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# Barriers to United States-Canadian Trade: Problems and Solutions, the Canadian Perspective

Richard Parker

*University of Connecticut School of Law*

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## **SPEECH**

### **BARRIERS TO UNITED STATES-CANADIAN TRADE: PROBLEMS AND SOLUTIONS, THE UNITED STATES PERSPECTIVE**

**RICHARD W. PARKER\***

#### **I. INTRODUCTION**

The United States and Canada are poised on the threshold of a truly historic set of negotiations which, if successful, will achieve almost total freedom of movement in goods and services between the two countries. The significance of this undertaking can only be gauged by the volume of trade already moving between the two countries, despite considerable impediments on both sides. United States exports to Canada last year accounted for around twenty-two percent of our total exports, while over seventy-five percent of total Canadian exports were to the United States. I am told that the volume of trade between the United States and Ontario alone exceeds the level of U.S. trade with our next largest trading partner, Japan.

A successful free trade area (FTA) is certain to expand and diversify this already enormous volume, benefiting consumers and enhancing the competitiveness of U.S.-Canadian production in an increasingly competitive global market. Such are the benefits of cooperation in trade. At the same time, no one is proposing a merger of the two economies. Both sides will continue to retain a measure of autonomy in their own domestic markets. The challenge for negotiators is to agree on an appropriate balance between integration and autonomy: deciding whether, in

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\* Associate General Counsel, Office of the United States Trade Representative. J.D., 1985, Yale Law School; Ph.D., 1982, Oxford University; B.A., 1978, Princeton University. The views expressed are those of the author only, and do not necessarily reflect those of the Office of the United States Trade Representative.

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what areas, and to what degree the agreement shall displace or modify the national laws and policies of the parties.

This afternoon I would like to share with you my view of the key U.S. objectives for the bilateral agreement and then discuss the likely relationships between this agreement and three different sets of pre-existing norms: international law as reflected in the General Agreement on Tariffs and Trade (GATT), U.S. domestic law, and the laws of the states or provinces. These are the relationships which both sides will focus on as they seek an agreement that properly balances autonomy and integration.

In the course of the discussion, I will have frequent occasion to refer to U.S. experience with the U.S.-Israel FTA, which went into effect in 1985. This is not to say that Canada and Israel are interchangeable as partners for free trade. Obviously, liberalizing trade with Canada will affect a vastly larger volume and diversity of trading interests. This means, inevitably, that the Canadian FTA negotiations will be longer and more complicated — involving tougher negotiations over higher economic stakes — than the U.S.-Israel talks.

Nevertheless, the Israeli talks represented the first U.S. experience with the negotiation of free trade areas; they were conducted from the outset as a possible precedent for a Canadian agreement, and they were subject to identical constraints in domestic and international law. That agreement serves as a useful point of reference for several of the issues I will address affecting the evaluation of proposals for liberalized U.S.-Canadian trade.

## II. UNITED STATES OBJECTIVES

The first, most obvious objective — in these as in the Israeli talks — is to eliminate tariffs on the widest possible range of traded goods and services. Canadian tariffs average between eight and nine percent, as compared to U.S. tariff levels averaging three to four percent. On both sides, these relatively low average figures conceal substantially higher tariffs in key sectors. In these sectors, even the mundane business of tariff reduction possesses formidable obstacles to agreement.

The second broad area of concern is nontariff barriers on trade in goods, maintained at both the federal and provincial level. A major challenge in this area will be agreeing on what *are* nontariff barriers, as distinct from valid health, safety, marketing

and/or consumer regulations or permissible uses of established trade remedy laws. Canada, for example, insists that U.S. application of antidumping or countervailing duty law to Canadian imports is a nontariff barrier. Canadians call it "contingent protection." Needless to say, Americans do not share this view.

In addition to the definitional dilemma, both sides must confront the fact that important areas of trade are regulated by independent or quasi-independent regulatory agencies and/or states or provinces. Each side must find a way to bind or obtain the voluntary cooperation of these separate entities if the comprehensive objectives of the agreement are to be obtained. I will return to this difficult issue in a few moments.

Third, the negotiations must resolve four particular issues involving Canadian practices if the end result is to be acceptable to the U.S. Congress. These are: (1) Canadian subsidization of timber exports; (2) Canadian provincial discrimination against U.S. brands in the marketing of alcoholic beverages; (3) inadequate Canadian protection of U.S. patents and copyrights; and (4) Canada's policy of reviewing and (possibly) forcing divestiture of U.S. companies investing in the "cultural" and energy sectors. Negotiations are currently underway on all but the last of these issues, and it is hoped that the issues can be resolved amicably outside the context of the FTA negotiations. In any case, the FTA discussions must resolve them.

Finally, both sides are seeking an agreement which will liberalize trade in services, such as insurance, aviation, leasing, construction and engineering. A successful agreement in this area would not only offer important economic benefits to the two sides but also could serve as a model and a catalyst for the inclusion of services in the new GATT round of multilateral talks. The goal will be to achieve national treatment and open market access in as many service sectors as possible. Defining these principles in particular contexts, however, will be a challenge. A larger challenge will be persuading independent regulatory agencies and/or political subdivisions to alter their own regulations and practices to conform to the terms of the agreement.

### III. PROBLEMS

We now come to the difficult questions of the relation of any

bilateral agreement to multilateral, domestic, and state/provincial law. The way these questions are answered will largely determine the balance between autonomy and integration implicit in the agreement.

Both the United States and Canada are committed to negotiating an agreement which is fully in accordance with the letter and spirit of internationally agreed rules of trade embodied in the GATT. The GATT generally requires nations to abide by the most-favored-nation principle *if* they enter into a customs union or free trade area which removes tariffs and quantitative restrictions on "substantially all" trade between the joining parties. The removal of barriers need not happen all at once — it may be staged in over a period of years, as in the U.S.-Israel FTA — but substantially all trade must eventually be covered.

To date, GATT practice offers no clear guidance as to the content of the "substantially all" requirement. On one extreme, the European Economic Community recently tried to claim that its citrus preferences for certain Mediterranean countries could be rationalized by labeling the arrangement a "free trade area." We rejected that characterization. On the other hand, the U.S.-Israel FTA, which provided for the reduction of tariffs on all traded goods by 1995, and which preserved an express option of quantitative restrictions only on small volumes of traded agricultural products, clearly qualified as a free trade area under the "substantially all" criterion. Between these extremes there is a gray area over which legal scholars could haggle. No proposed free trade area has ever been rejected by the contracting parties of the GATT for failure to meet the "substantially all" test; but neither the United States nor Canada have any interest in undermining this already weakened standard. The two sides will seek a comprehensive agreement as a legal necessity, as well as an economic desideratum.

A more difficult issue is the relation of a U.S.-Canadian agreement to U.S. domestic law. It is a truism of U.S. law that only the U.S. Constitution has the legal capacity to invalidate subsequent legislation. No treaty or executive agreement with Canada can strip Congress of the legal authority to pass inconsistent subsequent legislation.

However, as a political matter, Congress is understandably reluctant in principle to pass legislation which could violate an international commitment. The fact that any agreement would probably trigger a Canadian right of compensation or retaliation

could only add to this reluctance. This is the sense, and the only sense, in which the existence of an FTA might insulate Canada from future so-called "protectionist" legislation. It is, however, by no means insignificant.

What about the relation of the FTA to existing U.S. law, particularly in the area of trade remedies? Once again, the provisions of the U.S.-Israel FTA provide a useful reference point. In the U.S.-Israel negotiations, Israel argued long and hard for a bilateral mechanism to review U.S. application of countervailing and antidumping laws. Israel sought similar bilateral review for United States use of Section 301 of the Trade Act of 1974, which authorizes consultation and/or retaliation against practices which the President finds to be discriminatory, unjustifiable, or unreasonable. Israel also asked for a partial exclusion of Israeli products from Section 201, which provides relief against surges of imports that are found to have caused substantial injury to U.S. firms. Under the Israeli proposal, the President would be barred from including Israel in general relief from such injurious imports unless first determining that Israeli imports, *in and of themselves*, were a cause of substantial injury to U.S. products.

Despite the small size of Israel and the correspondingly diminished threat of Israeli exports to U.S. commercial interests, Congress responded to these particular requests with a categorical "no". Section 406 of the Trade and Tariff Act of 1984, passed while the negotiations with Israel were in full swing, provided that "no trade agreement with Israel . . . may affect in any manner or to any extent the application to any Israeli articles . . . of any provision of law under which relief from injury caused by import competition or by unfair trade practices may be sought." Moreover, U.S. negotiators in each instance insisted on terminology which preserves the full range of the President's discretion in each case, rather than on terminology which binds the President by agreement to exercise discretion in a certain way. Frankly, I would be surprised if the two sides were able to agree on a binding bilateral mechanism to review either party's application of its trade remedy laws.

#### IV. SOLUTIONS

This conclusion has important implications for the choice of a dispute settlement process. Obviously, a dispute mechanism cannot be binding and address itself to a party's trade remedy laws without effectively displacing those laws to a significant

extent. From the U.S. point of view, U.S. trade remedy law — particularly the countervailing duty and antidumping laws — applies internationally-agreed standards of conduct through fair and objective hearing procedures. Importers' interests already are adequately protected. Congress will not accept a bilateral dispute settlement mechanism with authority to review an application of our countervailing duty and antidumping laws. On the other hand, it is equally clear that some sort of joint committee is necessary and proper to supervise implementation of the agreement. Some sort of dispute settlement mechanism is needed to resolve differences of opinion between the two sides as to how the agreement should be interpreted, and/or to resolve claims by one side that actions of the other (though perhaps technically legal) have undermined fundamental objectives of the agreement. In this mode, formal mechanism for notice, consultation and resolution of disputes could do a valuable service for both sides.

One of the most interesting and difficult issues in the talks will certainly be how to handle the federal character of both nations. The issue arises particularly in the areas of services, sale of alcoholic beverages, and government procurement because states and/or provinces have traditionally wielded considerable regulatory authority (and autonomy) in these areas.

In Canada, the issue of provincial authority has a "constitutional" dimension, if you will, which is absent from the U.S. scene. The U.S. Congress, unlike the Canadian Parliament, has full legal authority to adopt agreements and pass laws which displace state laws in areas of traditional state function.

This legal distinction, however, misses the fundamental point. As a practical and political matter, it is unthinkable that either side would enter into an agreement binding on the states or provinces in these areas without the full consent and cooperation of those states or provinces. Getting that consent and cooperation is going to require a great deal of sensitivity, a great deal of consultation and a great deal of domestic diplomacy on both sides. In each case the object will be to find ways that states or provinces can preserve their autonomy, their individuality, and their fundamental regulatory objectives, without discriminating against or unnecessarily burdening foreign participants.

This is much easier said than done. Regarding services, for example, how does one distinguish between a valid health and safety or commercial purpose and a discriminatory regulation,



considering that standards in this area are often necessarily subjective and that the thing being measured or evaluated is invisible?

In the end, it may turn out that the best we can hope for is some sort of "best efforts" pledge with regard to states, similar to the kind we achieved in the U.S.-Israel Declaration on Trade in Services. Nonetheless, we are committed at this stage to seeking something more in the U.S.-Canada context, and we are encouraged by the forthcoming responses of the state representatives we have consulted with thus far. If the provinces turn out to be equally forthcoming on the Canadian side, I think we can anticipate an agreement, even in these particularly difficult areas, which will be of considerable benefit to both sides.

