection with Canada-United States trade liberalization is an employment or production guarantee. The Auto Pact,[45] for example, contains safeguards with respect to Canadian production. It has been suggested in Canada that production or employment safeguards should be included in a trade agreement. However, it seems to us that there is virtually no possibility that the United States would be prepared to accept permanent production or employment safeguards for Canadian industries as part of a CTA. (In fact, the very idea of permanent safeguards is at variance with the principles of liberalized trade.) The United States might be persuaded to accept short-term, transitional safeguards in order to provide Canada a measure of assurance against rapid and substantial employment losses in vulnerable industries. However, the same objective probably could be met by the inclusion of an adjustment provision. Because no trade negotiator can fully anticipate the strength of future adjustment pressures, a special provision could be included in a CTA to address the problem of unforeseen adjustment difficulties. This would operate as a "back-up" to the safeguard provision. As it would apply only in exceptional circumstances, the language of such a provision could be drafted so as to require the following:

- (1) for notification and consultation in respect of proposed emergency action;
- (2) in the notification, the Party taking action must demonstrate the urgency of, and necessity for, taking action;
- (3) the period of time permitted for such action should be limited to eighteen months unless an extension is agreed to by the other party; and,
- (4) to ensure that the provision is not a permanent part of the CTA, a "sunset" clause should be included to provide for its demise in five or, at the maximum, ten years after the CTA enters into force.

D. Rules of Origin

Under a free trade area agreement, the member countries may maintain different tariffs and other trade restrictions against imports from non-

45. Agreement Concerning Automotive Products, Jan. 16, 1965, United States-Canada, 17 U.S.T. 1372, T.I.A.S. No. 6093. The Agreement was enacted into U.S. law by the Automotive Products Trade Act of 1965, Pub. L. No. 89-283, 79 Stat. 1016 (1965) (codified at 19 U.S.C. 1202, 2001, 2011-2015, 2021-2024, 2031-2033 (1976)).

member states. This necessitates the development of rules of origin. The origin of products that cross the common frontiers of the free trade area must be determined so that free access can be denied to those which originate elsewhere. The EFTA Convention permitted a product to qualify for duty-free treatment provided that at least 50 percent of its export price originated in the free trade area.[46] The United Kingdom-Ireland free trade agreement of 1966 set a content requirement of 25-50 percent, depending on the products.[47] Whether the rules of origin in a future CTA would be relatively liberal or quite strict would of course be a matter for negotiation.[48] The United States, for its part, may well prefer a less liberal approach to rules of origin. It should be noted that to the extent that both countries maintained similar tariff levels vis-à-vis third countries, the rules of origin problem would be somewhat diminished.

E. Timing of the Agreement

In the section dealing with tariffs above, it was suggested that the trade liberalization under a CTA could be phased in over a period of, say, ten years for Canada and perhaps less for the United States. Because the adjustment burden would be greater for Canada than for the United States, it may be possible to gain U.S. acceptance of the principle that a longer transition period is needed for Canada. Under Article XXIV of the GATT, an interim regional trade agreement must lead to duty-free trade within a "reasonable" period of time. However, the term "reasonable" is not defined in GATT, and in practice GATT has accepted regional agreements with widely varying transition periods. EFTA originally provided for a transitional period of nine-and-a-half years; this was subsequently shortened to six-and-a-half years.[49] The 1983 Australia-New Zealand trade agreement envisages an eight-year transition period.[50] Both the Standing Senate Committee on Foreign Affairs and the Economic Council of Canada proposed an eight to ten year phase-in period.[51] Thus, there should be no problem in obtaining GATT approval of a bilateral CTA under which remaining tariffs on "substantially all" bilateral trade are removed within a period of up to ten years.

---

46. EFTA, *supra* note 29, art. 4.
47. Agreement Establishing a Free Trade Area, *signed at* London on Dec. 15, 1965; 565 U.N.T.S. 58, at art. 2(1) (b) (*entered into force* July 1, 1966).
48. Senate Committee Report, *supra* note 16, at 91-3.
49. *See supra* note 29.
50. *See supra* note 27.
51. Senate Committee Report, *supra* note 16, at 90; Economic Council of Canada, *Canada's Trade Options* (1975).

While GATT places a vague overall limit on the length of the transitional period leading to free trade,[52] there is no constraint on variations in timing for the removal of tariffs on particular products or sectors. Thus, in cases where Canadian or U.S. producers are currently fully competitive vis-à-vis their counterparts, remaining tariffs could be eliminated immediately. In more vulnerable sectors a longer transition period will be sought. One interesting approach would be for both countries to agree to eliminate immediately tariffs of 5 percent or less, and to phase out remaining tariffs by 1 percent per year.[53] This would confer a modest advantage on Canada because its tariffs on dutiable industrial imports are, on average, higher than U.S. tariffs.

F. Non-Tariff Measures

Canadian interest in a CTA is closely linked to concern over the growth and impact of U.S. non-tariff measures, particularly those which have often been categorized as "contingency protection" measures (the "import relief" laws)[54] and the government procurement practices of U.S. federal and state governments. The former can be invoked by domestic producers where it appears that dumping is occurring, or imports have benefitted from government subsidies in their country of origin, or even where the imports are being fairly traded but are nevertheless a substantial cause of serious injury. There are other U.S. import relief laws, such as section 337 of the Tariff Act of 1930[55] (unfair trade practices and methods of competition in the importation of products into the U.S.) and the 1916 Antidumping Act[56] (which makes dumping with intent to injure a criminal offence) which have not received widespread Canadian attention.

The second non-tariff measure, government procurement practices, refers to the purchasing practices of public authorities. Under the GATT, contracting parties are obliged to accord "national treatment" to one another in respect of internal measures that can affect trade. However, government procurement practices are excluded from the national treatment obligation. Article III, paragraph 8(a), provides:[57]

> The (national treatment) provisions of this article shall not apply to laws, regulations, or requirements governing the procurement by governmental agencies of products purchased for governmental purposes. . . .

52. GATT, *supra* note 40, at art. XXIV.
53. Lipsey & Smith, *supra* note 26, at 167.
54. *See, e.g.*, R. Grey, United States Trade Policy Legislation: A Canadian View 1-18 (1982).
55. 19 U.S.C.A. § 1337 (West Supp. 1986).
56. 39 Stat. 798, 15 U.S.C. 72 (1982).
57. GATT, *supra* note 2, at art. III: 8 (a).

Government procurement practices were addressed in the last Tokyo Round of multilateral trade negotiations (MTN). An Agreement on Government Procurement was concluded,[58] but its scope and product coverage remains limited. It does not cover matters of mutual interest to Canada and the United States, nor does it apply to subordinate governments in federal states such as Canada and the United States.

1. *The Import Relief Laws*

Antidumping duties can be imposed when foreign goods entering the domestic market are priced below their home market (or fair market value) price. The antidumping laws of both Canada and the United States have been enacted pursuant to internationally agreed standards negotiated under the auspices of GATT. Antidumping laws have been criticized as being essentially anticompetitive in terms of their normative content.[59] From the antitrust perspective, when determining "material injury," they place undue emphasis on quantitative factors such as the degree of price suppression, while ignoring such considerations as predatory intent. A respectable body of commentators in the United States has criticized the antidumping (and other import relief) laws for treating actions as "unfair" when, according to the antitrust laws, they would be regarded as procompetitive.[60] The existence of domestic price discrimination competition laws in the United States and Canada suggests that perhaps the antidumping laws could be made non-applicable to trade governed by the CTA, and that price discrimination that injured competition as opposed to domestic producers may be a more appropriate standard for the CTA (this is discussed further below[61]).

A more serious problem for bilateral trade is posed by subsidies and the use of countervailing measures against subsidized goods.[62] For Canada, the threat of U.S. countervail action against exports to the U.S. market is a source of great concern because of the aggressive way in

58. Agreement on Government Procurement, *done* Apr. 11, 1979, MTN/NTM/W/211/Rev. 1 *reprinted in* Agreements Reached in the Tokyo Round of the Multilateral Trade Negotiations, H.R. REP. No. 153, 96th Cong., 1st Sess., pt. 1 at 67-189 (1979).

59. *See* J. ATWOOD & K. BREWSTER, ANTITRUST AND AMERICAN BUSINESS ABROAD (2d ed.); J. Barcello, *Antidumping Laws as Barriers to Trade*, 57 CORNELL L. REV. 491 (1971); Barcello, *Subsidies and Countervailing Duties—Analysis and Proposal*, 9 LAW & POL. INT. BUS. 779 (1977); Paugh, *Antitrust Principles and U.S. Trade Laws: A Review of Current Areas of Conflict*, 12 LAW & POL. INT'L BUS. 545 (1980); Report of the American Bar Association's *Ad Hoc Subcommittee on Antitrust and Antidumping*, 43 ANTITRUST L.J. 653 (1973-74).

60. *See* sources cited *supra* note 59.

61. *See infra* text accompanying notes 64-68.

62. On U.S. subsidy and countervailing duty law and policy, and the growing importance of subsidies in an international trade policy issue, see GREY, *supra* note 54, at 37-43; G. HUFBAUER & J. ERB, SUBSIDIES IN INTERNATIONAL TRADE (1984).

which the United States deals with countervail cases. For example, as a result of the *Michelin* case,[63] Canada's regional development subsidies have been held to be countervailable under U.S. law. This was the first time in U.S. trade law history that a domestic as opposed to an export subsidy was countervailed. One of the most important challenges facing the negotiators of a CTA would be to devise mutually acceptable rules governing the use of subsidies and countervailing measures. This will be a priority for Canada in view of the impact which U.S. policies toward subsidies can have on jobs, exports, and investment decisions. For its part, the United States will no doubt be anxious to see new disciplines imposed on Canada's subsidy practices as part of any mutually acceptable CTA.

Among the possible means of addressing the problems caused by nontariff measures are such institutions as a joint commission that would have exclusive jurisdiction to settle bilateral trade disputes and the negotiation of common standards that would make the granting of relief more difficult (due to higher standards of injury, more difficult tests of causation, etc.).

The proposal for a joint commission with exclusive jurisdiction to settle disputes, while an interesting idea, does not accord with traditional Canada–United States dispute settlement practice. Both states have been reluctant to surrender sovereignty to an institution with binding powers. Indeed, the bilateral relationship is notable for the absence of such institutions and its reliance on ad hoc procedures. Thus, while not denying either the potential efficacy of a joint institution with recommendatory powers or its utility as a forum for consultations, there is some doubt that a permanent body with binding powers is feasible.

In respect of the second approach, it is conceivable that the parties might agree to modifications of the import relief laws in matters such as:

- (1) establishing a certain share of the domestic market that must be obtained by imports from the other party before permitting an anti-dumping or countervailing duty complaint to proceed. If the market share limit were set at 15 percent, then where the other party's imports accounted for less than 15 percent, no import relief proceedings could be brought;
- (2) in subsidy cases involving a complaint by a subsidized *domestic* industry brought against subsidized imports, the law could be changed

63. This case is discussed in F. LAZAR, THE NEW PROTECTIONISM 28 (1982). *X-Radial Steel Belted Tires from Canada*, 38 Fed. Reg. 1018 (Jan. 8, 1973); 46 Fed. Reg. 48,737, (1981) *aff'd in part, rev'd in part*, Michelin Tire & Rubber Corp. v. U.S., 49 F. Supp. 270, (cf. Int'l Trade Oct. 26, 1981).

to require that the "margin" of the countervailing duty would be the difference between the domestic subsidy and the foreign subsidy (if higher);

- (3) the standard of injury in antidumping and countervailing duty cases could be changed from "material" injury (defined as harm that is not unimportant or inconsequential) to a stricter standard of "serious" injury; and,
- (4) the causation test for linking the dumping or subsidization to injury to domestic producers could be changed to require a more direct link of causation than at present.

This approach has the attraction of making modest changes in the import relief laws. However, it must also be said that it gives rise to some significant problems. First, the United States already distinguishes between GATT contracting parties when determining whether a "material injury" standard should be applied to subsidized imports: it applies a material injury standard only in respect of imports from signatories of the 1979 GATT Subsidy Code; nonsignatories are not entitled under U.S. law to an injury standard. In the latter case, if a foreign "bounty" or "grant" is found, a countervailing duty is imposed without further inquiry into material injury.[64] This differential treatment has already exposed the United States to complaints in the GATT. India threatened to convene a dispute panel to decide whether the United States was violating its obligation under article I of the General Agreement, which extends unconditional most-favored-nation treatment to all contracting parties of the GATT.[65] It appears that rather than run the risk of a panel making such a determination, the United States agreed to apply the material injury test to imports from India. This experience in the GATT suggests that the United States' international trade obligations may lead it to resist Canadian attempts at a further differentiation in U.S. trade law (especially now that a new round of multilateral trade negotiations is in the offing).[66] The negotiation of standards that would make import relief more difficult to obtain also goes directly against the recent trend in U.S. domestic law, as exemplified by the *Trade and Tariff Act of 1984*,[67] which is to facilitate

64. For a discussion of this different treatment and a defense thereof, *see* Hufbauer, Erb & Starr, *The GATT Codes and the Unconditional Most-Favored-Nation Principle*, 12 LAW & POL. INT'L BUS. 29 (1980).

65. *See* BNA ITIM, vol. 97 (Oct. 7, 1981) at 5. This question is discussed by John Jackson in GATT Machinery and the Tokyo Round Agreements, in TRADE POLICY IN THE 1980S 159 (W. Cline ed. 1983).

66. The authors understand that the question of differential treatment continues to be discussed in the GATT, particularly in the Working Group on MTN Agreements and Arrangements.

67. Pub. L. No. 98-573, 98 Stat. 2948 (1984).

the bringing of import relief complaints and to make injury determinations easier rather than more difficult to obtain.[68]

Finally, there is doubt as to whether a change in substantive standards would actually inhibit the frequency of import relief actions. In this regard it is important to keep in mind the practical realities of the U.S. litigation process. First, contingency protection actions are less expensive than some other forms of other litigation because most of the investigation is conducted by the Commerce Department and the ITC (rather than the complainants themselves). Secondly, there is a considerable nuisance value in bringing a petition for import relief; the mere rumor of an impending petition can cause foreign producers to revise their prices upwards. This has a chilling effect on foreign competition that is well understood by U.S. complainants. Hence, it is far from certain that changes in the U.S. injury definition or causation standards would themselves materially improve the situation for Canadian exporters.

There are factors peculiar to the North American relationship which indicate that over the longer term the application of the import relief laws to intra-North American trade should be questioned. The extent of transborder direct investment (in both directions), together with the general similarity in the two countries' legislation dealing with commercial transactions, corporations, securities markets, and competition suggests that attention could usefully be devoted to moving away from the essentially mercantilistic character of GATT standards to a more liberal and functionally-based set of standards to govern the North American market for goods (and some services) that would be created by the reduction and removal of tariffs and quantitative restrictions.

There is no question that even on this approach agreement on subsidies practices would be desirable. One solution might be to impose a strong discipline on the granting of subsidies by governments at the federal and state/provincial levels. For example, under a CTA: (1) certain practices could be prohibited outright; (2) other permissible subsidy practices could be subject to consultation if, in the view of the importing party, they substantially frustrate the benefits expected from the removal or absence of duties and quantitative restrictions on trade between the parties; and, (3) finally, were government-to-government consultations to fail, a subsidy matter could be referred to a Canada-United States Trade Committee for dispute settlement. The purpose of such provisions would be to impose greater discipline on those who grant aid (i.e., the governments themselves) in return for taking subsidy complaints out of the sphere of private

68. For a discussion of the Act, see Bello & Holmer, *The Trade and Tariff Act of 1984: Principal Antidumping and Countervailing Duty Provisions*, 19 INT'L LAW. 539 (1985).

enforcement. Subsidy matters could be discussed on a government-to-government basis; if consultations failed, then the affected party could take "any appropriate measure" (one such measure could be to then impose countervailing duties).

Having reached an accommodation on subsidy practices the trade agreement could then contain provisions that would protect the integrity of the unified market being created. The second part of this approach could be to negotiate "Fair Competition Standards." A CTA could prohibit marketing practices such as: agreements between enterprises which have as their object or result, the prevention, restriction, or distortion of competition within the territory covered by the CTA; price discrimination which substantially injures competition; and such other distributive practices that the parties agreed had the effect of injuring competition in the North American market. The object of these provisions would be to shift the focus of a trade complaint from injury to the domestic producer to injury to competition. Thus, a CTA could dispense with the "material injury" determination and inquire into whether a private party's actions substantially injure competition or whether agreements between parties prevent, restrict or distort competition. Insofar as Canada-United States trade would be concerned, the two states would dispense with laws whose substantive standards are suspect to begin with, and, because of the relative ease of commencing proceedings, carry considerable nuisance value. Several considerations suggest that the two countries should move in this direction:

- (1) Experience in other trade liberalization arrangements indicates that a concern to remove *public* barriers to trade should be accompanied by disciplines on *private* barriers. As Lambrinidis states in his leading work, subtle methods of trade distortion can defeat the objectives of trade liberalization. Hence, it is "necessary to eradicate all activities the purpose and/or result of which is to distort, by artificial means, the natural conditions of international competition which would, otherwise, obtain."[69] Both the EFTA and the European Economic Community (EEC) have found it necessary to address private firm actions.[70]
- (2) The case for doing so in the North American context is all the more compelling given the fact that competition policy has occupied a more central role in the two countries (particularly in the United States). The fact of the matter is that in respect of distributive prac-

69. Lambrinidis, *supra* 14, at 177.

70. Convention Establishing the European Free Trade Association, *supra* note 29, art. 15; and Treaty Establishing the European Economic Community, *done at* Rome, Mar. 25, 1957, 298, U.N.T.S. 11, arts. 85 & 86.

tices, there are considerable areas of commonality between the existing laws of the two countries.

- (3) There is an uneasy coexistence between the import relief and competition laws. Were the two sets of laws not reconciled with each other, producers on both sides of the border could find that with enhanced access they could actually be subject to more, rather than fewer, legal actions than at present.
- (4) The fact of the matter is that U.S. courts and regulatory agencies *already* claim jurisdiction over foreign anticompetitive practices. This claim is highly unlikely to change. Thus, Canadian producers will find their actions subject to greater scrutiny (from an antitrust perspective) than at present, both when they take advantage of increased market opportunities in the United States and when U.S. firms take advantage of more open markets in Canada.
- (5) From the governmental perspective, as a CTA promotes the creation of a single North American market for goods, the basis for Canada's traditional objection to the extraterritorial application of U.S. antitrust law, namely, that markets are territorially divisible, will be eroded.

By suggesting the inclusion of competition standards as a means of addressing the import relief laws problem, we do not contemplate the adoption in Canada of U.S. antitrust law in toto (although we recognize the sophistication of many aspects of that body of law). Quite the contrary: the goal would be to draw from those areas of common approach to marketing practices a set of standards that would govern trade conducted pursuant to a CTA. These standards would be the exclusive grounds for challenging unfair marketing practices. By shifting the focus of the inquiry away from injury to domestic producers to injury to competition, relief would be more difficult to obtain. The more problematical question of mergers could be left out of a CTA, to be dealt with by the two national legislatures (perhaps subject to a duty to consult). We recognize that considerable study would have to be given to this suggested course of action. Nevertheless, a "fair competition" standard would assist in facilitating the changes in thinking that would be necessitated by the new trading relationship. Moreover, a failure to address competition concerns would be counterproductive; the parties could be perpetuating overlapping and indeed contradictory legal regimes in the new trading environment.

2. *Government Procurement Practices*

As part of a CTA, Canada and the United States should strive to open up markets for government purchases of goods and services to greater competition from the other country. Both countries maintain a plethora of laws and more informal policies at the national and sub-national levels

of government the effect of which is to provide preferential treatment for domestic suppliers of goods and services sold to public entities and, in some cases, to private entities whose activities are partly funded or otherwise regulated by government. Until the Tokyo Round of GATT trade negotiations, virtually no progress had been made in seeking to impose meaningful international disciplines on GATT contracting parties in respect of government procurement.[71] During the Tokyo Round, however, the major industrialized countries succeeded in negotiating a new code to govern behavior in this increasingly important area. The resulting Agreement on Government Procurement—signed by both Canada and the United States—represents a modest effort to open up government procurement to greater international competition.[72] Code signatories agreed to apply to each other treatment "no less favorable" than that accorded to domestic products and suppliers in respect of the procurement practices followed by selected government entities operating under their control.[73] However, much of government procurement—in the defense area, for example—remains outside the ambit of the GATT Agreement. From the perspective of Canada and the United States, it has done relatively little to open up their respective markets for government purchases to greater competition from suppliers located in the other country.

One approach that might be followed in a CTA would be to develop a "national treatment" rule, whereby each country would agree to treat suppliers from the other country as if they were domestic suppliers in its procurement decisions. However, this probably would prove to be too ambitious. Liberalization of procurement practices will be a gradual process, and it would not be a simple matter to reach a definitive resolution of this issue in the CTA itself. Instead, the two countries might agree to a provision as follows:

- The Parties recognize that the maintenance of preferences for domestic suppliers of goods to government agencies is inconsistent with the objectives of the Agreement.
- The Parties accordingly agree to work, on a reciprocal basis, to reduce and eliminate existing preferences in relation to federal, state, and provincial government procurement.

In addition to this type of general commitment, it would be desirable for Canada and the United States to achieve a measure of liberalization in

71. K. DAM, *supra* note 10, at 199-209.

72. Agreement on Government Procurement, *supra* note 58 [hereinafter cited as Procurement Agreement]. *See* Macdonald, *Foreign Trade Barriers to Canadian Exports and International Law: The General Agreement on Tariffs and Trade*, in NEW DIMENSIONS IN INTERNATIONAL TRADE LAW (J. Ziegel & W. Graham, eds. 1982), at 164-66.

73. *Id.* Art. II.1

government procurement matters when the CTA enters into force. This could be accomplished by developing lists of government departments and agencies on both sides of the border which would thereafter accord national treatment to suppliers from the other party in their purchasing policies.

In this connection, the situation which both countries face with respect to other levels of government should be mentioned. Provinces in Canada practice both "buy-Canadian" and "buy-provincial" discriminatory government purchasing policies,[74] while U.S. states have legislated many "buy-American" laws.[75] A formal bilateral trade treaty would restrict the ability of U.S. states to maintain purchasing preferences, but in Canada the constitutional position of the federal government is weaker.[76] Thus, Ottawa would have to convince the provinces to participate in a bilateral commitment with the United States in relation to government procurement; it probably could not compel them to do so.

G. Trade in Services

Services comprise an increasingly important share of world trade, and the development of more liberal rules to govern trade in services is now a priority for the United States.[77] Barriers to trade in services are not regulated by the GATT or other international accords, although the next round of GATT trade negotiations will begin to address the question of liberalization of services trade. Barriers typically take the form of domestic regulatory rules, administrative practices, licensing requirements, and restrictions on the right of establishment. It is expected that Canada and the United States would agree to reduce barriers to trade in at least some services as part of the CTA.

Largely because services have not been negotiated within the context of GATT, it is not clear exactly how amenable they would be to rules formulated in respect of trade in goods. Moreover, it is often extremely difficult to discern the differences between services trade and investment issues.[78] Hence, if the two countries are prepared to loosen restrictions

74. *See* Stegemann & Acheson, *Canadian Government Procurement Purchasing Policy*, 6 J. World Trade L. 442-78 (1972); and de Mestral, *The Impact of the GATT Agreement on Government Procurement in Canada*, in Non-Tariff Barriers After the Tokyo Round, 171-94 (J. Quinn & P. Slayton eds. 1982).

75. Lipsey & Smith, *supra* note 30, at 145-147.

76. On this problem, see F. R. Flatters & R. G. Lipsey, Common Ground for the Canadian Common Market (1983).

77. *See* J. Aronson & P. Cowhey, Trade in Services: A Case for Open Markets (1984).

78. In a recent article in the Journal of World Trade Law, Steven F. Benz stated:

The analysis of trade distortions in services becomes somewhat complex however, due

on the right of establishment in respect of investment, they should recognize that this may erode their ability to control trade in services. This is of particular importance when it is recalled that many services are subject to federal or provincial/state regulatory control in order to safeguard the public interest.

We contemplate a gradual movement towards liberalization of trade in services. First, the parties could include certain services in the CTA. These could be set out in an annex and would be governed by the rules of the CTA applicable to trade in goods except where significant national, provincial or state regulatory interests dictate otherwise. This point is extremely important. The object of applying the rules regarding trade in goods to trade in services is to separate as clearly as possible services trade from the provisions dealing with investment. This would protect services industries being established by characterizing them as "investments." In addition, the inclusion of a "significant regulatory interest" exception would be needed to protect the public interest.

Since the issues are complex and the terrain is largely uncharted at the international level, the process of freeing up trade in services would be an ongoing one. Thus, the CTA could provide for the establishment of a Working Group to continue to examine ways of liberalizing bilateral trade in services:

> To ensure the harmonious development of trade in services, the Canada-United States Trade Committee shall establish a Working Group on Trade in Services, to examine means of further liberalization of trade in services.

H. INVESTMENT

Canada and the United States have had a number of disputes over investment-related matters, the two most controversial being the trade-performance requirements of the Foreign Investment Review Agency (FIRA) and the "back-in" provisions of the National Energy Program.[79]

---

to the thin line between trade and foreign investment in services trade. For example, in the case of a Des Moines insurance company wishing to insure a German national, there exists the option of exporting its insurance service from Des Moines, or the establishment of a direct presence through a branch in Germany. In the first scenario, there is trade in a service. In the second, the international transaction will most likely be a flow of investment capital into Des Moines resulting from the ownership of its German capital assets.

BENZ, *Trade Liberalization and the Global Service Economy*, J. WORLD TRADE L. 100-101 (1985).

79. The trade performance requirements of FIRA were the subject of a GATT dispute panel. FIRA was established by the Foreign Investment Review Act, ch. 46, s. 2(1), 1973-74 Can. Stat. 620, *amended by* ch. 52, 1976-77 Can. Stat. 1274, *repealed by* the Investment Canada Act, Bill C-15 (1984). For a discussion of the Investment Canada Act, see Note, *The Investment Canada Act: A New Approach to the Regulation of Foreign Investment in*

Recognizing that investment concerns rank high on the United States negotiating agenda, the CTA could incorporate provisions derived from existing bilateral investment protection treaties. We envisage the two countries agreeing to accord the standard of "national treatment" with respect to bilateral investment. Specifically, the parties would agree to accord national treatment to investment originating from each other once that investment initially has been permitted to enter the territory of the other member state. This would not preclude the use of a screening process to examine the merits of allowing foreign investment—either in the form of acquisitions or new investment—to enter in the first instance.[80] The purpose of a national-treatment provision rather would be to ensure that, once foreign investors from a member state are allowed to invest in the other member state, they will be accorded treatment identical to that accorded to domestic investors.

Such a provision would not necessarily preclude the development of policies designed to protect particular industries or sensitive sectors from investment from the other signatory. Consistent with international treaty practice, the "right of establishment" article could be qualified to permit such screening:

> Each party shall encourage and create favorable conditions for nationals or companies of the other party to invest capital in its territory and, *subject to its right to make or to maintain exceptions falling within one of the sectors or matters listed in Annex*—to this Agreement, shall admit such capital.

However, the CTA should in general require each party to refrain from discriminating against the other's investment once the decision has been made to allow the investment to be made. It should be noted in this regard that existing treaty practice contemplates a qualification of the national-treatment principle. The United States itself has insisted on protecting its own right to restrict investment in certain sectors.[81] Accordingly, the CTA could set out the national treatment principle and then provide:

> The foregoing provisions of this Article *shall not be construed so as to oblige a Party to extend* to nationals or companies of the other *the benefits of any treatment, preference or privilege resulting from:*

Canada, 41 BUS. LAW. 83 (1985). Canada's National Energy Program was implemented, *inter alia*, by the Canadian Oil and Gas Act, ch. 81, 1980-82 Can. Stat. 2655. *See* Lacasse, *Legal Issues Relating to the Canadian National Energy Program*, 16 VAND. J. TRANSNAT'L L. 301 (1983); and B. DOERN & G. TUPPER, THE POLITICS OF ENERGY: THE DEVELOPMENT AND IMPLEMENTATION OF THE NEP (1985). A key provision of the NEP was the reservation for the Canadian Government of a 25 percent interest in all developments in areas known as the "Canada Lands" (basically, in northern Canada and offshore) that began production after December 31, 1980. This quickly became known as the "back-in" provision. Canadian Oil and Gas Act, sections 27-29. *See also* Lacasse, *supra*, at 344-49.

80. Lipsey & Smith, *supra* note 30, 160-62.

81. *See, e.g.*, Panama-United States treaty, *supra* note 6.

(a) (taxation laws or treaties); or

(b) *domestic legislation* in force at the time of signature of this Agreement *relating to specific economic activities reserved to nationals or companies of a Party.*

Acceptance of the national-treatment principle may be in both countries' best interests in the long run regardless of whether a CTA is established. It is consistent with both GATT rules and the code of conduct of the Organization for Economic Cooperation and Development on the treatment of foreign investment.[82]

I. Institutional Matters and Dispute Settlement

We envisage that as part of a CTA a permanent institutional structure would be established. We have chosen to call this a Canada-United States Trade Committee. This body would be charged with performing several important functions: (1) it would supervise the functioning of the agreement; (2) it would hold consultations on any matter affecting the operation and interpretation of the agreement; (3) it would consider ways of improving the functioning of the agreement and of the relationship over time; and (4) it would be able to establish working groups to conduct research and examine the prospects for further liberalization in areas that are not dealt with definitively in the agreement itself (e.g., services trade and government procurement preferences).

It is also to be expected that a dispute settlement mechanism would be an integral part of a CTA. In our view, it is unlikely that the two countries would consent to the creation of a supranational institution with binding powers. More likely is the development of a process whereby a trade dispute would initially trigger consultations. If this failed to solve the matter, the Canada-United States Trade Committee would then be convened to attempt to resolve the dispute. If this too proved unsuccessful, then either party could decide to refer the dispute to a conciliation panel which would endeavor to resolve the problem through the agreement of the parties. The panel would be called upon to issue a nonbinding report. Only after all of these steps had been taken would it be open to the aggrieved party to take appropriate measures to deal with the dispute in question. Although each party would thus remain free to take such action, there would nonetheless be considerable merit in the consultation and conciliation process. It would require the parties to choose whether to "elevate" the matter from consultations to the Committee and, in turn, to the conciliation panel. This would provide a means for "crystallizing" the issues between the parties. Over time, as with the GATT's dispute

82. A. E. Safarian, *Trade-Related Investment Issues*, in W. Cline, *supra* note 65, at 611.

panel decisions, a nonbinding yet persuasive body of jurisprudence could evolve. Moreover, the two countries might be constrained by the consultation-conciliation process from taking precipitate action. Not until the process had run its course would a party be free to take unilateral measures to deal with a trade conflict.

It is a remarkable characteristic of the Canada-United States economic relationship that even though it is extensive and multifaceted, relatively little in the way of formal institutionalization has grown up around it. Efforts to move toward a closer bilateral economic relationship should be accompanied by the establishment of improved institutional mechanisms to manage the emerging bilateral system and to provide a way of dealing with disputes and conflicts. A number of scholars recently have proposed the creation of new institutional and conflict resolution mechanisms.[83] In particular, the negotiation of a CTA will require the two countries to agree on the creation of a formal machinery both for dispute settlement and for monitoring the operation of the agreement. In the past Canada and the United States have relied on the GATT and on a host of ad hoc mechanisms to deal with trade disputes and irritants. This will no longer be sufficient once a new trade arrangement is put in place.

V. Conclusion

The bilateral trade negotiations which began in May 1986 represent a historic opportunity for two great trading nations to improve their commercial relationship by reducing the barriers that have been erected between them and by providing a clearer legal framework to govern bilateral trade. Many problems will have to be surmounted before an agreement acceptable to both countries can emerge. On the Canadian side, considerable concern exists in some quarters about the magnitude and impact of the adjustment burden that would have to be borne by domestic industries faced with an environment of freer bilateral trade. Some groups in Canada are also of the view that liberalization of trade with Canada's principal economic partner will threaten the existence of cultural institutions, domestic social programs, and other features of national life that, on the surface, appear to be rather remote from the subject of a trade agreement. For its part, the U.S. government is likely to encounter some opposition to the idea of a trade agreement with Canada in Congress and in a few industrial sectors presently suffering from import penetration due to the overvalued U.S. dollar.

83. *See, e.g.*, Cohen, *Canada and the U.S.—New Approaches to Undeadly Quarrels*, INTERNATIONAL PERSPECTIVES, 16-22 (Mar.-Apr. 1985); Drouin & Malmgren, *Canada, the United States and the World Economy*, FOREIGN AFFAIRS 395 (1981-82).

However, if both governments remain committed to the goal of a CTA, there is a reasonable chance that such an accord can be negotiated. If so, many of its elements would likely bear similarity to the proposals and provisions discussed above. In particular, a future Canada–United States trade agreement would almost certainly: phase out remaining tariffs on bilateral trade in goods within a period of up to a decade; provide for a measure of liberalization in respect of trade in selected service industries; contain some form of national-treatment obligation in respect of investment; reflect new rules and standards as applied to a variety of nontariff barriers and (perhaps) import relief laws; and provide for new mechanisms and procedures to deal with bilateral trade disputes. Whether a CTA would go further, to embrace the view that a single market is being created by the two countries which, in turn, requires the development of common competition policy and other standards, is more problematic. Regardless of how a future bilateral trade agreement may be structured, the complexity and magnitude of the Canada-United States economic relationship strongly suggests that it should be a flexible and open-ended accord suited to subsequent modifications and improvements.