Government of Canada Gouvernement du Canada

This paper replies to questions set out in the Federation of Canadian Municipalities' document *Municipal Questions Respecting Trade Agreements*, as well as replies to subsequent draft resolutions to be debated by the Board of Directors. This response was submitted to the FCM on April 11th, 2002.

This document is also pursuant to the discussions of the joint Federation of Canadian Municipalities (FCM) - Department of Foreign Affairs and International Trade (DFAIT) working group on international trade. The joint working group was struck at the request of the FCM and as of April 2002 had met on three occasions - in Ottawa on December 19, 2001, in Vancouver on January 18, 2002, and again in Ottawa on February 8, 2002 - to discuss, in detail, the questions raised in the above noted document. Officials from the Department of Finance and Industry Canada also participated in the working group.

Table of contents

OVERVIEW

The FCM's questions were of four types. First, there were questions regarding the nature of Canada's existing trade agreements and obligations, and the extent to which these obligations have impacts upon municipal governments. It is our understanding, from reports of the working group discussions and the comments made by FCM representatives before the Parliamentary Standing Committee on Foreign Affairs and International Trade, that these discussions were successful in addressing the majority of the members' concerns.

The second group of questions related to Canada's position on possible future trade agreements, which might result from the on-going Free Trade Area of the Americas (FTAA) negotiations and the new round of World Trade Organization (WTO) negotiations on a broad range of issues, including: (a) services, (b) investment, (c) subsidies, and (d) government procurement. In respect to those questions, the intent of our discussions was to clarify what position - if any - Canada has taken in the negotiations and to consult the FCM on Canada's future positions. It is our hope that the FCM will remain actively engaged in consultations on trade negotiations and that

the working group will become a permanent consultative committee.

A third group of questions posed more difficulty for the DFAIT side on the working group. These questions related to Constitutional arrangements and the division of jurisdictional authority for trade agreements, on the one hand, and for provincial and municipal powers, on the other hand. It was agreed by the working group that these questions were beyond the competence of DFAIT officials and would have to be pursued, as required, with other authorities.

Finally, there were a few questions that the working group agreed to set aside, as their focus and intent were not clear. The FCM may wish to re-frame some of these questions based on the clarifications provided in our discussions.

There were, in addition to the questions posed in the FCM document, a number of specific issues raised by draft resolutions on which you have sought a written response.

The first of these sought an assurance from the federal government that it would refuse to participate in any WTO negotiations that might "undermine the public nature of health care, education, social services and government procurement". We believe that the Government has, in fact, already given that assurance, in its *Initial Canadian Negotiating Position*, submitted in the WTO in the context of the GATS negotiations and available on the department's web site for *Trade Negotiations and Agreements*. In particular, Canada's position states that:

> "The GATS cannot be interpreted as requiring governments to privatize or to deregulate any services. We recognize the right of individual countries to maintain public services in sectors of their choice: this is not a matter for the GATS negotiations."

In addition, Canada sets out among its objectives for the negotiations:

> "To preserve the ability of Canada and Canadians to maintain or establish regulations, subsidies, administrative practices or other measures in sectors such as health, public education, and social services."

We recognize the concerns raised by some observers that the exclusion in the GATS for "services supplied in the exercise of governmental authority" does not offer an unconditional exemption for public services in every possible circumstance or by any definition. However, Canada has taken no commitments - and will take no commitments - in respect of social services, public education or health services. Therefore, these services are protected, whatever the scope of the exclusion.

Regarding the question of government procurement, the notes below present the Canadian Government's position, which, in summary, is not to accept procurement commitments at the municipal level.

The second additional issue you raised was with respect to the ongoing efforts to clarify the provisions of the investment chapter of the NAFTA (Chapter 11). In particular, you asked that we ensure that:

> "... the promised review of NAFTA Chapter 11 takes place, with the objective of narrowing the investment protections and ensuring that expropriation is defined to mean the explicit taking of property and does not also include incidental interference with the use of property which may deprive an owner of economic benefit;"

and that

> "... future NAFTA dispute tribunals confine themselves to ruling on whether the parties have complied with international law, and that it be explicitly reinforced that unless given specific authority, these tribunals cannot overrule the decisions of domestic courts or act as if they were an appellate body from domestic courts."

With regard to the first point, discussions with our NAFTA partners on further clarifications to Chapter 11 are continuing. Indeed, as was noted in the statement by NAFTA Ministers last July, on the occasion of the first such clarifications, this is viewed as an ongoing process.

As discussed with the FCM Working Group, the scope of the expropriation discipline is one of the possible issues for discussion with our NAFTA partners. The Government of Canada is on the public record opposing the views of some NAFTA litigants and certain tribunals with respect to excessively broad definitions of the scope of expropriation intended in the agreement. It is important to note, however, that no Tribunal award has, in fact, established a definition of expropriation with which Canada disagrees. In two cases, tribunals have agreed with Canada that the language of the NAFTA (i.e. the use of the phrase " ... measures tantamount to ... expropriation ... ") does not create a new or wider concept of expropriation.

This is not to say that Canada does not agree that indirect expropriation should be compensated in certain circumstances. Such compensation can be compensable in Canadian courts, under Canadian law, and the general intent of investment agreements is to ensure comparable treatment for Canadian investors in other countries. Ultimately, it is only on a case-by-case basis, with a specific fact situation, that appropriate judgements can be made about what compensation is warranted by a government measure that expropriates a business.

The deeper question, of course, is what constitutes a “taking” for the purposes of the expropriation provisions of Chapter 11. Obviously, all NAFTA governments believe that the right to regulate in the public interest must be preserved and, therefore, that appropriate guidance should be given to tribunals to ensure that the exercise of legitimate regulatory authority is unfettered by investment protection commitments. We believe we can give you the assurance of the Government of Canada that we share the same objectives in this regard. It is important to remember, however, what the expropriation provisions of Chapter 11 seek to prevent - expropriations that are not for a public purpose; that are discriminatory; that are not in accordance with due process; and for which compensation, has not been paid. Canada does not intend to retreat from these undertakings.

Regarding the second point, NAFTA tribunals only have authority to interpret the NAFTA. They cannot overrule domestic law nor act as an appeal process for domestic law. Indeed, the reverse is true: in certain circumstances, domestic laws can be used to review the decisions of NAFTA tribunals, as witnessed by Canada’s referral of a NAFTA Tribunal’s award to domestic courts for judicial review. NAFTA tribunals can, however, make determinations on whether Canada - including all levels of government and bodies acting under delegated authority of from governments - have met the obligations of the NAFTA.

Finally, you have asked whether the Government of Canada would provide “ ... written confirmation that ... (it) would not sue or otherwise claim compensation from, and will indemnify and save harmless under international law, any municipality whose actions or decisions result in an international trade tribunal decision that goes against the Government of Canada, so long as the municipality’s conduct would have been valid under domestic law”.

This request approaches trade agreements from the wrong direction. Surely our objective should be to agree on what obligations Canada should take in trade negotiations and a shared undertaking to respect those obligations. Federal and municipal governments ultimately seek the same result - economic opportunities for Canadians, consistent with the protection of Canadian values (such as the protection of the environment, the promotion of cultural diversity or the maintenance of social safety net programs). We both seek investment in Canadian communities by foreign investors and the protection of Canadian investors in other countries. Our goal, then, should be to collaborate in the development of Canada’s positions in trade negotiations and to share a commitment to the resulting agreements. That is certainly the intent of the consultations the Minister has invited the FCM to participate in with respect to future trade negotiations.

Your request seeks licence from Canada not to respect international obligations - obligations with which the Working Group has found little concern, in relation to the current practices of Canadian municipalities. The fact is that Canadian

municipalities do not seek to discriminate on the basis of nationality; they do not regulate without a public purpose; they do not make arbitrary decisions without due process; and they do provide compensation, where warranted, for the taking of property for public use. Indeed, future discussions of the Working Group will need to focus on what specific behaviours Canadian municipalities wish to protect that are contrary to any trade obligation.

It should be noted, here, that trade agreements do not instruct national governments on how to enforce trade obligations domestically. In most circumstances, enforcement of trade agreements takes the form of the withdrawal of trade concessions by other countries. And, as your question implies, in the case of financial awards under investment agreements, it is the Government of Canada that is liable. The circumstances in which Canada would seek compensation from provincial or municipal governments in respect of such a ruling are not obvious. Certainly, there have been no circumstances to date - with over a decade of experience with such investment agreements - in which compensation from another level of government has been contemplated. This having been said, we do not believe that federal governments, both present and future, should waive their rights in respect of all possible circumstances in the future. Indeed, we believe there is a principle of law that rights cannot be waived where the implications of future events cannot be known.

What remains is to address the questions in your document *Municipal Questions Respecting Trade Agreements*. As was agreed for the Working Group discussions, the questions have not been treated in serial fashion. Instead, we have provided descriptive pieces on each issue (services, investment, subsidies and government procurement) in which we address the questions in context. The footnotes will, nevertheless, direct the reader to the specific FCM questions to which the text refers. These texts are attached.

We trust that you will find this information useful and we look forward to continuing the work of the joint working group, both to address any outstanding questions your members may have regarding Canada's existing trade agreements and to shape our positions in future trade negotiations.

TRADE IN SERVICES

This section responds to both specific questions and general issues and concerns raised by the FCM during the ongoing consultative process that has been established between the FCM and the Government of Canada. To date, the principal focus of these discussions relating to services trade has been on the General Agreement on Trade in Services (GATS). It is understood that the FTAA negotiations are still in a preliminary phase. [1]

- The GATS is the first multilateral agreement covering trade in services. It is part of the World Trade Organization (WTO) which now includes 144 members making decisions on a consensual basis. The agreement was negotiated during the Uruguay Round, and came into force in 1995. The GATS provides a framework of rules governing services trade. It is designed to allow countries to make commitments to liberalize trade in services in the areas they select and at the pace they wish to liberalise.

- The **objectives** of the GATS are to:

  a) provide a rules-based system to facilitate international trade in services;
  b) ensure fairness of treatment between service providers when they access foreign markets;
  c) offer predictability in treatment and transparent rules for service providers.

<u>The Scope of the Agreement (and its impact on municipalities)</u>

- The GATS deals with **measures** affecting trade in **services**. "Measures" include laws, regulations, rules, decisions, administrative actions taken by governments at all levels -- national, regional and local.[2]

- Measures relating to many services <u>provided by</u> municipalities are excluded from the GATS. The GATS excludes "services supplied in the exercise of governmental authority." These are services that are provided either by public or private entities and that meet the following two criteria: they are supplied neither on a commercial basis, nor in competition with one or more service suppliers. This exclusion covers many services provided directly by municipal governments,

---

[1] This is relevant to the document *Municipal Questions - Respecting Trade Agreements* published by the Federation of Canadian Municipalities specifically questions A.1a; A.1.b; A.1.d; A.2.b; A.2.c; A.4.c; A.4.d; B.2.b; B.5.c. From now on, footnotes indicate relevant questions from the same document that are addressed by a given paragraph.

[2] Question B.1.

such as library services or water distribution services. It is important to note that the GATS does not attempt to define the notion of "public services", as this is for each country to decide in the context of its own domestic environment.[3]

- In cases where municipal governments contract out certain activities through government procurement (for example, the treatment and distribution of drinkable water on contract for a municipality), GATS Article XIII states that obligations on most-favoured nation treatment, national treatment and market access do not apply to measures governing government procurement. GATS Article XIII applies in respect of the procurement by governmental agencies of services purchased for governmental purposes and not with a view to commercial resale or with a view to use in the supply of services for commercial sale. [4]

- It should also be noted that nothing in the GATS prevents the adoption of measures necessary to protect public morals, to protect human, animal or plant life or health, or to maintain public order.

<u>The key obligations found in the GATS</u>:

- The GATS contains four key obligations: **Most-Favoured Nation Treatment**, **Transparency**, **Market Access** and **National Treatment**.

- The **Most-Favoured Nation Treatment** obligation is a general principle of trade policy by which we treat any foreigner at least as well as the one we treat the best (whether or not we discriminate between domestic and foreign firms). This obligation applies to all measures affecting trade in services (excluding "services supplied in the exercise of governmental authority" and measures governing procurement by governments). Canadian measures generally respect this principle at all levels of government.

- The GATS also includes rules to ensure **transparency** and objectiveness of rules. These obligations require publishing of rules of "general application", notification of new or amended measures "significantly affecting trade in services", and procedure for exchange of information. The majority of these obligations apply to all measures affecting trade in services (excluding "services supplied in the exercise of governmental authority"). [5]

---

[3] Questions A.1.d'; A.2.b; B.1.a; B.2; B.3; B.5; B.6.

[4] Questions A.1.d; A.1.d'; A.2.b; B.4; B.5.a; B.6; C.1; C.1.a; C.1.b; C.1.c; C.2.

[5] Questions C.1.b; E.

- These rules on transparency are very important for Canadian service providers abroad, as many countries do not publish or make readily available information regarding their laws and regulations, as we do in Canada. In Canada, publication and notification of changes in regulations and by-laws are already common practice. Canadian municipalities already fulfill these transparency requirements, and usually go beyond them.[6]

- The **National Treatment** obligation requires that foreign businesses be treated at least as well as similar domestic businesses. This obligation applies only in sectors where specific liberalization commitments have been undertaken (and does not apply to measures affecting "services supplied in the exercise of governmental authority" and measures governing procurement by governments).[7]

- The **Market Access** obligation prohibits WTO Members from imposing certain types of quantitative restrictions meant as limitations to access a market. Once again, this obligation applies only in sectors where specific liberalization commitments have been undertaken (and does not apply to measures affecting "services supplied in the exercise of governmental authority" and measures governing procurement by governments). This obligation is not a limitation as such on the ability of local governments to adopt regulatory measures of general application such as zoning by-laws.[8]

- As noted above, the market access and national treatment obligations apply only in sectors where a country has undertaken specific liberalisation commitments. In reading Canada's GATS schedules of commitments, one could see the extent of obligations undertaken by Canada. The number of sectors where Canada undertook commitments reflects the fact that Canada is one of the most open services economy in the world. At the same time, Canada has maintained some measures that are not consistent with market access and national treatment obligations of the GATS, and which are reflected in our schedules of commitments.[9] The following examples provide an illustration of how these "commitments" work:

    - Canada has made commitments for "snow removal services". This

---

[6] Ibid.

[7] Questions A.2

[8] Question A.1.c.

[9] Questions A.1.b; C.2. For more details on Canada's schedule of commitments under the GATS, please consult the following web page: http://strategis.ic.gc.ca/SSG/sk00039e.html.

reflects the fact that Canada does not impose, for example, restrictions on the number of service providers that may offer these services in Canada, nor does it discriminate on the basis of nationality. Concretely, these commitments deal with business-to-business or business-to-individual activities (e.g., a snow removal business providing its services to customers like car dealers or homeowners). Business-to-government activities would generally take place as part of a government procurement arrangement, and would therefore not be subject to GATS obligations on market access and national treatment.[10]

- Canada has made commitments on "real estate services", but inscribed the non-conforming measures that Canada wishes to maintain (for example, in most provinces, real estate agents must maintain a local presence). This means that, by maintaining such a requirement, Canada is not in breach of its GATS obligations.

- As mentioned above, the obligations on most-favoured nation, national treatment, and market access do not apply to measures governing the procurement by governmental agencies of services purchased for governmental purposes and not with a view to commercial resale or with a view to use in the supply of services for commercial sale. In the case of snow removal for instance, market access obligations do not extend to the contracts awarded by municipalities for the removal of snow on, for example, public roads. Regulations regarding contracting of such services by governments are not subject to these market access obligations. In addition, The GATS does not prevent a municipality from returning to direct provision of a service (such as garbage collection) after a opting for contracting out arrangement. [11]

"Domestic regulation" and the GATS

- Some have expressed concerns that the GATS may impede the legitimate right of governments to regulate even if these governments regulate in manner consistent with market access and national treatment obligations. That perception is often based on a narrow interpretation of GATS Article VI:4 concerning "domestic regulation".

- This article sets out a work program to develop disciplines within the GATS to ensure that commitments on national treatment and market access are not "nullified" by other regulatory measures. This work program (and GATS Article VI:5 which provides for interim disciplines that apply only to sectors where

---

[10] Questions A.1.d; C.2.

[11] Question A.1.d; C.1.a, C.1.b, C.1.c, C.2.

specific commitments have been made) does not impinge on a government's ability to regulate in pursuance of national policy objectives, nor does it submit to WTO review national regulations.

- This work program is limited to measures relating to qualifications requirements and procedures, technical standards and licensing requirements and procedures. For example, we do not see zoning bylaws, as defined under Canadian law, as measures covered by article VI:4.

- The discussions on the development of potential disciplines on domestic regulation remain at an early stage. Most countries consider that any such disciplines should apply only in sectors where specific commitments have been undertaken (i.e., these disciplines would not apply in all sectors).[12]

The GATS does not prevent governments, federal, provincial/territorial or municipal, from regulating. This "right to regulate" is recognized in the preamble of the GATS and was reaffirmed in the Declaration adopted at the WTO Ministerial meeting held in Doha, Qatar in November, 2001.

The GATS has been in effect since 1995 and governments at all levels have continued to be able to regulate to promote and protect the interests of their citizens. This will remain the case in the future.

[12]Question A.4.c.

INVESTMENT TRADE POLICY

This section responds to specific questions and general issues, regarding investment trade policy, that have been raised by the Federation of Canadian Municipalities (FCM) during the ongoing consultative process established between the FCM and the Government of Canada. Please note that the following document is not intended to provide legal advice.

Canada's Position on Investment Rules

- As an open and dynamic economy with significant international trade and investment flows, Canada has consistently supported a strong rules-based system, multilaterally, regionally and bilaterally. We believe that investment rules can play an important part in providing a stable, transparent and predictable environment for international investment.

- Canada has a vested interest in keeping the flow of trade and investment strong. The value of Canadian direct investment abroad has increased by 400 percent between 1985 and 2000, from $57 billion to $301 billion. In addition, in 2000 we benefited from over $291 billion in foreign direct investment in Canada. This, in turn, generates Canadian jobs and fosters growth of Canada's Gross Domestic Product.

The Current Rules

- Canada currently benefits from high-standard investment rules in the North American Free Trade Agreement (NAFTA), Canada-Chile Free Trade Agreement (CCFTA) as well as the twenty-one bilateral Foreign Investment Protection Agreements (FIPAs) to which it is a Party[13]. These agreements include obligations with respect to non-discriminatory treatment, minimum standard of treatment, performance requirements, transparency, free transfers, compensation for expropriation as well as investor-state and state-to-state dispute settlement.

- Investment agreements provide protection through a rules-based system to Canadian and foreign investors in order to promote investment. Such rules as those contained in NAFTA Chapter 11 and numerous FIPAs apply to measures taken by Governments that relate to investors and their investments.

- International investment agreements are international treaties which are interpreted in accordance with international law. In particular, widely recognized rules of

---

[13] Approximately 63 per cent of Canadian direct investment abroad and 72 per cent of FDI in Canada are currently covered by these "NAFTA-type" investment rules. Information on individual FIPA Agreements can be found at: http://www.dfait-maeci.gc.ca/tna-nac/fipa-e.asp .

international law specify that treaties are to be interpreted in light of the ordinary meaning of the words being used and the context in which they are being used. The object and purpose of the treaty is also relevant. Each party to an international agreement has a general duty to ensure the consistency of its laws with its international obligations under that agreement. Treaties thus contain provisions to which all parties have agreed and which represent commitments that all parties have undertaken to respect.[14]

- Investment agreements typically provide investors and their investments with protection against discrimination on the basis of nationality and prevent the imposition by governments of a number of trade-distorting requirements, subject to certain exceptions[15]. These rules also ensure that investments are not treated in a manner inconsistent with the basic requirements of customary international law (e.g., due process), that they are not expropriated without compensation, and that they are able to transfer funds abroad.

- International rules on investment complement other trade rules, as trade in general and international investment are two sides of the same coin. Indeed, to be able to export their goods and services, Canadians often need to establish a presence in foreign markets. Discriminatory barriers against Canadian investments abroad can translate into restrictions on Canadian exports.

- The obligations under the NAFTA are assumed by the governments of Canada, the U.S. and Mexico. In Canada, the federal government would be respondent in any dispute arising from alleged breaches of the Agreement, and would work closely with the relevant provincial, territorial or municipal officials.

- Investment rules have not jeopardized our economic and social values. Foreign investors and their investments in Canada are subject to the same laws and regulations as are Canadian investors and their investments, including the laws aimed at protecting the environment and those ensuring high labour, health, building and safety standards.

- Chapter 11 does not prevent municipal governments from conducting their normal activities. These activities must simply be conducted in a manner that is consistent with the relevant international obligations such as the obligation not to discriminate based on nationality.

---

[14] Reference: question A.1(b).

[15] There are exceptions permitted to certain obligations. In addition, the NAFTA specifies that non-conforming measures of municipalities that existed prior to the January 1, 1994 have been grand-fathered (Article 1108(1)(a)(iii) of the NAFTA). Canada has also maintained restrictions on foreign investment in certain sensitive sectors such as culture and social services. - Reference: question C(a).

Expropriation

- A common feature of investment agreements, including Chapter 11 of the NAFTA, is protection against direct or indirect expropriation without compensation at fair market value. These are concepts well known in international law.

- In Canada there is federal law and a variety of provincial laws governing expropriation. Hence, it is difficult to make a comprehensive comparison between international law standards of direct and indirect expropriation and those contained in Canadian law. Under international law, however, expropriation generally involves the taking of property from an investor or a degree of interference with an investment's operations sufficiently restrictive to support a conclusion that the investment has been taken from the investor.[16]

- It is important to note that a mere diminution of profits does not constitute a breach of the expropriation obligation under Article 1110 of the NAFTA .[17]

- The only NAFTA Chapter 11 Award to date on compensation for expropriation was the *Metalclad Award*[18]. This Award was based entirely on Metalclad's sunk cost (i.e. land value plus investment in infrastructure). It should also be noted that neither the Tribunal Award nor the B.C. Supreme Court statutory review in *Metalclad v. Mexico* held that NAFTA restricts the right of a local government to regulate on environmental and public health grounds.

- In the final Award on *Metalclad*, the Tribunal found that changes to the rules by the state government, by way of issuance of an *Ecological Decree*, after Metalclad had been led to believe that it had all necessary authorisations and had invested a substantial amount in its operation, were tantamount to expropriation. This decision was not over-ruled by the B.C. Supreme Court. This is not the same as denying the right of governments to regulate - NAFTA Chapter 11 does not restrict any level of government from legitimately legislating and regulating in the public interest.

- In the only other rulings on this issue, investor-state tribunals rejected allegations that Canada breached its obligations with respect to expropriation in the *Pope and Talbot* and *S.D. Myers* cases and that Mexico breached its obligations in the *Azinian* case.

- In defining the term "expropriation", NAFTA Chapter 11 Tribunals have generally held that expropriation requires more than merely a deprivation of an investor's

---

[16]Reference: question A.2(a) and (e).
[17]Reference: question A.2(b).
[18]For information on the Award: http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-e.asp#11.

property by the state. In *Pope & Talbot*, the tribunal held that expropriation requires a "substantial deprivation" that would justify an inference that the owner will not be able to use, enjoy or dispose of property.[19] In *S.D. Myers*, the tribunal found that an expropriation usually amounts to a lasting removal of the ability of an owner to make use of its economic rights although it may be that, in some circumstances, it would be appropriate to view a deprivation as amounting to an expropriation, even if it were partial or temporary.[20]

- Compensation for expropriation under NAFTA Chapter 11 must be at "fair market value". Compensation is equivalent to the "fair market value" of the expropriated investment immediately before the expropriation took place and does not reflect any change in value occurring because the intended expropriation had become known earlier.

- Valuation criteria include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.[21]

Minimum Standard of Treatment

- NAFTA Chapter 11 includes in Article 1105 (1) a minimum standard of treatment afforded to investment. Specifically, this provision states that "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security." This is a standard of protection below which the NAFTA Parties have undertaken not to go.

- On July 31, 2001, the NAFTA Free Trade Commission, which is comprised of the NAFTA Trade Ministers, issued a binding interpretation of this provision. This binding interpretation reaffirmed that the standard of treatment set out in Article 1105 reflects customary international law concerning the treatment of foreigners, or aliens. It confirmed that a purported breach of another NAFTA Article or indeed a provision from another treaty cannot constitute a breach of Article 1105. The binding interpretation also confirmed that "fair and equitable treatment" and "full protection and security" do not create additional obligations beyond those required

---

[19] *Pope & Talbot*, Interim Award by Arbitral Tribunal (June 26, 2000), at para. 102. Copy available at: http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-e.asp#11

[20] 102; *S.D. Myers*, Partial Award (November 13, 2000), at paras. 282-283. Copy available at: http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-e.asp#11

[21] Reference: question A.2(c)

by the customary international law described above. The issuance of this binding interpretation has thus contributed to a proper understanding of Article 1105.[22]

Investor-State Arbitrations

- Under NAFTA Chapter 11, an investor may submit a claim to Arbitration only after 6 months have elapsed since the events giving rise to a claim. In addition, an investor may not make a claim if more than three years have elapsed from the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the investor incurred loss or damage. In order for there to be a breach of Chapter 11, the measure in question must be found to contravene a specific obligation under Chapter 11. It is important to note that there can be no order to remove the measure in question. The sole result of a breach is monetary compensation or possibly restitution.[23]

- Investor-state arbitrations are heard by tribunals of three adjudicators - one arbitrator is named by each party to the dispute and the third by mutual agreement or, failing agreement, by the World Bank International Centre for Settlement of Investment Disputes (ICSID).
- Tribunal awards are based on monetary damages - a Chapter 11 Tribunal may not order a party to pay punitive damages. In addition, a Tribunal does not specify how a Party is to ensure compliance with an award. This is a matter for the Party to resolve internally.

- When deciding issues of dispute under NAFTA Chapter 11, a Tribunal must adhere to the specific provisions of the Agreement; the applicable rules of international law; and any interpretation issued by the NAFTA Free Trade Commission of a provision of the Agreement.

- The jurisdiction of a NAFTA Chapter 11 Tribunal is defined and confined in the Agreement. A NAFTA Tribunal is not an appellate body and has no jurisdiction to reverse a decision of a domestic court. A Tribunal established under the NAFTA is confined to ruling exclusively on breaches of the Agreement's provisions covered by Chapter 11.[24]

- Under Canada's *Commercial Arbitration Act*, decisions of NAFTA Chapter 11 Tribunals are subject to review before domestic courts on specific grounds. In reviewing a Tribunal's decision, the domestic court can set aside a Tribunal's award in whole or in part or it can refer it back to the Tribunal for reconsideration.

---

[22]Reference: question A.3(a).
[23]Reference: question A.2(d)and C(b)
[24]Reference: question C(b).

Transparency

- Canada is working closely with its NAFTA partners to make the investor-state dispute settlement process, including arbitral hearings, as open and transparent as possible. The Department of Foreign Affairs and International Trade web site contains publicly available documents related to Chapter 11 arbitrations involving the Government of Canada.[25] Canada also actively advocates that NAFTA Chapter 11 arbitral hearings be open to the public.[26]

- On July 31, 2001, the NAFTA Free Trade Commission reaffirmed that, subject to certain limits, each NAFTA Party will make available to the public all documents submitted to, or issued by, Chapter 11 Tribunals. NAFTA Governments may also share all relevant Chapter 11 documents, including confidential information, with their respective federal, state and provincial officials. It is important to note that, in any dispute arising from alleged breaches of NAFTA Chapter 11 the federal government would work closely with the relevant provincial, territorial or municipal officials.[27]

Clarification Process:

- The NAFTA text was built on a longstanding experience and institutional knowledge of international trade and investment law. In order to ensure that it is understood and used in its proper context the NAFTA Parties are fully engaged in an in-depth review of the NAFTA Chapter 11 provisions and have intensified trilateral work to clarify key procedural and substantive provisions of Chapter 11 and increase the transparency of the arbitral process. In July 2001, the NAFTA Free Trade Commission issued their first Notes of Interpretation[28] (details of which are covered in the *Minimum Standard of Treatment* and the Transparency sections above)[29]

- Trade experts of the NAFTA parties have been directed to continue their work examining the implementation and operation of Chapter 11.

- In addition to the ongoing work through the NAFTA Free Trade Commission, NAFTA parties continue to participate on a case-by-case basis through a provision in the NAFTA that allows non-disputing NAFTA Parties to make submissions to a Tribunal on a question of interpretation of the Agreement (Article 1128 of the NAFTA).

- It is important to emphasize that the clarification process is a reaffirmation of the proper interpretation of a specific provision. It does not change the obligations under the Agreement.[30]

Future Agreements and Investment Rules

---

[25]Web site address is: http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-e.asp .
[26]Reference: question E(b).
[27]Reference: questions E(b) and (c).
[28]A copy can be found at: http://www.dfait-maeci.gc.ca/tna-nac/NAFTA-Interpr-e.asp .
[29]Reference: question A.1(b), A.(2)(a)-(e), A(3)(b), B, C and D.
[30]Reference: questions A.2(e) and A.3(a).

- In the development of rules on investment in the Free Trade Area of the Americas (FTAA) Canada will be guided by the government's extensive consultations and our experience in the NAFTA, including our analysis of specific obligations for clarification. As with the NAFTA, Canada will develop exceptions to certain investment obligations, in addition to restrictions placed on foreign investment in certain sensitive sectors such as culture, environment, education, health and social services.[31] We must aim to balance the protection investment rules provide to Canadian foreign business investments with the transparency and obligations needed to attract investment to our communities while ensuring that Canada's social and economic values are not compromised.[32]

- The FTAA negotiations are still in their nascency with much work still to be done. To date, the only proposal that Canada has submitted is on the language for *Minimum Standard of Treatment* which reflects the clarification issued by the Free Trade Commission in the NAFTA Chapter 11 clarification process.[33] Updates on the negotiations and Canada's position can be obtained through the Department of Foreign Affairs and International Trade's website.[34]

- An issue of particular interest is Canada's position on dispute settlement in the FTAA. Canada supports the establishment of a state-to-state dispute settlement mechanism for the whole agreement that would provide for adjudication of disputes arising from investment obligations in a fair, transparent and effective manner.

- With regard to an investor-state dispute settlement mechanism provision, which would provide for investors of countries within the free trade area the right to seek arbitration of disputes arising from alleged breaches of obligations in the investment chapter, Canada is not advocating the replication of the NAFTA investor-state dispute settlement mechanism in the FTAA. Nor has Canada supported the proposals made so far by other countries to include such a type of dispute settlement mechanism in the FTAA.[35]

- Canada supports the inclusion of investment negotiations in the World Trade Organization (WTO), as a means to provide greater predictability and security for Canadian investors abroad. At the WTO Doha Ministerial in November 2001, WTO Members recognized the case for a multilateral framework on investment and agreed to a focussed work program in the Working Group on Trade and Investment on elements of a possible framework. A decision to proceed with multilateral investment negotiations will be taken at the next Ministerial, to be held in Mexico in 2003, on the basis of a consensus regarding how negotiations will proceed[36]

---

[31]Reference: question C(a).

[32]Reference: questions A(1)(b), A.(2)(a)-(e), A(3)(b), B, C and D.

[33]Reference question: A.3(a) - Canada's proposal can be found at: http://www.dfait-maeci.gc.ca/tna-nac/inv-aug01-e.asp .

[34]Web site address for FTAA updates: http://www.dfait-maeci.gc.ca/tna-nac/I-P&P-e.asp#CP - The FTAA is referred to throughout Section II (Investment), however, questions A.1(b), A.3(b), B, C, D and E(a) are specific to the FTAA.

[35]Reference: questions D(a), (b) and (c).

[36]Reference: question A.1(a) - addition information on the WTO can be found on the Department's web site: http://www.dfait-maeci.gc.ca/tna-nac/wto-back2-e.asp .

SUBSIDIES

This section responds to both specific questions and general issues regarding subsidies that have been raised by the Federation of Canadian Municipalities (FCM) during the ongoing consultative process that has been established between the FCM and the Government of Canada.

Do municipal or provincial programs that are designed to promote exports conflict with the WTO subsidies rules (and thus the proposed FTAA rules as well)?

- Under the WTO Agreement on Subsidies and Countervailing Measures (ASCM), subsidies contingent on export performance (or on import substitution) are prohibited.

- These disciplines also apply where the granting authority is municipal. (Indeed, if it were otherwise, ASCM prohibited subsidy disciplines could be easily circumvented).

Will the federal government take action to exclude municipal subsidies from coverage under the FTAA?

- Given its federal system of government, Canada fought hard and was successful in the Uruguay Round in ensuring that subsidies by sub-national granting authorities, (e.g., provinces and municipalities) could not be automatically found "specific" and therefore subject to retaliatory countermeasures or countervailing duties. The *quid pro quo*, of course, was that sub-national subsidies would remain subject to the rules/disciplines in the ASCM, including in respect of general availability and prohibited subsidies.

- Turning to your specific question of whether the government is seeking, in the FTAA, the exclusion of municipal subsidies from WTO rules/disciplines, the short answer is No: In this regard:

    i) it would not be open to countries of the hemisphere, in the context of the FTAA, to countenance the violation of prohibited subsidy obligations owed to the broader WTO Membership, including countries outside the hemisphere.

    ii) Moreover, we would not want to encourage situations where Canadian municipalities would be pitted against the treasuries of other (wealthier U.S.) municipalities.

- While there may be some scope for deepening existing subsidy disciplines in the FTAA, Canada is of the view that such issues, by their very nature, could only be appropriately addressed in the WTO.

Will the federal government take action to include general exceptions for "green light" subsidies in the FTAA?

- For the reasons indicated earlier, fundamental ASCM framework/architecture issues such as whether the lapsed green-light category should be revived can only be appropriately addressed at the WTO-level.

Would the federal government support a proposal to re-introduce "green light" subsidies back into the WTO subsidies agreement?

- While Canada supports, in-principle, a restoration of the traffic-light framework in the WTO/ASCM, developing countries will undoubtedly try to exact a price for reinstatement of the green-light category. As such, Canada's ultimate position will have to be taken in consultation with stakeholders and having regard to the overall balance of trade-offs/concessions.

GOVERNMENT PROCUREMENT

This section responds to questions put forward by members of the Joint Working Committee between the Federation of Canadian Municipalities and the Government of Canada as they relate specifically to Canada's international trade obligations for government procurement.

Canada is currently a member of three international trade agreements which include provisions on government procurement[37]. The government procurement provisions of these three agreements do not apply to Canada's provinces or municipalities. Only purchasing by Canada's federal government is included. Canada's position in international negotiations is not to accept government procurement commitments at the municipal level [38].

NAFTA Chapter 10 commits participating governments to open an estimated $ 50 billion federal government procurement market in Canada, the U.S., and Mexico. Canadian business have the opportunity to bid on these procurements and be treated on a non-discriminatory basis.

The World Trade Organization Agreement on Government Procurement (AGP) commits Canada to open similar federal government procurement to the 28 member countries of the AGP[39]. These countries include the U.S., all the member states of the European Union, Japan, Korea, Switzerland, Norway, Iceland, Hong Kong, China, Singapore, etc.. AGP member countries are generally developed countries, although some developing countries are pursuing accession to the agreement.

The Canada-Korea Telecommunications Equipment Procurement Agreement is a bilateral agreement which builds on the WTO AGP to open federal government procurement of telecommunications equipment and related services for the Canadian federal government and Korea Telecom, Korea's government-owned telecommunications agency.

The Scope of the Agreements

All of the procurement agreements apply only to procurement specified in Annexes to each agreement. Thus, countries may tailor the procurements they include based on their own circumstances. For each country, the annexes identify:

- the specific **government organizations** that are included;
- the specific **goods, services and construction services** that are included;
- the **thresholds** or minimum dollar value of individual procurements that are included;

---

[37]Responds to III, first paragraph of header.

[38]Responds to III, first paragraph of header.

[39]Note that other members of the WTO AGP have opened procurement of sub-federal governments to each others suppliers, but, since Canada has not opened its sub-federal procurement, this access is not available to Canadian business in other WTO-AGP markets.

- specific **exceptions** or exclusions to the scope of procurements a country has included.

The key obligations of procurement agreements

The obligations of each of these agreements are substantively the same. The key elements are:

The specific procurements included in the agreements are open to each others suppliers on a ***non-discriminatory basis***.[40] This means that no buy local provisions or price premiums may be applied to those procurements which are included in the agreements.[41] Treating suppliers from other member countries as least as well as local suppliers is the fundamental means of ensuring non-discriminatory treatment. The following example provides an illustration of how this commitment works:

- For snow removal services, Canada has committed to open to bidders from NAFTA countries any contract with an estimated value above Cdn.$84,400 that federal government departments and agencies let for snow removal services. Typically, the snow removal contracts would be contracts to clear driveways for federal buildings or other roads on federal government property. Potential suppliers from any of the NAFTA countries may bid on the requirement. The department will not apply any premiums, price, or other preferences which favour a Canadian bidder when deciding which potential supplier will win the contract.

- This obligation does not in any way compromise the ability of the government department to obtain the service that it needs. The government department or agency buying the snow removal service has the right to specify its needs in precise terms, for example the frequency of clearing, the minimum response time, the gravel or other products put on the property by the contractor, etc. The government department has the right to require the contractor to comply with all laws and regulations for doing business in Canada and in the particular jurisdiction where the snow clearing activity is taking place, including all labour laws, licensing requirements, etc.

- There is nothing in government procurement obligations that would require a government department to continue to contract out the work in the future. A government department has the right to decide not to contract out and to hire its own staff to perform the service.

The members of the agreements agree to meet a standard of ***transparency*** for each of the procurements included in the agreement. This permits suppliers to obtain all the necessary information that they will need to understand how to bid on a procurement

[40]Responds to Introduction, Section IIA.3rd item and Section III, B.1.

[41]These provisions have no impact on procurement that is not included in the agreements. Buy local and other offsets may be applied to procurement not included in the agreements. For example, the federal government applies its Canadian content policy to procurement not included in the agreements.

and to understand that the transaction has been carried out on a non-discriminatory basis. The transparency obligations include:

- publication of all measures such as laws, regulations, procedures and standard contract clauses;
- publication of notices of upcoming procurement;
- minimum bid periods;
- providing bid documents to bidders with all requirements bidders must meet and other information necessary to prepare a bid; and
- publication of notices identifying the winner of each contract.

The members agree to meet a standard of ***openness in the procurement process*** for each of the procurements included in the agreement. The obligations include:

- open competition is the norm;
- procurement without competition only in specific circumstances identified in the agreements;
- technical specifications that are not an unnecessary barrier to trade;
- making the procurement decision based on bid evaluation criteria specified in advance; and
- independent mechanism for suppliers to pursue concerns about the fairness of a procurement[42].

The members agree to ***exceptions*** for national security and measures to protect human, animal or plant life or health.

[42]The agreements set out the essential characteristics of a review mechanism (e.g. independent of the procuring organization, timely, etc.). Countries then choose their own domestic mechanism or mechanisms. Canada's federal government uses the Canadian International Trade Tribunal (CITT).

Environmental procurement policies[43]

Neither the national treatment nor the technical specifications provisions of government procurement agreements "prohibit" the application to procurement of policies supporting environmental goals. Governments participating in the government procurement agreements can and do apply policies which support environmental goals through procurement. In designing a policy, a government would need to take the provisions of the agreements into consideration.

Key factors to consider in developing procurement policies that support environmental goals include:

- Has the policy goal been formally authorized by the government?
- Does the policy goal address environmental impacts within that government's jurisdiction? (e.g. prevention of harmful waste from leaching into the ground within a government's jurisdiction.)
- For the procurement affected by the policy, have all steps been taken to ensure that the technical specifications (which describe the characteristics of goods and services to be procured and/or related processes and production or operating methods) do not have the purpose or effect of creating an unnecessary obstacle to trade?
- Is the proposed policy necessary to protect human, animal or plant life or health?

Government Procurement Agreements being negotiated[44]

Canada is currently participating in negotiations on government procurement in the Free Trade Area of the Americas and in the WTO. Generally, the proposed obligations or text of the agreements are developed first before discussion takes place about what specific procurement might be included. These negotiations, all of which are at the text development stage, are described below.

Work continues on the development of a text for a government procurement chapter in the **FTAA Negotiating Group on Government Procurement**. It would be premature to say that any one of the existing government procurement agreements is likely to be a "model" for the FTAA government procurement chapter,[45] although the core obligations of an FTAA chapter on government procurement are likely to be similar to those of existing agreements.

The WTO is undertaking a review of the **Agreement on Government Procurement** mandated as part of the built-in agenda of the Uruguay Round. Work has focussed on streamlining and updating the text of the agreement.

---

[43]Responds to Introduction, Section IIA.3rd item and Section III, B.2.
[44]Responds to Section III, first paragraph of header
[45]Responds to Introduction, Section IIA.3rd item

In the WTO, the **Working Party on GATS Rules**[46] has been examining how to include government procurement in the GATS. The Working Party, which has been in place since 1996, has undertaken preliminary reviews of WTO member's procurement systems and discussed some technical issues related to including procurement in the GATS. The Working Party has not determined whether any obligations specific to procurement would be needed in the GATS.

The WTO is working on the possibility of an agreement on **Transparency in Government Procurement**. An agreement on transparency would provide for information on procurement rules and notices of individual procurements to be made available to potential suppliers. Transparency would enable suppliers to make informed decisions about participation in procurement in foreign markets. Transparency can also reduce the possibility of corruption in these markets.

At the WTO Doha Ministerial in November 2001, WTO Ministers agreed that a transparency agreement would not affect member's ability to maintain domestic preference policies. This means that a transparency agreement would not include any market access guarantees at any level of government, including municipalities[47].

Work continues on the development of an agreement, with a decision on negotiations to take place at the next WTO Ministerial meeting, likely in the latter half of 2003.

[46]Responds to Section I., B.1.

[47]Responds to Introduction, Section II, A., 3rd item; Section III, header second paragraph; and Section III, C.