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# The Administration of Chapter 19 Binational Proceedings under NAFTA

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# THE ADMINISTRATION OF CHAPTER 19 BINATIONAL PROCEEDINGS UNDER NAFTA

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## I. INTRODUCTION

To provide some context for this article on the North American Free Trade Agreement (NAFTA),[1] a brief review of Chapter 19 is important. It has been eight years since the beginning of the Canada-United States Free Trade Agreement (FTA),[2] and three years have past since NAFTA went into force.

## II. HOW DID CHAPTER 19 COME ABOUT?

The context leading to the creation of Chapter 19 of NAFTA has to do with trade in the early to mid-1980's between the United States and Canada particularly, but also more generally under GATT.[3] Both the United States and Canada had conservative political administrations. Brian Mulroney was the Prime Minister of Canada and Ronald Reagan was the President of the United States. They were good personal friends, both conservatives and both Irishmen. Every time they talked to each other, they would discuss trade disputes: cedar shakes and shingles, wheat, pork, swine, lumber, etc. Many people characterized the trading relationship between the U.S. and Canada, which is the single largest bilateral trading relationship in the world, as "hogs and logs," or "suds and spuds."[4] At the Shamrock Summit in 1985, Brian Mulroney finally said, and I paraphrase, "Ron, you know we're good friends! We've got to cut this out. Even though we have so many things in common, we're always fighting about these trade disputes. Can't we do something to fix this?" He proposed the negotiation of a free trade agreement.

A free trade agreement had been tried several times before in United States-Canada history. In fact, a free trade agreement had been passed by the Canadian parliament in the early part of this century, but the Canadian government which negotiated it fell on the basis of that agreement. Thus, suggesting negotiation of a new free trade arrangement was a courageous proposal.

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1. North American Free Trade Agreement, Dec. 17, 1992, U.S.-Can.-Mex. (effective Jan. 1, 1994), 32 I.L.M. 605 (1993).

2. Canada-United States Free Trade Agreement, Jan. 2, 1988, U.S.-Can. (effective Jan. 1, 1989), 27 I.L.M. 281 (1988).

3. General Agreement on Tariffs and Trade, Oct. 30, 1947, T.I.A.S. 1700, 55 U.N.T.S. 194.

4. For further information about this relationship *see* WILLIAM J. DAVEY, PINE & SWINE: CANADA-UNITED STATES TRADE DISPUTE SETTLEMENT (1949). William J. Davey is the head of legal affairs at the World Trade Organization.

Negotiations began in 1986. They were conducted under a fast-track negotiating authority approved by the U.S. Congress that was to expire at the end of the fiscal year in 1987.[5] Under the U.S. Statute, notification of the intent to negotiate a trade agreement had to go to Congress under that Fast-Track authority by midnight of September 30, 1987, or the negotiations could not go forward from there.[6] At the same time in 1986, U.S. representatives were preparing for the meeting in Punta del Este, Uruguay, which led to the initiation of the Uruguay Round of multilateral trade negotiation under the GATT.

The U.S. negotiating objective in the GATT talks was to get the biggest agreement possible, and to cover subjects that had been traditionally left out of GATT negotiations such as: agriculture, intellectual property, services, and investment. Both the U.S. team and the Canadian team would fight very hard for its country's best interests throughout each part of the negotiation. At the same time, the teams were working toward a win-win agreement and wanted to show the way for a broad agreement among the parties of GATT.

One of the goals for the United States in that negotiation was to eliminate Canadian domestic subsidies. Canada provided substantial provincial and federal government subsidization. In fact, Canada had a regional development policy to provide subsidies to insure that the country did not over-urbanize, and that there would always be people throughout the country. However, about eighty percent or more of the population is within twenty-five miles of the U.S. border.

One of the goals of the Canadian government was to eliminate U.S. "contingency protection." Those are buzz words for eliminating or getting a special exemption or waiver for Canada from the application of U.S. unfair trade laws. Canada was specifically targeting the U.S. antidumping and countervailing duties. Antidumping laws impose duties on goods that are sold at less than fair value, and allow a country to raise the value or price of goods to the price of market value of the goods in the importing market.[7] Countervailing duties offset unfair government subsidies.[8]

The subsidies negotiation failed. There was no way the Canadian government could accede to the U.S. demands that reduce its regional subsidies. At the same time, the U.S. Congress would not have stood for, and to this day would not stand for, the elimination of the unfair trade laws, an exemption, or a waiver. This was true even for Canada, in spite of the tremendous amount of political good-will for the Canadians and the proposed agreement.

Two weeks before the deadline for the expiration of the U.S. Fast-Track negotiating authority, the Canadians walked out of the negotiations.

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5. Trade Act of 1974, 19 U.S.C. § 2112(b)(1) (1993).
6. *Id.* § 2112.
7. Tariff Act of 1930, 19 U.S.C. § 1673 (1993 & Supp. 1996).
8. *Id.* § 1671.

The U.S. negotiating team worked day and night, literally, for weeks prior to that. Over twenty chapters of the proposed agreement had been negotiated. Everything was in place. Each chapter had been distilled down to the point of making a few final decisions. However, contingency protection and subsidies loomed as a real problem because the Canadians had negotiated those issues in the media. The Canadians were vocal from the beginning of the negotiations that they were going to eliminate U.S. contingency protection. There was no way they could sign the agreement without the assurance that they were going to have something arranged to address the unfair trade laws. As a result, the Canadians walked out.

The chief U.S. negotiator, Peter Murphy, and a couple of other folks were bemoaning the fact that the agreement was not going to happen. The expiration of fast-track was three to four days from the deadline, and it appeared as though we had failed. That night a call came through to the Secretary of Treasury, Jim Baker, from Michael Wilson, the Finance Minister in Canada. They took the issue to the next phase. They felt that to close the deal it would be necessary to go beyond the negotiators to the cabinet level. The Canadians needed to have assurances that the agreement was going to stick. If they could get Jim Baker to agree to the deal, they knew President Reagan would support the agreement and get it through the Congress.

Literally, around-the-clock negotiations started. For the final negotiations, the United States had Jim Baker and his team on one side while the Canadians had Wilson and his team on the other. Each negotiator would walk in and the group would negotiate a deal for each chapter. The last chapter discussed was Chapter 19. The Chapter 19 people were in the back room writing like crazy, trying to cobble something together that worked for the Canadians.

The agreement needed to provide something for the Canadians to show their public that they were benefiting from some form of contingency protection. Chapter 19 was the political panacea for that. What it provided was originally proposed by Sam Gibbons, who at the time was Chairman of the House Ways and Means Committee. His proposal had been discussed a little bit, but there had been no working group that was actually dealing with it. Prior to this proposal, dispute settlement was the subject of Chapter 18. There really was not any concern for doing anything broader in the dispute resolution area. His proposal just went by the wayside. When the Canadians came back to negotiate in the last three days of the talks, this proposal was turned into Chapter 19.

## II. WHAT DOES CHAPTER 19 PROVIDE?

Chapter 19 confers contingency protection. It was intended to be temporary and last only five years. It provides for binational panels of trade experts from the United States and Canada to be convened for each antidumping and countervailing duty determination or material injury determination made by the relevant investigating authorities in each country on the other country's goods. Experts are drawn from rosters known

for their objectivity and impartiality. These panels act in place of domestic courts because in Canada, federal courts could review these sorts of decisions. In the United States the Court of International Trade (CIT) handles these disputes. Essentially, Chapter 19 carves out a piece of domestic jurisdiction and gives it to a panel of experts who can make binding decisions. Binational panels are not given injunctive authority and therefore can not grant injunctive relief, but they can make a ruling that is as binding as a court decision on those determinations based on domestic standard of review under domestic law.

Under the FTA, fifty-seven different matters have been considered up to this time, five were under Chapter 18 which is outside of the scope of this article, and fifty-two under Chapter 19. Thirty cases were filed in the United States and nineteen in Canada. Three were extraordinary challenges. Rules of procedure were prepared for the conduct of reviews. These were amended on four different occasions. The last amendment to the panel rules was made in February of 1994, and served as the basis for the NAFTA panel rules. They were published in the Federal Register,[9] and the NAFTA rules came out February 23 of 1994.[10]

A code of conduct[11] was also created because it is necessary that panels of experts act with objectivity and adhere to a very strict standard. This is true both as to conflicts of interest and appearances of conflicts of interest. For these purposes, a very rigorous disclosure system was created. Panelists cannot be affiliated with one of the Parties, that is, one of the governments; they must disclose their government contracts or representation of the United States, Canada or Mexico.[12] Each partner of a law firm has to make sure they are not representing anybody that may be impacted by the decision. Panelists must be very careful not to be representing other clients on issues that are under litigation before the panel. In fact, issue conflicts caused a lot of problems for the Secretariats because the subject had not been addressed adequately in the first Code of Conduct. The administration of the Code of Conduct is the single most important role that the NAFTA Secretariat plays by serving as the "clerk of the court" for this system. Secretariats under NAFTA act as the institutional memory by default, because each one of the panels is ad hoc by its very nature. Some of the panelists may have had experience but in many cases they have not. Therefore, the experience level of the panelists varies each time one is put together.

The Office of the U.S. Trade Representative (USTR) elects U.S. panelists; and corresponding ministries in Canada and Mexico appoint panelists from their countries. The national sections of the Secretariat have no responsibility under Chapter 19 for antidumping or countervailing duty matters until requests for panel reviews are filed. Then, the NAFTA

9. 59 Fed. Reg. 8702-01 (1994).
10. 59 Fed. Reg. 8686 (1994).
11. 59 Fed. Reg. 8720 (1994).
12. *Id.*

Secretariat coordinates the selection of the panel with the USTR; that is, the Secretariat sends documents to the roster members, receives them back and forwards them to USTR, where the selection is made.

After the Secretariat is notified as to who is going to sit on a particular panel, USTR's involvement ends. The NAFTA Secretariat handles the entire matter, including reviews of U.S. administrative agency decisions. The NAFTA office in Ottawa handles Canadian appeals, and there is a *Sección Mexicana* [Mexican section] in Mexico City, which handles all appeals from determinations of the *Secretaría de Comercio y Fomento Industrial*[13] (SECOFI).

The United States and Canada have a bifurcated process for review of antidumping and countervailing duty administrative decisions. First, a decision is made by one of the agencies as to the existence of dumping or subsidies. If the decision is affirmative, the issue of material injury is reviewed separately by a different agency. Each of those decisions can be appealed separately. Previously, the issues had to be appealed together to federal courts in the United States. In Mexico, SECOFI makes both the dumping or subsidy decision and then follows up with an injury decision. Thus, panels in Mexico will generally have twice the work than a panel in the United States

A very important part of what we do concerns the standard of review. Each country has a standard of review that is spelled out in Chapter 19, and they differ significantly from each other.[14] The standard in the United States is based on substantial evidence on the record, and the agency's decision must be made in accordance with the law.[15] In Mexico, the standard of review is set out in Article 238 of the "Código Fiscal de la Federación"[16] [Federal Fiscal Code], based solely on administrative record. In Canada, the standard of review involves the application of principles of natural justice and fair play, a much more equitable view of things. Although it looks like due process, it is not exactly application of due process as we think of it in the United States. Thus, the standard of review is distinct for each country.

The extraordinary challenge committee is also important. If a panel is accused of impropriety, its decision may be appealed to an extraordinary challenge committee. Such a challenge may only be initiated by one of the governments, not by one of the private parties. There is no further review, with the exception of constitutional issues in the United States.[17]

The governments have to allege one of three grounds: first, that there has been panel misconduct. That would include bias, misconduct, a bribe, something really exceptional by a panelist. A second ground is that they

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13. Secretariat of Commerce and Industrial Development.
14. NAFTA, *supra* note 1, Annex 1911, 32 I.L.M. at 693.
15. *Id. See also*, Tariff Act of 1930, 19 U.S.C. § 1516(a) (1983 & Supp. 1996).
16. D.O., 31 de diciembre de 1981.
17. A special process has been put into place for review of constitutional issues only by the courts of the United States. There has been some criticism by Mexican attorneys that there is no process for review of constitutional issues under the Mexican Constitution.

have had a gross procedural error. The third ground is an allegation that the panel acted in excess of its authority. A clause was added to NAFTA that specifically addressed failure to apply the standard of review,[18] because that was the claim made in all three challenge committees under the FTA, that they had failed to properly apply the standard of review.

The party challenging a panel decision must also demonstrate before the extraordinary challenge committee that the errors alleged by the government materially affect the panel decision. In my opinion, if a government is complaining about the decision, this demonstrates material effect by itself. The third hurdle is the most important one; the decision has to threaten the integrity of the binational panel review process. None of the extraordinary challenge committees reversed or sent back a panel decision, however, the committees are moving a little closer to it.

There have been some controversial decisions, three in particular. One involved pork;[19] one involved live swine;[20] and the third involved lumber,[21] all from Canada. These issues have been categorized as "hogs and logs," or "pine and swine." In the first extraordinary challenge case involving a decision by the U.S. International Trade Commission on Fresh, Chilled, or Frozen Pork from Canada, the committee dismissed the U.S. claims, stating that the United States had not come close to meeting the standard of review required. The second extraordinary challenge committee reviewed the decision of a panel which had remanded a decision of the U.S. International Trade Administration involving live swine from Canada for further proceedings. There was a very vigorous dissent by the chairman, and the extraordinary challenge committee in their review of that decision castigated the panel for not trying to find more evidence on the record to support what the agency had done. Essentially, the majority of the committee said, "You haven't gone so far that we need to take action and step in, but we can see perhaps in the future that there might be a need for that by another committee."

The third committee reviewed the decision of a panel in which the majority, consisting of three Canadians, essentially required the U.S. International Trade Administration to revoke a countervailing duty order on Softwood Lumber from Canada. The two Americans on the panel wrote a vigorous dissent. It went before a three-member extraordinary challenge committee. Two Canadians affirmed the panel decision, and the American dissented. The shrillness of the dissent greatly diminished the force of the argument.

## III. CONCLUSION

This process is still in its toddler stage, and we are going to have to see how it evolves over time. The procedures furnish expeditious, efficient

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18. NAFTA, *supra* note 1, ch. 19, art. 1904 § 13(a)(iii), 32 I.L.M. at 683.
19. *In re* Fresh, Chilled, or Frozen Pork from Canada, 13 I.T.R.D. (BNA) 1859 (ECC 1991).
20. *In re* Live Swine from Canada, 15 I.T.R.D. (BNA) 2025 (ECC 1993).
21. *In re* Certain Softwood Lumber Prods. from Canada, No. ECC 94-1904-01 USA (ECC Aug. 3, 1994).

and low cost review of government agency decisions. I think we provide the services we are intended to provide. Meanwhile, the jury is out as to how effective this system will be in the very long term.