

GENERAL AGREEMENT ON

RESTRICTED

Spec(91)61
12 July 1991

TARIFFS AND TRADE

Working Party on the Free-Trade Agreement
between Canada and the United States

MEETING OF 11 JUNE 1991

Chairman: H.E. Mr. D. Hawes (Australia)

Note by the Secretariat

1. The Chairman suggested that the Working Party start its second meeting by examining the outstanding questions on the information provided on the Free Trade Agreement between Canada and the United States and the replies given by the two parties to the Agreement (Spec(91)18/Add.1).

A. EXAMINATION OF OUTSTANDING QUESTIONS

I. SECTION I - GENERAL POINTS

2. The representative of the EEC noted a contradiction between the two parties to the Agreement concerning their rights and obligations with regard to third countries or each other in a dispute settlement process under the GATT (Answer I.1.4). Canada had a fairly straightforward understanding of its rights and obligations under the multilateral system whereas the United States believed that if a dispute were pursued both in the bilateral and multilateral framework, it was logical that the instances of the FTA dispute settlement mechanism double-check the results of dispute settlement proceedings under the GATT. In their response, parties had not addressed the fundamental question of what would happen if the conclusions of the FTA dispute settlement proceedings and those reached under the multilateral dispute settlement proceedings were different or even contradictory. The representative of the United States stated that the procedures followed presently by the FTA partners were consistent with their obligations under the GATT. Any question relating to a possible situation in the future could not be answered at this time.

3. The representative of Australia said that the divergence in the way in which the two parties perceived the relationship between the provisions of the FTA and GATT, including the provisions relating to dispute settlement, had also become apparent in the recent discussions on the adoption of the pork panel report in the Council. The negotiations in the Uruguay Round aimed to strengthen and to give further predictability to the dispute settlement procedures, including the procedures for adoption of panel reports. He asked the parties to comment on the relationship between the provisions of the FTA and the dispute settlement system as it would emerge

from these negotiations. The representative of Canada said that both parties to the FTA had stated their views during the discussions in the Council. His delegation also sought to strengthen the dispute settlement procedures in the Uruguay Round.

4. The representative of Japan said that dispute settlement was one aspect of the issue of the precedence of the FTA or GATT provisions. The FTA dispute settlement process affected not only the implementation of the results of multilateral dispute settlement process in GATT but also created a problem of discussion and adoption of panel reports in the Council. He recalled the answer of the United States that either party to the Agreement was free to consider how the results of FTA dispute settlement proceedings might bear upon the execution of its responsibilities under the GATT (Answer I.1.4). Bilateral procedures should not delay the consideration by the CONTRACTING PARTIES of the pork panel report. Notwithstanding the answer to which he had just referred, such obstruction of the proper functioning of the multilateral dispute settlement process was not in accordance with the responsibilities of parties under the GATT.

5. The representative of New Zealand was concerned about the implications for third countries interested in a dispute between the United States and Canada under the GATT, if a second process were allowed to impinge upon the results of the GATT dispute settlement process and possibly prevent the implementation of these results. Although both parties to the Agreement had expressed the wish to strengthen the dispute settlement procedures under the GATT, their replies on the relationship between the dispute procedures and the multilateral dispute settlement system lacked precision both in legal and procedural terms.

6. The representative of Sweden, on behalf of the Nordic countries, said that in the consideration of the relationship between the FTA and GATT, a fundamental question was the precedence of the rights and obligations under FTA or GATT. It was not clear how the parties maintained that the FTA did not affect the rights and obligations of either parties under the GATT with regard to third parties or each other (Answer I.1.4), when they also affirmed that the FTA prevailed in the event of an inconsistency between the FTA and the GATT (Answer I.1.6). The representative of Canada emphasized that the FTA prevailed between the two parties to the extent of any inconsistency between the FTA and GATT provisions, except as otherwise provided in the FTA.

7. The representative of Hong Kong noted the parties' responses to question I.1.6 that the FTA rules had precedence over GATT rules, unless otherwise specified in the FTA, thus inferring, in the event that the dispute settlement process under the bilateral and multilateral dispute settlement procedures arrived at different conclusions, the conclusion under the FTA would prevail so far as parties to the Agreement were concerned. She further noted that as there might be interested third parties in the dispute raised under the GATT, she too shared concerns expressed by other contracting parties about the implications of the precedence on such third parties.

8. The representative of the EEC said that while a dispute settlement process under GATT was usually initiated by a country which was specifically affected by a measure taken by another party, any clarification of rights and obligations under the GATT through such a process was of interest to all contracting parties. The recourse to a bilateral dispute settlement mechanism could lead to delays in the adoption of the results of the multilateral process, as recent experience had shown. There was also a danger that the results would never be adopted because of contradictory findings. This could be a matter of serious concern for all interested third parties if the application of the bilateral procedures between the two parties prevented the interpretation of the multilateral rights and obligations.

9. The representative of the United States said that contracting parties would look at the dispute settlement procedures that would be agreed in the Uruguay Round. In future, the contracting parties may also have the need to review how the process worked in other respects and, for instance, to examine the relationship between a decision by the European Court of Justice and the dispute settlement process in GATT. He emphasized that the rights and obligations of the FTA parties under the GATT remained unchanged. If any third parties felt that either party to the Agreement had failed to observe its obligations and that their action nullified or impaired its rights under GATT, it could initiate GATT dispute settlement procedures.

10. The representative of Japan recalled the parties' answer to the effect that, in the event of any inconsistency between the FTA and GATT, the FTA provisions would prevail unless otherwise specified in the FTA (Answer I.1.6) and asked whether, if a new agreement on safeguards emerging from the Uruguay Round clearly prohibited any conclusion of VRAs in future, Canada and the United States would consider VRAs to be prohibited between them even if the provisions of the FTA did not provide such prohibition.

11. The representative of Canada said that, in terms of Article 104 of the Agreement, parties affirmed their rights and obligations under multilateral and bilateral agreements as they existed at the time of entry into force of the FTA. When Canada and the United States implemented any results of the Uruguay Round they would also consider how these results would apply with respect to the FTA.

12. The representatives of Australia, EEC, Japan and New Zealand said that the replies of the two parties to the questions regarding the impact of the FTA on the rights and obligations of Canada and of the United States under the GATT with respect to third countries or each other required further clarification.

13. With respect to obligations of parties to the Agreement at the sub-federal level, the representative of Japan noted that the "specific obligations" incurred by parties in terms of Article 103 of the FTA, appeared to be more direct than the obligations of Article XXIV:12 to ensure compliance at the sub-federal level in respect of international trade matters. The representative of the EEC went on to say that, the provision in the FTA appeared to go beyond the undertakings in the Uruguay

Round on Article XXIV:12 at present. In one framework, for constitutional reasons, it was not possible for the parties to ensure respect of trade matters at sub-federal level, to the same extent as it seemed to be possible under a bilateral agreement.

14. The representative of the United States said that Article 103 did not alter the federal jurisdiction on international trade, regardless of how the wording was formulated in the two provisions. The draft text on Article XXIV:12 negotiated in the Uruguay Round provided further detailed provisions on the relationship between federal and sub-federal governments in international trade matters. The representative of the EEC asked whether the terms used in the FTA ("shall ensure that all necessary measures are taken") would also be acceptable to the two parties in the context of the negotiations on Article XXIV:12 in the Uruguay Round.

15. The representatives of Canada and the United States said that the language in the two provisions served two different purposes: Article 103 of the FTA dealt with the specific obligations related to the FTA, whereas Article XXIV:12 of GATT related to the rights and obligations of contracting parties to GATT. The difference in the formulation of the relevant provisions in the FTA would not in any way alter the obligation of parties to the Agreement under the GATT in this respect.

16. The representative of New Zealand said that the provisions of Article XXIV:8(b) did not give an open-ended permission to maintain quantitative restrictions, and asked how the parties to the Agreement had reached the judgement that their use of the exceptions under Article XI was "necessary", given their obligation to eliminate duties and other restrictive regulations of commerce on substantially all trade. The representative of Canada said that they had considered it "necessary" to maintain particular programmes in respect of dairy products and poultry under Article XI, a measure that was consistent with Article XXIV:8(b). He also said that it may not be feasible to calculate the value of the "trade foregone" in the dairy sector as requested by the representative of New Zealand (Question 2).

II. SECTION II - RULES OF ORIGIN

17. The representative of Japan said that her delegation still had doubts as to the neutrality of the clause on circumvention in the FTA Article 301:3(c). However, since the parties to the Agreement affirmed that this clause was to be interpreted narrowly (Answer II.12), Japan would check on a case-by-case basis that the operation of this clause did not undermine its interests and would revert to it in future if warranted.

18. The representative of Japan continued by saying that while a change in the percentage of local content required might not, in the strictly legal sense, constitute a new barrier to trade in terms of Article XXIV, in practice an increase in this percentage could have adverse effects on the trade of third parties and could give rise to disputes. In operating the provisions of the Agreement on rules of origin, parties should bear in mind the provisions of Article XXIV, which clearly stipulated that any new

regulations of commerce shall not be more restrictive than those existing prior to the formation of free trade areas. The representative of Canada said that it was important to note that the provisions on rules of origin in the Agreement affected only the bilateral trade between the parties. The representative of Japan said that, even if that were the case, it should be noted that rules of origin in the context of the FTA had to be operated in such a manner as not to cause adverse effects on the trade of third parties, as provided in Article XXIV.

III. SECTION III - BORDER MEASURES

19. The representative of Australia said that from the reply of the United States to their question concerning the consistency of the waiver of customs user fees with respect to Canada with Article I of the General Agreement seemed to suggest that Article XXIV was necessary to justify the provisions of Article 403 of the Agreement, and that in the absence of Article XXIV the United States would be in breach of the obligation of non-discrimination of Article I (Answer III.2). The representative of the United States said that the legislation had been amended to bring the customs user fee into conformity with GATT. By virtue of Article XXIV, the consistency of the waiver with Article I was a moot point. The fee from which Canadian trade was exempted was not collected from other countries. The representative of Japan asked which provisions of Article XXIV justified the waiver granted by the United States to Canada under the Agreement. The representative of the United States said that the customs user fee was an "other regulation of commerce" covered under Article XXIV, paragraph 5(b).

20. The representative of Sweden, on behalf of the Nordic countries, asked how the 32 per cent drop in the collection of the fees in the first six months of the fiscal year 1991 could be attributed to the exemption of fees on imports from Canada (Answer III.2.2). In order to demonstrate whether other countries were bearing a disproportionate share of the burden, the rate of decrease in the fees collected had to be compared to the percentage share of United States imports from Canada in the total imports over the same period. The representative of the EEC said that in order to appreciate whether the 32 per cent drop in the collection of customs user fee effectively related to the trade between the two parties, the calculation had to take into account the details of the variation in the rate of fees charged on different imports.

21. The representative of Japan reserved the right to return to the issue of the scheme regarding export licences for short supply or conservation reasons since it had not been convinced of the consistency of the scheme with GATT.

IV. SECTION VI - AGRICULTURE

22. The representative of Australia said that, under Article 702 of the Agreement, each party reserved the right to reimpose a temporary duty on fresh fruit and vegetables over a period of twenty years. He questioned

the consistency of this provision with the "reasonable length of time" stipulated in Article XXIV:5(c) and with the terms of the draft decision negotiated in the Uruguay Round which envisaged that such period would not exceed ten years. The representative of Canada said that the "snapback" clause was basically applied as a safeguard measure for which the Agreement did not provide for a time frame compared to the elimination of duties where the Agreement had a clear set of rules. Article 702 specified the temporary nature of any such reimposition of duties.

23. The representative of Australia noted that the gap between the relative levels of government support for wheat and wheat products in the United States and Canada had narrowed, and that Canada had removed the import permit requirements for these products when originating in the United States. However, since the relevant provisions under Article 705 did not set a time frame for phasing out such restrictions between the two parties, import permit requirements could be reintroduced at any time. He said that the lack of such a time frame raised doubts as to the consistency of these provisions of the Agreement with the requirements in Article XXIV. The representative of Canada confirmed that import permit requirements had been removed pursuant to Article 705 the Agreement and in the light of the results of a technical exercise conducted under the FTA, which showed that the subsidy levels in the United States were less than the subsidy levels in Canada. In terms of Article 705 of the Agreement Canada could reintroduce import permit requirements if imports from the other party increased significantly; if this increase were the result of a substantial change in the relative support levels in either party; and if the action were consistent with other obligations under the Agreement including those relating to emergency measures. The parties to the Agreement considered that the particular provisions for fruit and vegetables and for grain and grain products were applied as a safeguard clause and therefore met the requirements of Article XXIV.

V. SECTION IX - TRADE IN AUTOMOTIVE GOODS

24. The representative of Japan said that the US/Canada Auto Pact was maintained despite the concerns expressed previously by third parties as to its appropriateness. It had developed into an exclusive arrangement with three types of membership.

25. The representative of the EEC said that, while the suppression of the export-based duty remission scheme might not have affected any consolidated GATT rights, it established a situation that was more restrictive than that which had prevailed prior to the coming into force of the Agreement. The representative of Japan shared the view that the elimination of the export-based duty remission scheme had the effect of distorting trade patterns. They were considering whether to raise this matter and, more specifically, whether to do so in the broader context of the General Agreement. The representative of Canada said that the objective of not raising barriers to the trade of other parties in Article XXIV:4 had to be considered together with the requirements of Article XXIV:5(b). Any judgement as to the restrictive effect of the elimination of the scheme in comparison to the situation which prevailed prior to the Agreement should be made with respect to trade in goods with bound rates. The

representative of the EEC noted with interest that the parties interpreted Article XXIV to mean that the obligation not to increase the restrictiveness of duties related exclusively to bound rates.

26. The representative of Japan asked why the parties had decided to suppress the duty remission scheme if it were neutral. The representative of Canada said that the decision to remove the scheme was part of the overall package of measures taken by parties to remove conditional provisions existing prior to the conclusion of the Agreement. The duty remission scheme was a measure applied unilaterally by Canada in the past, but there was no obligation under the GATT to continue such measures.

27. The representative of the EEC noted that the parties had a narrower interpretation of the derogation given in Article XXIV as regards other restrictive regulations of commerce in the case of the duty remission scheme than in the case of customs user fees.

28. In this connection, the representative of Australia drew attention to the draft decision on Article XXIV drawn up in the Uruguay Round with the participation of the parties to the Agreement.

VI. XI - EXCEPTIONS FOR TRADE IN GOODS

29. In response to the representative of Japan, the representative of the United States explained that, while the Jones Act dealt essentially with trade in services, they had referred to trade in goods when they had stated that the Jones Act was exempted from the coverage of the FTA (Answer XI), since the question was put to them under the section entitled "exceptions for trade in goods". To the extent that trade in services was covered by the Jones Act, the present provisions of GATT were not relevant. The representative of Sweden, on behalf of the Nordic countries suggested that the explanation might be that the Jones Act also dealt with the actual origin of vessels. The representative of the United States confirmed that the Jones Act covered the construction of ships in the United States but excluded trade in ships.

VII. SECTION XII - GOVERNMENT PROCUREMENT

30. The representative of the EEC noted that under the Agreement rules of origin were applied in the context of preferential trade. He asked the reason why a specific set of rules of origin was needed for the input of supplies from third countries which was different from the rules of origin which applied to other areas of the Agreement. He asked to what extent these different rules would be taken into consideration in the attempt to arrive at a single set of rules of origin in the Uruguay Round.

31. The representative of the United States said that nineteen different systems were applied in his country, each designed for determination of origin under a particular circumstance. For that reason his country had been active in pursuing the work on rules of origin in the Uruguay Round.

He hoped that the draft text that was tentatively agreed would create a unified system of rule of origin that would be of broad application.

32. The representative of Sweden, on behalf of the Nordic countries, referred to the terms of Article 104 and asked which rules of origin would prevail, in the event of any inconsistency between the rules of origin of the FTA and any such new rules developed in the area of government procurement? The representative of the United States said that there was no inconsistency in this respect since the rules of origin for government procurement in Article 1309 of the Agreement were developed to apply to procurements above a threshold of twenty-five thousand US dollars set in that Agreement and below the threshold of the Agreement on Government Procurement.

VIII. SECTION XIII - SERVICES

33. The representative of Japan asked the reason for the inclusion of Article 1703, paragraph 2 in the Agreement if these provisions had no impact on the freer flow of financial services (Answer XIII). He suggested that the impact of these provisions should not be assessed only on the basis of the overall share of foreign bank subsidiaries in total domestic bank assets, or the relative shares of US and non-US banks, since these shares might have remained unchanged since the implementation of the FTA due to certain other factors. The representative of Canada said that since the introduction of the FTA, all requests from the United States and from other countries for authorization to increase the capital of Canadian bank subsidiaries had been granted. No other steps had been taken in the past two years which could have an impact on domestic assets of foreign bank subsidiaries in Canada.

34. The Chairman reiterated that it would be best to take a pragmatic approach to the discussion of services and investment, and that the Working Party pursue the information exchange on these issues, without prejudice to the nature of conclusions that it would ultimately draw in the light of the provisions of the General Agreement.

IX. SECTION XVII - TRADE IN STEEL

35. The representative of Hong Kong noted that there were no existing "voluntary export restraints" between Canada and the United States (Answer XVIII) and reiterated the hope that none would be introduced, since the agreement on safeguards that was likely to emerge from the Uruguay Round would prohibit "grey area" measures.

36. The representative of Sweden, on behalf of the Nordic countries, asked whether the FTA should be understood to mean that when the current steel programme expired at the end of March 1992, the United States would not request a VRA on steel import from Canada. The representative of the United States said that the outcome of the ongoing negotiations in the steel sector would determine their policy on steel, including the question of the present arrangements which expired on 31 March 1992.

X. SECTION XVIII - OTHER QUESTIONS

37. The representative of the EEC noted that recourse to Section 301 of the Trade Act of 1974 was compatible with the Agreement (Answer XVIII.1) but that no measures could be taken before the exhaustion of the bilateral dispute procedures under the FTA. The representative of the United States said that the Agreement did not have provisions on the application of Section 301. By concluding the FTA with Canada, the United States had exhausted the possibilities of achieving the objective of trade liberalization set out in Section 301.

38. The representatives of the EEC and Japan said that, as the written replies to additional questions (Spec(91)18/Add.1) had been made available only recently, they reserved the right to seek further clarification on these at a later stage.

B. CONSIDERATION OF CONCLUSIONS

38. The Chairman said that in its first two meetings the Working Party had had the opportunity to review the factual information provided by parties to the Agreement on the basis of questions and answers exchanged in the Working Party. He invited those delegations wishing to seek more detailed or additional clarification on various aspects of the Agreement, to give notice of their questions to the parties sufficiently in advance of the next meeting.

39. The Chairman recalled the terms of reference of the Working Party (L/6823/Rev.1) and outlined an indicative list of the issues that might reasonably be expected to be addressed in the examination of the Agreement in this context. The Working Party could examine these and any other issues suggested by the members of the Working Party, when considering its conclusions at the next meeting.

40. He suggested that the Working Party next meet in the second half of July (subsequently scheduled on 23-24 July 1991). In order to assist the discussion at that meeting the secretariat would prepare a draft of the factual part of the report of the Working Party.