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Communiqué

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Emphasize WTO Instead of the NAFTA for Complex Canada-US Subsidy Disputes, says C.D. Howe Institute study

Canada should consider using the dispute settlement process of the World Trade Organization (WTO) instead of that of the North American Free Trade Agreement (NAFTA) to oppose any future US countervail action against Canadian lumber or in any other complex subsidy case, says a C.D. Howe Institute study released today.

The study is entitled *Settling Trade Remedy Disputes: When the WTO Forum Is Better than the NAFTA*. It was written by Robert Howse, Associate Professor of Law, Associate Director of the Centre for the Study of State and Market at the University of Toronto, and an Adjunct Scholar of the C.D. Howe Institute. Next year, he will be a Visiting Professor at the University of Michigan and at the Harvard Law School.

Howse contrasts the use of the NAFTA Chapter 19 process, in which binational panels expeditiously review the consistency of contested antidumping and countervailing duty decisions with the trade laws of the country imposing the duties, with the possibility of resorting to WTO dispute settlement in similar disputes.

Howse says that the quality of the NAFTA binational panels' economic and legal analysis has generally been high. Their role is to decide whether NAFTA countries' domestic agencies decisions to impose antidumping and countervailing duties correctly interpret the country's trade law. And this, Howse says, can lead to serious problems in cases involving high politics and controversy over the meaning of the law. The process can then be deprived of legitimacy by delays, high costs, divisions of panelists along national lines, and lack of consistency in decisionmaking, since each panel is an *ad hoc* decisionmaker in a particular dispute and can be circumvented if countries rewrite sections of their trade legislation.

Howse argues that these weaknesses were particularly evident following Canada's challenge of US countervailing duties imposed in 1992 on Canadian softwood lumber. The panel decisions in this case — in Canada's favor, and with a majority of Canadians on the panel — led prominent Americans to view the Chapter 19 process as flawed. Subsequent changes to the US trade law prevented Canada's resorting to the legal arguments with which it prevailed at the binantional panel, thereby reversing any gains for Canada in terms of future market access. This led Canada to accept restraints on its softwood lumber exports to the United States.

Howse notes, however, that, at the WTO, multilateral dispute settlement procedures were strengthened following the Uruguay Round of trade negotiations. For example, the consent of the losing party is no longer required for panel reports to be adopted. And the new WTO Agreement on Subsidies provides more precise definitions and benchmarks of what constitutes a countervailable subsidy, against which determinations by US agencies can be scrutinized, but which, crucially, as obligations of international law, cannot be affected by unilateral US legislative action.

These changes suggest that, although relatively routine cases — particularly those concerning antidumping actions — should continue to be handled through the NAFTA's Chapter 19, Canada should put greater emphasis on the WTO dispute settlement mechanism in controversial subsidy cases.

At the same time, says Howse, Canada should work to strengthen the Chapter 19 process itself, through the establishment of a permanent tribunal, or multinational panels that could reduce potential conflict-of-interest problems relative to the current binational panel system, or even by instituting a permanent appeals body for panel decisions.

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Communiqué

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Il faut mettre l'accent sur l'OMC plutôt que l'ALENA pour les différends sur les subventions de nature complexe, soutient une étude de l'Institut C.D. Howe

Le Canada devrait envisager d'utiliser le mécanisme de règlement des différends de l'Organisation mondiale du commerce (OMC) plutôt que celui de l'Accord de libre-échange nord-américain (ALENA) pour faire opposition à toute imposition future par les États-Unis de droits compensateurs sur le bois d'oeuvre canadien, ou pour tout autre cas portant sur des questions de subventions de nature complexe, soutient une étude de l'Institut C.D. Howe publiée aujourd'hui.

L'auteur de l'étude, intitulée *Settling Trade Remedy Disputes: When the WTO Forum Is Better than the NAFTA* (Régler les différends concernant les recours commerciaux : lorsque l'OMC est supérieure à l'ALENA) est Robert Howse, professeur agrégé de droit et directeur adjoint du Centre for the Study of State and Market à l'Université de Toronto, et attaché de recherche auprès de l'Institut C.D. Howe. L'an prochain, M. Howse sera professeur invité à l'Université du Michigan et à la Harvard Law School.

L'auteur met en contraste l'utilisation du mécanisme du chapitre 19 de l'ALENA, dont l'objet est d'établir rapidement, par le biais de groupes spéciaux bilatéraux, si les décisions contestées d'un pays d'imposer des droits antidumping ou compensateurs sont conformes aux lois mêmes de ce pays, avec la possibilité d'utiliser le mécanisme de l'OMC dans des cas semblables.

M. Howse explique que les groupes spéciaux de l'ALENA émettent généralement des décisions d'analyse des questions économiques et de droit de grande qualité. Leur rôle consiste à établir si les décisions des organismes gouvernementaux qui décident des droits antidum-ping et compensateurs procèdent d'une interprétation correcte des lois du pays où elles sont émises. Ceci peut mener à de sérieux problèmes, dit M. Howse, lorsque qu'il y a controverse sur la signification des lois existantes et que le problème se hisse au niveau politique. Les retards alors créés, les coûts élevés, les divisions des membres du groupes selon leur nationalité, un manque de cohérence dans les décisions des divers groupes, qui sont reconstitués à neuf chaque fois qu'il y a un cas à examiner, et le fait qu'un pays perdant une décision peut toujours réécrire ses lois pour la contourner, peuvent remettre en question la légitimité même du mécanisme.

M. Howse soutient que ces faiblesses furent tout particulièrement évidentes lors de la contestation par le Canada des droits compensateurs imposés par les États-Unis sur le bois d'oeuvre canadien en 1992. Les décisions du groupe spécial, composé en majorité de Cana- diens, qui

s'est penché sur ce différend furent favorables à la position canadienne, mais amenèrent certains Américains en vue à déclarer que le mécanisme était défaillant. Par la suite, des changements apportés à la loi américaine ont eu pour effet d'empêcher le Canada d'avoir recours aux arguments juridiques qu'il avait invoqués devant le groupe spécial binational, infirmant du même coup tout avantage qu'il aurait pu obtenir en matière d'accès futur au marché. Ceci a donc mené le Canada a négocier des restrictions sur ses exportations de bois d'oeuvre vers les États-Unis.

Par ailleurs, fait remarquer M. Howse, les procédures de règlement des différends à l'OMC ont été renforcées à la suite des négociations commerciales d'Uruguay. Par exemple, il n'est plus nécessaire d'obtenir le consentement d'une partie perdante pour faire adopter les rapports des groupes spéciaux concernant un différend. Et le nouvel Accord sur les subventions contient des définitions et des points de référence plus précis de ce qui constitue une subvention susceptible de donner lieu à un droit compensateur, et qui peuvent être utilisés pour examiner les décisions des organismes américains mais qui, parce qu'il s'agit d'obligations découlant du droit international, ne peuvent être touchées par une mesure législative unilatérale de la part des États-Unis.

Ces changements font penser que le Canada devrait s'appuyer d'avantage sur le mécanisme de règlement des différends de l'OMC pour les cas controversés de subventions, bien qu'il serait de mise de continuer à utiliser le chapitre 19 de l'ALENA dans les cas relativement routiniers — particulièrement ceux concernant les mesures antidumping.

Dans un même temps, M. Howse propose aussi que le Canada s'applique à renforcer le mécanisme du chapitre 19, soit par l'établissement d'un tribunal permanent, soit par le recours à des groupes multinationaux plutôt que bilatéraux, ce qui réduirait les éventuels conflits d'intérêt, ou encore en instituant un comité d'appel permanent pour les décisions des groupes spéciaux.

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Settling Trade Remedy Disputes:
When the WTO Forum Is Better than the NAFTA

by

Robert Howse

The binational panel process set up under Chapter 19 of the North American Free Trade Agreement (NAFTA) to review antidumping and countervailing duty decisions has been under a cloud ever since a US judge opined that the process was flawed under US law and Canada was forced to negotiate restraints on its softwood lumber exports to the United States despite a panel ruling in its favor.

NAFTA binational panels have been effective in relatively routine cases — particularly those concerning antidumping actions. But in cases involving high politics and conceptual controversy, the process can be deprived of legitimacy by delays, high costs, division of panelists along national lines, and lack of consistency due to the *ad hoc* nature of the panels.

Since the Uruguay Round of trade negotiations, however, the dispute settlement procedures under the World Trade Organization (WTO) have been made much more effective. Furthermore, the new WTO Agreement on Subsidies provides increasingly precise definitions and benchmarks of what constitutes a countervailable subsidy, against which determinations by US agencies can be scrutinized, but which are not bound by US judicial interpretation.

These changes suggest that Canada should emphasize the WTO process in any future US countervail actions against Canadian lumber or in any other complex subsidy cases.

At the same time, Canada should work to strengthen the Chapter 19 process itself, perhaps through the establishment of a permanent tribunal, multinational, rather than binational, panels, or even a permanent appeals body for panel decisions.

Main Findings of the Commentary

- In 1994, the United States challenged the decision of a dispute settlement panel set up under Chapter 19 of the Canada-United States Free Trade Agreement (FTA) that directed the US agency responsible for imposing countervailing duties on Canadian lumber to remove those duties.
- The United States lost the challenge, but the US member of the Extraordinary Challenge Committee (ECC) dissented, implying that the Chapter 19 process, designed to expeditiously review the consistency of antidumping and countervailing duty decisions made in one country with the trade laws of that country, cannot work consistently with US law. His comments opened the door to modifications of US trade law, ensuring that the US agency's interpretation of the pre-existing law stood. This forced Canada to accept negotiated restraints on its lumber exports. Ever since, the Chapter 19 process — now part of the North American Free Trade Agreement (NAFTA) — has been under a cloud.
- NAFTA binational panels have certainly disposed of routine appeals more expeditiously than the alternative legal process, and the quality of their legal and economic analysis has generally been high. But in controversial cases, such as *Softwood Lumber*, delay and costs can be great and the division of panelists along national lines can deprive panels of legitimacy. Another weakness is a lack of consistency, since each panel is an *ad hoc* decisionmaker in a particular dispute. And panels must show a greater deference to Canadian than to US agency decisions, because the standard of review of agency decisions in both countries, which panels must apply, differs.
- Furthermore, compared with the FTA, the NAFTA extended the grounds for the extraordinary challenge of panel decisions, the time period under which ECCs can consider such challenges, and the ability of ECCs to examine whether a panel correctly analyzed a case.
- Following the Uruguay Round of trade negotiations, the multilateral dispute settlement process, which was already able to redress much of the power imbalances between large and middle-sized trading partners, was much strengthened under the aegis of the World Trade Organization (WTO).
- In addition, the new WTO Agreements on Subsidies and on Dumping offer increasingly precise definitions of concepts such as "subsidies," "dumping," and "material injury," providing benchmarks against which US agency determinations can be scrutinized that are not bound by US judicial interpretation. In particular, clearer criteria now exist for the definition of a countervailable subsidy.
- These changes suggest that, while relatively routine cases — particularly concerning antidumping actions — should continue to be handled through NAFTA's Chapter 19, Canada should put greater emphasis on the WTO dispute settlement mechanism in subsidies cases, such as lumber, that involve high trade politics and considerable conceptual controversy.
- At the same time, Canada should work to strengthen the Chapter 19 process itself, perhaps through the creation of a permanent tribunal or the establishment of multinational, rather than binational, panels, which could reduce potential conflict-of-interest problems, or even by transforming the ECC procedure into a permanent appeals body.

As a middle power whose main trading partner is the United States, Canada has long relied on the rules and processes of international trade law — including the dispute settlement processes of the General Agreement on Tariffs and Trade (GATT) — to constrain US protectionism.

With the rise of administered protection in the 1970s and 1980s, however, the multilateral legal framework appeared increasingly incapable of maintaining open borders between Canada and the United States, despite the considerable reduction of conventional tariffs accomplished in the GATT negotiations. In the early 1980s, even before the election of the Progressive Conservative government under Brian Mulroney, thinking in Canadian policy circles began to turn to the notion of a comprehensive bilateral trade deal with the United States, one that would eliminate (or severely constrain) the application of countervailing and antidumping duties between the two countries. Curbing these forms of administered protection was perhaps the primary concern of the Canadian negotiators of the Canada-US Free Trade Agreement (FTA).[1]

In the event, the United States did not accept any substantive limitation on the application of its trade remedy laws within North America. It did, however, agree to a process of review of domestic countervail and antidumping determinations by *ad hoc* binational panels of five members that, in the context of US trade law, would replace appellate review by the US Court of International Trade (CIT).

Canadian trade analysts had generally viewed the CIT as extremely deferential to the International Trade Administration (ITA) of the Department of Commerce and the International Trade Commission (ITC), the US agencies that rule on whether their country believes actionable subsidy or dumping exists in a particular case (see Box 1). Binational review would at least subject these decisions to scrutiny against basic US administrative law standards of reasonableness and of substantial evidence from the record.

In a number of early decisions of binational panels, these hopes seemed to be vindicated. Several decisions of the ITA and ITC were found wanting in legal coherence or in evidence to support conclusions of fact and law. Often, on reconsidering their findings in the light of panel rulings, the agencies removed or reduced countervailing or antidumping duties on Canadian imports.[2]

Not long after these successes, however, US producer interests began to protest that the binational panels were applying a standard of scrutiny that was not as deferential as that stipulated by US administrative law. These complaints soon found a sympathetic ear in Congress. One result was a significant weakening of the dispute settlement process in the text of the North American Free Trade Agreement (NAFTA). It expanded considerably the grounds on which a binational panel ruling could be appealed to an “extraordinary challenge committee” (ECC) of three members, and it shifted the emphasis in panelists’ credentials from trade expertise to judicial experience, the US view being that generalist judges have fewer intellectual resources to scrutinize carefully the highly technical legal and economic analysis of the domestic trade agencies than do specialists in the law and economics of international trade.

Even before the weakened NAFTA rules were in place, the FTA-based process was itself put into crisis by the *Softwood Lumber* case. When the United States lost the last of a series of panel decisions, with members of both the panel and the ECC dividing on national lines, US producer interests were furious. Their fury was supported by a vitriolic dissent by Judge Malcolm R. Wilkey, the US panelist on the ECC, in which he impugned the integrity of the entire binational review process, claiming that Canadian experts were unable to under-

Box 1: *How Administered Protection Works*

If countries are to provide administered protection to their trade, some agency must be empowered to decide whether a particular case justifies action. For countervailing duties to be applied, there must be a finding that a subsidy in the relevant legal sense exists. For antidumping duties to be applied, there must be a finding of dumping (usually, selling at a lower price in the importing country's market than in the exporting country's, or selling below cost). In both cases, proof of material injury is also necessary.

In the United States, the International Trade Administration (ITA) determines the existence of subsidies in countervail cases and dumping in antidumping cases, while the International Trade Commission (ITC) makes determinations of injury. A similar bifurcation of function exists in Canada between the Department of National Revenue and the Canadian International Trade Tribunal.

stand or properly apply US standards of administrative law review.

Following Wilkey's diatribe, prominent US trade lobbies questioned whether, in replacing judicial appellate review with an international mechanism, the NAFTA process was consistent with US sovereignty or even constitutional. In the event, the US Congress changed the law itself, allowing the imposition of new duties after the panel ruling. This move, in turn, led Canada to accept new restraints on lumber exports to the United States. In effect, after years of litigation and high hopes for the FTA binational review process, Canadian lumber producers were back where they had started in terms of security of access — and faced a huge bill for legal costs.

Reactions to the debacle in Canadian business and policy circles and the media have ranged from disappointment to outrage. Nevertheless, some trade experts apparently see the *Softwood Lumber* case as a kind of exception, with the binational panel mechanism likely to continue to function effectively in the future in Canada's interests, even in the weakened form embodied in the NAFTA.

I believe, however, that *Softwood Lumber* simply illustrates the weaknesses inherent in binational panel review, particularly in controversial matters entangled with high trade politics. In light of these weaknesses, I argue that Canada should consider placing greater emphasis on the use of the World Trade Organization's (WTO's) dispute settlement in cases that involve antidumping and countervailing duties against Canadian imports to the United States.

Relatively routine cases, particularly dumping matters, may continue to be well handled through the process specified in Chapter 19 of the NAFTA, which has the advantage of not requiring that the Canadian government become directly involved in a dispute that lacks major long-term policy implications. (Under the Chapter 19 FTA/NAFTA process, the actual claimants are usually affected private sector producers or their industry associates — a point further discussed in the next section. In contrast, the WTO process requires that a government be the claimant.)

At the same time, Canada should, as part of future negotiations expanding the free trade agreement beyond the three existing parties, work toward increasing the legitimacy of the Chapter 19 process, perhaps through the creation of a permanent appeals tribunal or of different selection rules that would ensure that a majority of panelists is from neither country involved in the dispute they are hearing.

Outline of the *Commentary*

This *Commentary* has seven parts. The first describes the FTA process of binational panel review; the next summarizes the experience with that procedure and discusses some of its struc-

tural weaknesses and drawbacks. The third part analyzes changes to the review process under the NAFTA and explains how they are significantly adverse to Canadian interests.

I then consider the *Softwood Lumber* dispute as an illustration of virtually all the main structural weaknesses of the binational review process.

The next part discusses the track record of multilateral GATT dispute settlement, including on countervail and antidumping matters; I also review the Uruguay Round's changes to the process and explain how they have strengthened it. Part six outlines how the new WTO dispute settlement mechanism, in tandem with the WTO agreements on subsidies and dumping, can be effectively used to challenge the imposition of duties by US trade authorities.

In the conclusion, I suggest a three-pronged approach to strategy in trade disputes with the United States.

The FTA Process

Chapter 19 of the FTA contains the binational panel review procedures for dispute settlement. Article 1904 provides that binational panels replace judicial review of the "final determinations" of the domestic trade authorities of Canada and the United States in countervail and antidumping cases between the two countries.[3] At the request of either party, a panel may consider and issue a binding decision as to whether a particular final determination conforms with the domestic trade remedy law of the importing country. The standard of review is that laid down by each party's relevant statutes (as amended from time to time) and by "the general legal principles that a court of the importing Party would otherwise apply."

Requests for panels, which must be made within 30 days of the issuance of an agency's final determination, can come only from a party to the FTA, but Article 1904(5) allows interests that would normally be entitled to judicial review under domestic law to petition their government to establish a panel. This means that, in practice, the panel process is largely driven not by governments but by private litigants, with producer interests in both countries heavily represented by counsel throughout.

In the case of US countervail and antidumping decisions, the panels' standards of review are largely derived from the general principles of US administrative law. The standards require that an agency's determination represent a reasonable interpretation of US law — that is, it need not be correct but it must be defensible as one of several possible reasonable interpretations of the law — and that findings of fact be supported by substantial evidence on the record, evidence that would allow a reasonable person to draw the inference in question.[4]

Where a binational panel deems that a finding is not in accordance with a reasonable interpretation of the law or is not supported by substantial evidence on the record, its powers are limited to remanding the matter to the domestic agency that made the original determination, to reconsider its findings in light of the panel's recommendations. In other words, the binational panel itself is powerless to remove duties; it can only order the domestic authorities in question to redetermine the matter.

In a number of cases, two or three panel remands have been necessary before the domestic agency in question has brought its decision in line with the law (or given up on finding adequate evidence to support it) and removed or reduced duties. Ultimately, if an exporter is dissatisfied with a redetermination, its only recourse is to have its government request yet another panel.

Panel decisions are made by majority vote, and reasons (majority, concurring, or dissenting) are provided in writing. Under the FTA

rules, panelists are chosen from rosters of trade experts provided by the two countries. (As discussed later, the criteria for panelists changed with the introduction of the NAFTA.)

Panels comprise five members, two chosen by each country and a fifth selected by agreement between them. If the parties fail to agree, they will decide by lot which of them will choose the fifth panelist.

Article 1904(13) provides for an "extra-ordinary challenge" mechanism whereby a panel ruling may be appealed to a committee (an ECC) composed of three persons, who must be judges or former judges of a US federal court or a Canadian court of superior jurisdiction.

The grounds for an extraordinary challenge under the FTA are:

- a panel member was guilty of gross misconduct;
- the panel seriously departed from a fundamental rule of procedure; or
- the panel manifestly exceeded its powers, authority, or jurisdiction as set out in Chapter 19.

Only if the ECC determines that the panel's decision has been materially affected by one or more of these defects and the integrity of the binational review process is threatened can an extraordinary challenge succeed. (But, as discussed later, the grounds for an extraordinary challenge have been substantially broadened in the NAFTA.)

Experience with Binational Reviews

The early prognosis for the capacity of binational panel review to constrain abuse of trade remedy law was largely positive. In a 1993 review of several years' experience with the process, Boddez and Trebilcock find:

> [T]he panels will use the substantial evidence test in such a way as to reduce barriers by placing greater restrictions on the administrative discretion exercised by the ITC and ITA.[5]

Other, earlier studies reach similar conclusions.[6]

In a more recent study, which includes *Softwood Lumber* (but which was published before its final aftermath), John Mercury finds:

> Canadian exporters realized substantial reduction in duties following appeal to binational panels while U.S. exporters enjoyed no such success....[T]he reduction of duties in nine out of fourteen [antidumping and countervailing duty] cases is a significant accomplishment for Canadian exporters,

and the average reduction from the initial duty imposed was substantial, amounting to 28.2 percent.[7] (How the figure was derived remains unclear, however. It should also be noted that the average assumed that the impact of removing all the duty in *Softwood Lumber* would not be reversed through US legislative action, as it has been.)

Some Limitations

These reviews seem impressive, but they cannot conceal several major limitations in the success of the process from a Canadian perspective. First, even a reduction of 28.2 percent of duties does not necessarily mean a substantial increase in market access for Canadian products; depending on the nature of the market and elasticities of supply and demand, countervail and antidumping duties can still provide US producers with a substantial price advantage over imports. What is important to Canadian exporters is how much duty reduction lessens that advantage and increases their sales. None of the studies mentioned above examines the success of the binational review process against this criterion.

Second, even if victorious, a complainant to a binational panel must pay its own legal costs. Mercury and Boddez and Trebilcock fail to provide data on these costs or to estimate the extent to which they mitigate the gains from reduction in duties. Michael P. Ryan, an analyst associated with the Brookings Institution, Washington, DC, estimates costs in the typical case at between US$200,000 and US$300,000 per litigant.[8] The amount is presumably much higher in complicated, multistage disputes such as *Pork* and *Softwood Lumber*, for which senior practitioners provide informal estimates of about US$500,000 to US$600,000.

A third and related problem is the amount of time that the process can take to settle a dispute. As Mercury notes, a number of major cases have required two more remands before the US agencies actually removed the duties. Thus, although panel review is touted as a much more timely process than appeal to the US CIT, and there has clearly been a substantial savings of time in routine cases, in many of the more controversial cases, including *Carbon Steel* and *Softwood Lumber*, delays have been almost as great or greater as the CIT's historic average of 734 days.[9]

Binational panels have become impatient with US agencies' lack of adequate response in remand determinations to failures in their initial analysis or, alternatively, to shifts in the grounds (legal, evidentiary, or both) of their decisions to impose duties merely so as to evade panels' criticisms. Thus, in several cases, including *Softwood Lumber*, panels have essentially said that the process cannot go on forever and that, since the agency involved has repeatedly failed to support its findings on the basis of law and evidence, it must remove duties.

This practice was unanimously upheld in extraordinary challenges in the *Pork* and *Live Swine* cases. However, it has also led to criticism of the process by US politicians and producer interests.

Indeed, the early success that Canadian exporters achieved with the binational panel process has led to considerable disapproval of the process south of the border. Much of this criticism has centered on the panels' supposedly undeferential treatment of US agency decisions. Some Americans claim that the trade experts on the FTA panels, insufficiently impressed with the analysis of the ITA and ITC, were taking the opportunity to use their special knowledge to redo the original decisions, rather than merely ensuring that they were reasonable in legal interpretation and supported by some factual evidence.[10]

At least until *Softwood Lumber*, ECCs were unanimous in rejecting the view that a panel's interpretation of the standard of review could easily become a basis for finding that it had manifestly exceeded its jurisdiction. However, these decisions did leave the door open, in egregious cases, to finding that a panel had exceeded its jurisdiction when it clearly misstated or failed to "conscientiously apply" the administrative law of the country whose ruling was appealed. But a panel's conscientious, good faith interpretation of the law, even where contrary interpretations would also be reasonable, is clearly a mere legal issue, not grounds for a finding of manifestly exceeded jurisdiction.

Despite these weaknesses, binational panels have certainly disposed of routine appeals more expeditiously than has the CIT, and the quality of legal and economic analysis employed by the panels has been high.

The NAFTA Process

During the NAFTA negotiations, especially in their final phases, some US congressional leaders launched a concerted assault on the binational panel process, focusing on the absence of deference to US agencies and several panels' supposedly incorrect application of US law.[11]

The Concerns

Although much of this criticism was clearly sour grapes due to US domestic producer interests' having lost a number of cases, several genuine concerns about the legitimacy and coherence of the process were also in play.

First, Canadian and US administrative law standards for judicial review of agency determinations differ, a point generally acknowledged by those with an understanding of both countries' systems.

This asymmetry is, of course, built into the panel process itself. For example, if US interests challenge a Canadian agency determination, the panel must apply the Canadian standard, as embodied in the *Federal Court Act*, which is one of significantly greater deference to agency decisionmaking than the US standard. With respect to errors of fact, the threshold is very high indeed: the finding must have been made in a perverse or capricious manner without regard to the evidence before the agency or tribunal. (This standard has been interpreted in recent Supreme Court of Canada decisions as requiring that agency decisions would almost have to be manifestly insane to be overturned.[12])

By contrast, US law requires merely that any finding not based on substantial evidence on the record be overturned. Thus, Canadians and Americans do not have an equal opportunity to have adverse agency findings reversed by panels.

A second area of legitimate concern is that, since each panel is an *ad hoc* decisionmaker in a particular dispute, different panels need not take the same approach to legal issues. One result is lack of legal certainty; ironically, arbitrariness in agency legal interpretations may now be replaced by inconsistent panel rulings.

The most obvious case of inconsistency has been panel interpretation of the specificity test in US countervailing duty law, particularly whether the relevant agency must consider all of a number of factors that go to *de facto* specificity (a concept explained in the next section of this paper). The *Magnesium* panel deemed that the agency did not have to look at all factors, while one of the *Softwood Lumber* panels, ruling almost at the same time, said that all factors must be weighed. And the extraordinary challenge procedure does not provide a means of clarifying inconsistent panel rulings so as to produce legal coherence for the future.

A third, related concern is that, even if panels are applying the US standard of review in an acceptable manner, they are nevertheless evolving the law somewhat differently than are the US courts with respect to countervail and antidumping actions that apply to all other countries. At one level, this concern may be the result of misunderstanding the process because, at least in theory, any future binational panel would be bound by the rulings of the US courts in cases dealing with parties not signatory to the NAFTA as one aspect of the law to be applied. Nevertheless, in practice, the fact that two kinds of institutions are evolving US law as it applies to different countries suggests the potential for some lack of legal coherence.

The Changes

The changes that US negotiators insisted on in the NAFTA reflect the weight the US Congress and administration attached to these various concerns.

One change was extending the grounds for an extraordinary challenge to include failure "to apply the appropriate standard of review" (Annex 1904.13). This rubric is very broad, going far beyond the notion in the *Live Swine* and *Pork* decisions that an extraordinary challenge may be available where the standard of review has clearly been incorrectly articulated or not applied conscientiously (that is, not in good faith). "Appropriate" is a vague legal category

and leaves ample room for voicing objections to just about any panel ruling.

In this respect, it is significant that the NAFTA's provisions on extraordinary challenges, unlike those of the FTA, explicitly invite the ECC, in effect, to reopen the whole case through "examination of the legal and factual analysis underlying the findings and conclusions of the panel's decision" (Annex 1904.13 (3)). To permit the committee the opportunity to re-examine the whole case, the period for extraordinary challenge review has been tripled from 30 to 90 days. The US House Ways and Means Committee all but suggested that these changes will turn the extraordinary challenge procedure into another kick at the can:

> By expanding the period of review and requiring ECCs to look at the panel's underlying legal and factual analysis, the changes to Annex 1904 clarify that the ECC's responsibilities do not end with simply ensuring that the panel articulated the correct standard of review. Rather, ECCs are also to examine whether the panel correctly analyzed the substantive law and underlying facts.[13]

Finally, with respect to the primary panels themselves, the roster of panelists is to "include sitting or retired judges to the fullest extent practicable" (Annex 1901.2 (1)). This criterion is a major change from the FTA's, which allowed for rosters dominated by experts in international trade law and economics.

The full import of this change can be understood only when one recognizes that the kind of errors in US agency determinations that binational panels identify, especially those relating to the "substantial evidence" standard of review, involve the examination of complex methodologies, empirical economic studies, econometric modeling, and sometimes dozens of specific calculations. Counsel for these cases are usually highly experienced experts from the Washington trade bar, supported by teams of consulting economists and econometricians.

Indeed, as Davey notes in writing about decisions made under the FTA rules:

> The principal explanation for the favourable reviews of the panel process, and, in particular, the high quality of the panel opinions, is that the panels were composed largely of active international trade law experts. While it may be helpful to expand the use of non trade law practitioners, it would likely be a mistake to severely curtail the use of trade law practitioners as panellists.[14]

The *Softwood Lumber* Dispute

The *Softwood Lumber* case may be considered an acid test of the value to Canada of the binational panel review process. Very significant exports (several billion dollars' worth per annum) were at stake in an industry of considerable importance to the Canadian economy. The high trade politics of the dispute were precisely the kind that require defusing by a transnational dispute settlement process that is rules based and impartial (as illustrated by the fact that an initial US agency ruling in Canada's favor was reversed after enormous congressional pressure intervened — although such a causal relationship is impossible to *prove*).

Yet instead of demonstrating the value of the process where major Canadian export interests are at stake and protectionist pressures below the border are high, *Softwood Lumber* illustrates its fragility and perhaps futility in such high-stakes trade disputes. Indeed, the result of the extraordinary challenge has been to create a legitimacy crisis for the whole process. Ironically and perhaps characteristic of Canadian timidity, this crisis is mainly located in the United States; since years of hard-won Canadian panel victories have been reversed

politically, it is *Canada* that should be questioning the worth of the whole exercise.

Some History

To appreciate the significance of *Softwood Lumber*, one needs a brief overview of the history of the dispute.

Since the early 1980s, the US softwood lumber industry has claimed that the fees for stumpage (the right to cut standing timber) payable by logging companies to Canadian governments are set below the resource rents that would be payable in a competitive market; this "subsidy" results in lower log costs for lumber producers than would prevail under competitive market conditions.

An important fact relevant to this claim is that the Canadian logging and softwood lumber industries are 75 percent integrated — that is, three-quarters of the softwood lumber market is represented by firms that purchase stumpage and transform their own logs into lumber.

Another important fact, on which the US industry relied heavily throughout this dispute, is that Canadian stumpage fees are lower than the fees private US forest owners charge logging companies in that country. The Canadian response throughout has been that the two regulatory approaches are not comparable and that the Canadian fees reflect, for instance, important environmental and infrastructure maintenance obligations imposed on Canadian logging companies.

In 1982, the US industry brought a countervailing duty action, now known as *Lumber I*, against softwood lumber imports from Canada. In 1983, the ITA found that Canadian stumpage programs provided no countervailable subsidy. This determination was based largely on the finding that the programs were not "specific" within the meaning of US domestic trade law, whose long-standing rule is that only specific subsidies are countervailable. (The distinction, at its most obvious, is between subsidies directly targeted to particular industries and enterprises — for instance, the bailout of a firm — and generally available benefits, such as education or health care.)

The US lumber industry was dissatisfied with this outcome and actively lobbied Congress to widen the definition of "specificity" so as to allow a positive determination in this kind of case. These efforts to change the statute did not succeed at first, but the US industry did see signs that the Commerce Department might be prepared to shift to a more expansive interpretation of the existing law. A coalition of lumber interests petitioned to reopen the case in 1986, claiming it had new evidence that, through administrative discretion exercised by provincial authorities, Canadian stumpage programs were being explicitly targeted to producers of softwood lumber and were therefore specific.

In the 1986 proceeding, generally called *Lumber II*, the ITA reversed itself and found that the "subsidy" was specific within the meaning of US law and therefore countervailable. This reversal was based less on any new evidence of targeting than on an approach to the law different from that adopted in *Lumber I*.

Duties were, however, never imposed since Canada came to a negotiated arrangement with the United States whereby an export tax of 15 percent was imposed on soft-wood lumber exports to that country, an arrangement referred to as the Memorandum of Understanding (MOU). A 1987 amendment to the MOU exempted British Columbia, on the basis of its decision to increase stumpage fees, and the Atlantic provinces (on slightly different grounds).

In 1988, under pressure from US domestic industry interests, Congress explicitly expanded the definition of "specificity" to include subsidies that, although not *prima facie* targeted to specific industries or firms, in fact benefit only a small number of them. The Commerce

Department's own internal rules for the application of these statutory requirements (the Proposed Regulations) contain a four-factor test encompassing an inquiry into both *de jure* specificity (targeting) and *de facto* specificity:

> In determining whether benefits are specific,...[the department] will consider, among other things, the following factors:
>
> (i) The extent to which a government acts to limit the availability of a program;
> (ii) The number of enterprises, industries, or groups thereof that actually use a program;
> (iii) Whether there are dominant users of a program, or whether certain enterprises, industries, or groups thereof receive disproportionately large benefits under a program; and
> (iv) The extent to which a government exercises discretion in conferring benefits under a program.[15]

In 1991, Canada unilaterally terminated the MOU, and shortly thereafter the Commerce Department itself initiated a new proceeding against Canadian lumber exporters (known as *Lumber III*). The ITA's final positive determination on subsidy (hereinafter called the Final Determination) was issued on May 28, 1992, following a preliminary positive determination in March. It found that stumpage programs in the various provinces conferred an average subsidy of 2.91 percent (ranging from 1.25 percent in Alberta to 5.95 percent in Ontario).

The Canadian provinces and lumber industry requested review of the positive determination by a binational panel, which issued its decision on May 6, 1993. The panel remanded numerous matters to the ITA for redetermination or clarification. On a number of issues, it found that the ITA had misapplied US law, and on others that there was no evidentiary basis for choices the ITA had made with respect to economic methodology or the conclusions it had drawn from economic evidence. On yet other matters, the panel found that the legal standard the agency had applied was unclear, ambiguous, or unarticulated.

The ITA Determination on Remand

On September 23, 1993, the ITA released its Determination on Remand, finding, in fact, even higher rates of subsidization than had been found in the initial determination. Issues of specificity and market distortion played an important role.

Specificity

In its Final Determination, the ITA had found, solely on the basis of its regulations' second factor (the small number of users), that the Canadian stumpage programs were specific. The Canadian complainants had argued, on the basis of classifying the range of products manufactured from softwood lumber, that 27 industries and 3,600 firms benefited from the program. The ITA took the view, however, that only two or three industries or industry groups benefited. Moreover, it ruled that, even on the Canadian view that 27 industries benefited, this number was still small enough to justify a finding of *de facto* specificity.

The panel, in its original decision, had accepted the possibility of there being extreme situations in which the limited number of users was, in itself, sufficient to find specificity (such as where only one or two companies were users of a program). In the case at hand, however, the panel held:

> Clearly, the 3600-odd stumpage users..., representing between two and twenty-seven industries (depending on the definition of industry being used), do not fall into the category of extreme cases.[16]

Thus, the panel made a remand to the ITA, requiring it consider all four factors in the test in determining whether the stumpage programs were specific. The panel also held that it was appropriate for the ITA to take into account the extent to which the number of users was merely a function of the inherent characteristics of the industry.

In its Determination on Remand, the ITA attacked the panel's interpretation of the specificity test. The test, according to the agency, could be applied sequentially, so that if one of the four factors pointed to specificity, considering the others was unnecessary. But with reluctance, the ITA did go on to consider the other three factors.

Overall, the ITA found that the evidence of statutory limitation of the programs to the lumber industry and of administrative discretion was insufficient, on its own, to require a finding of specificity. Pointing much more clearly to such a finding were the number of users and their dominance in the programs' benefits.[17]

Market Distortion

In its Final Determination, the ITA had also rejected a Canadian argument that the existence of a market distortion was a legal requirement for a finding of countervailable subsidy.

At the panel, the Canadian complainants had relied on two economic studies — one by Nordhaus, the other by Nordhaus and Litan — in arguing that no market distortion existed. The ITA criticized the former severely.[18]

The Nordhaus study outlines the basic economic theory that, when the supply of a resource is fixed, the quantity exploited does not depend on the access fee charged, provided that fee is positive (more than zero) but not so high as to push the marginal cost of exploiting the next unit of the resource above marginal revenue. Within this range, called the "normal range," the number of trees harvested is determined solely by the normal market demand and price for logs, not on the amount of the access fee.

Of course, the study admits, a negative access fee is a theoretical possibility — that is, government could pay users a grant to induce them to harvest trees if the cost of doing so exceeded sales revenue in a normal competitive market. But no one denied that the Canadian stumpage program had positive access fees.

The Nordhaus-Litan study reports a regression analysis of the effect on the quantity of trees harvested when, pursuant to the amended MOU of 1987, British Columbia substantially increased its access fees for stumpage. The study finds an elasticity close to zero — that is, the rise in fees did not result in a statistically significant decrease in the quantity of timber harvested.

In its original decision, the panel had reversed the ITA and found that, on a correct interpretation of US law, the existence of market distortion was a legal precondition for a finding of countervailable subsidy. As well, the panel had found that the ITA's rejection of the Nordhaus study was not supported by substantial evidence on the record. In particular, the agency's specific criticisms were based on misunderstandings or misinterpretation of the study and Nordhaus's testimony. Moreover, the ITA had not produced any competing expert testimony or significant empirical studies.

In rejecting the agency's criticisms of the Nordhaus study, the panel had placed special emphasis on the fact that the view presented by the ITA — that, in theory, stumpage access charges could affect the quantity of timber harvested — was consistent with the study. But, as the panel decision had indicated, nothing in Nordhaus proves that a fee set in the normal range could be so low that the quantity harvested would be greater than that harvested in a normally competitive market. With the fee in the excessive range, in fact, timber would go unharvested even if the cost of harvesting (but

for the access fee) was lower than the value to society of cutting that timber.

Finally, the panel had described the study by Nordhaus and Litan as the only empirical evidence either side had offered on the issue of market distortion and noted that the ITA had not even mentioned, let alone rebutted, this work.

In its Determination on Remand, the ITA stated criticisms of the Nordhaus study similar to those the panel had already found to be unsupported by substantial evidence on the record. It also put forward what it described as an alternative theory of the market distortion/marginal cost theory. Finally, it made some criticisms of the Nordhaus-Litan study.

Attempting to perfect that study, the ITA chose to alter some of the variables and rerun the regressions. Without explanation, it added the size of the harvest as a variable, and with this change, it found that, as stumpage access fees decrease, output increases! The complete arbitrariness in the choice of variable gives rise to the suspicion that the agency was prepared to select anything that would give it the result it wanted when it reran the regressions.

The Final Panel Decision

After receiving the Determination on Remand, the panel was once again convened to examine the ITA's findings. On specificity, the panel found that the agency had failed to articulate any rational, objective benchmark to sustain the conclusion that the subsidy was specific because there were too few users. In effect, said the panel's final decision, the ITA had not gleaned from the relevant case law any set of legal or economic principles that could provide a benchmark for the meaning of "too few," and its own tests were inconsistent and based on highly debatable classifications of the industries and firms that benefited from the alleged subsidy.

The panel also found that the ITA continued to reject the Canadians' market distortion argument without any meaningful economic evidence in the record to refute it. Furthermore, the agency's reworking of the empirical study, although it yielded a result that suggested that price and output might be affected by the subsidy, was not based on a rational methodology.

A majority of the panel — the three Canadian panelists — *instructed* on remand that duties be removed since the ITA had failed to furnish reasons and evidence for its conclusions despite having been afforded ample opportunity to do so.

In vigorous dissenting judgments, the US panelists — including the distinguished Yale international law professor Michael Reisman — criticized the Canadian majority for misapplying the US administrative law standard of review. Whether the number of users of a subsidy is too many or too few, they claimed, is inherently a judgment call, one based on accumulated agency experience and expertise, and as long as the result reached is not manifestly irrational, demanding that such determinations be justified against strict objective standards or benchmarks defeats the intention of Congress.

The dissent relied heavily on a recently decided US trade case, the *Daewoo* decision, which emphasized that the role of appellate review is not to perfect an agency's economic methodologies. But the majority of the panel viewed *Daewoo* as simply restating the existing standard of review and insisted that what was at issue in *Softwood Lumber* was not imperfection in a US agency's methodologies but manifest gaps in reasoning and evidence — that the ITA's conclusions could not reasonably follow from the record.

The Extraordinary Challenge

Not surprisingly, ***Lumber III*** was the subject of an extraordinary challenge by the United States on the grounds that the standard of review was misunderstood and/or incorrectly applied by the panel majority.[19]

Following the approach of the decisions in the ***Pork*** and ***Live Swine*** extraordinary challenges, the two Canadian members of the ECC rejected the argument, stating that at stake were differences of view about the US law, not a failure to apply the correct standard of review conscientiously. In any case, the integrity of the binational panel process was not threatened. The majority also applied the test of whether an appellate court ***could*** have reached the same conclusion as the panel and suggested it could.

The US member of the ECC, Judge Wilkey, launched a broadside attack not only on the panel and the ECC Canadian majorities but on the binational panel process itself, claiming,

> [T]he Binational Panel Majority opinion may violate more principles of appellate review of agency action than any opinion by a reviewing body which I have ever read.[20]

Further, he suggested, this was symptomatic of a systematic and apparently incurable failure of Canadian panelists to understand US administrative law. The implication was that a ***binational*** panel process simply cannot work on the basis that it is established in the FTA and the NAFTA, which, of course, inherently involves the application of US law by Canadian panelists in any case where rulings by US agencies are at stake.

Judge Wilkey's dissent did not fall on deaf ears in Congress, which effectively reversed Canada's victory by changing the law on specificity and market distortion so that it conformed to the US agency's interpretation of the pre-existing law.[21] In light of these changes, Canada felt compelled to negotiate anew voluntary restraints on the export of softwood lumber to the United States. They are now in place.

Weaknesses of Binational Panel Review

If one considers the entire ***Softwood Lumber*** saga, it displays all the following inherent weaknesses of the binational panel process:

- Delay and costs can be great. ***Lumber III*** took almost three years to work its way through the panel process to the extraordinary challenge, involving enormous expense on legal resources. (I worked as an assistant to one of the Canadian panelists, and the lawyers' briefing material on the case was so voluminous that it resulted in my university office being declared a fire hazard!)
- In controversial cases, division along national lines deprives panels of legitimacy, since the victory seems based on whichever country has three, rather than two, panelists. (By contrast, dissent has been rare in relatively routine cases, and decisions have never split along national lines.)
- Again in controversial cases, Americans are likely to be suspicious of interpretations of their own law by foreign nationals.
- The ***ad hoc*** nature of the process, which leads to inconsistency between panels' decisions, deprives controversial rulings of needed legitimacy. An illustration is that the binational panel in ***Magnesium***, which was contemporaneous with ***Softwood Lumber***, took a view of the application of the US trade law's specificity test that was opposite that of the ***Lumber*** panel, and corresponded with the US view of the matter.
- Any victory that Canada may have gained through the binational panel process with respect to future market access can be re-

versed by legislative action in the United States since, apart from notice requirements, the NAFTA does not constrain changes to US law, even if they reverse binding decisions of binational panels. Thus, years of costly litigation can come to naught.[22]

The Multilateral Alternative

An alternative to settling trade disputes through binational panels under the NAFTA (or FTA) is to turn to the multilateral process developed under the GATT and now incorporated, in an improved form, in the WTO.

The GATT Process

Despite persistent criticism that the GATT multilateral dispute process was slow and not legally rigorous, it worked well to resolve most trade disagreements between "contracting parties" (the technical term used to described GATT members). The GATT panel process required consensus for the adoption of panel reports and offered limited resources for enforcement beyond international pressure and a rarely invoked right of retaliation by the offended party. Yet Hudec, Kennedy, and Sgarbossa find, in a definitive study, that about 88 percent of the disputes put before it between 1948 and 1989 were successfully resolved (according to legal rules and/or agreement of the parties involved).[23]

Canada was successful against the United States in seven out of eight legal actions to which both countries were parties, a remarkable record that indicates a multilateral process can do much to redress a power imbalance between large and middle-sized international trade partners.[24]

Several problems did emerge under the GATT system, however — problems that made Canada justifiably interested in a binational process. The first was the United States' increasing trend in the 1990s toward noncompliance with panel rulings, especially in cases concerning antidumping and countervailing duty actions (and many of Canada's successes at the GATT were in trade disputes that did not involve such measures). Noncompliance was tempting because the party that lost a dispute had to agree to panel report before it was adopted.

Second, GATT rules provided panels with limited guidance in resolving controversial cases, especially with regard to subsidies and countervailing duties. The same could be said of disputes involving agriculture, where certain exceptions in the rules had been so bent or broadly interpreted over a long period of time that panels grappling with these very sensitive matters were likely to have limited legitimacy, leading to a high noncompliance rate.

A further legitimacy problem, especially in the United States, was lack of any appeal mechanism that could correct cases aberrantly decided (historically, GATT panels were often staffed by trade diplomats, not lawyers).

The WTO Process

The WTO Understanding on Dispute Settlement, negotiated in the Uruguay Round of the GATT, addresses many of the weaknesses just described.

For example, the consent of the losing party is no longer required for adoption of the panel report. Rather, adoption is automatic unless there is a consensus of WTO members (including the winning country!) against adoption. An appeal process has, however, been established; it involves a permanent appellate body staffed by a small roster of distinguished experts in international trade.

Second, strict time limits are set for panel proceedings. They are to take no longer than six months (three, in urgent cases); an exten-

sion to nine months is possible, but only if the panel submits a request, with reasons.

As well, the rules for subsidies and countervailing duties have been expanded substantially (details are in the next section), providing WTO panels with much clearer benchmarks against which to resolve these controversies.

Thus, multilateral dispute settlement, as strengthened in the Uruguay Round, offers numerous advantages over the binational panel process from the perspective of Canadian interests:

- Panels are staffed by trade diplomats or experts drawn from countries not party to the dispute (unless the parties themselves agree otherwise). So the nationality of the panelists is not an issue in assessing the legitimacy of a ruling.
- Each country's government has carriage of the case. Many countries do hire outside lawyers in these cases, but Canada's federal government and provinces, taken together, have some of the best trade law experts in the world already on staff, and they have proven adept at arguing the Canadian case in these forums (although consultants' reports have sometimes been necessary).
- Since rulings can no longer be legally vetoed by the losing party, walking away from a ruling by a WTO dispute panel is like walking away from the legal judgment of the world community. Legitimacy is enhanced by the establishment of an appeals body where distinguished specialists can assess claims that the panel erred in law.
- The standards and benchmarks employed in WTO dispute settlement are rules of international, not domestic, law, so the suspicions that exist when nationals of one country interpret the law of another cannot arise.
- Precisely because the standards and benchmarks are international, the US Congress cannot change the law to reverse a panel decision that has been unsuccessfully appealed. As part of a compromise that allowed Congress to vote in favor of implementing the WTO agreements, the United States did set up a mechanism to scrutinize adverse dispute rulings, but the worst that can happen in the event of negative findings is a congressional resolution of censure or a call for US withdrawal from the WTO — both of which are unlikely.

Disciplining US Administered Protection

Can Canada use the WTO dispute settlement process to defend its industries from overly zealous US trade "protection"? Even superior dispute procedures will not constitute an attractive alternative to the binational panel process unless the WTO dispute panels can apply legal standards and benchmarks guaranteeing scrutiny of the coherence and evidentiary basis of US agency decisions that is at least as effective as the standard of review employed by the binational panels.

I believe the WTO agreements on subsidies and dumping create this situation.

The WTO Agreements

Neither the Agreement on Subsidies nor the Agreement on Dumping embodies the concept that decisions made under it must accord with the law of the country imposing the duties. Yet by providing broad but increasingly precise definitions of concepts such as "subsidy," "dumping," and "material injury," as well as in various respects emphasizing the requirement of proof or convincing evidence, these agreements, taken as a whole, provide a number of important benchmarks against which controversial US agency determinations may be scrutinized.

(These benchmarks have largely been entrenched in US domestic law, so the point here is not that WTO law is better law as such, but that Canada may be better off invoking benchmarks as *international* law rules before a genuinely international body that is not bound by US judicial interpretations of the benchmarks.)

Subsidies and Countervailing Duties

The case of subsidies and countervailing duties is the clearest. The WTO agreement sets out a number of criteria that must be present for a subsidy to be actionable (the subject of either a multilateral complaint or a successful countervail action).

First, the subsidy must conform to the definition stated in Article 1, which makes it clear that a subsidy must involve a disbursement or financial payment by a government or an exemption from revenue otherwise owed government (for instance, a tax credit).

The Canadian stumpage practices at issue in the *Softwood Lumber* case likely would have fallen outside this definition altogether, since log and lumber producers received no financial payment and were not exempted from paying revenue otherwise due under some general taxation scheme or statute. The only possible argument would be that stumpage is a good or service the government provides without “adequate remuneration” (Articles 2.3 and 14). But general infrastructure is exempted from this meaning of subsidy.

Also, the definition requires that a “benefit” be conferred. In the market distortion argument of *Softwood Lumber*, the theoretical and empirical studies that Canada presented and the United States did not refute, showed that stumpage fees did not affect the quantity or price of logs supplied to the softwood lumber industry and therefore did not confer any recognizable benefit on that industry (even if they did reduce the costs of *log* producers).

Moreover, the Agreement on Subsidies states that, when government provides goods and services,

> the adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale). (Article 14 (d).)

This is, of course, what the Canadian empirical studies examined, coming to the never-refuted conclusion that lumber producers were not, in effect, receiving a benefit.[25]

We thus need go no further than the agreement’s definition of subsidies to see that, if Canada were to gain its courage and terminate voluntary restrictions on lumber exports to the United States, it could make a very powerful appeal to the WTO in any future countervail action — one that could not possibly be impugned by the kind of claims Judge Wilkey made in his extraordinary challenge opinion.

Moreover, Article 2 of the agreement sets out specificity as a requirement for actionability, and the criteria given for a finding of *de facto* specificity are very similar to those employed in US trade law. Thus, the same arguments about specificity litigated by the binational panels can now be litigated on the basis of a truly international benchmark at the WTO.

And whatever one may think of Judge Wilkey’s or the *Lumber III* dissent’s view that figuring out specificity is inherently a judgment call to which wide discretion should be afforded, the WTO takes a different view. The Agreement on Subsidies states:

> Any determination of specificity under the provisions of this Article shall ***be clearly substantiated on the basis of positive evidence.*** (Article 2.4, emphasis added.)

The agreement has many other provisions, of course, including criteria for determination of material injury.

Antidumping Actions

In the case of antidumping actions, the Uruguay Round did not lead to substantial clarification of legal standards or benchmarks in the way that it did for subsidies. But the Agreement on Dumping has a number of provisions that imply the requirement that important determinations be based on sound evidence.

In the case of injury, for example, it requires

> an evaluation of *all* relevant economic factors and indices having a bearing on the state of the industry. (Article 3.4, emphasis added.)

And it states that the

> demonstration of a causal relationship between the dumped imports and the injury to the domestic industry shall be based on an examination of all relevant evidence before the authorities. (Article 3.5.)

In effect, with respect to the major issues in injury determinations, the WTO agreement imposes a standard at least as rigorous as the "substantial evidence on the record" standard in US administrative law.

This may be precisely why the United States insisted on including, in the Agreement on Dumping, provisions that, in effect, make its domestic benchmarks the WTO's benchmarks for review. Thus, the agreement states that panels, in reviewing the factual determinations of domestic agencies, shall defer to the agencies

> if the establishment of the facts was proper and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion (Article 17.6(i))

and, where a provision of the WTO agreement

> admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the agreement if its rests upon one of those possible interpretations. (Article 17.6(ii).)

While the United States may have gained something by having its own standards put into an international agreement, it can hardly now complain that they are being interpreted by foreigners who do not understand US law. The standards are now a rule of *international* law.

This point is actually underscored by another part of Article 17.6(ii):

> the panel shall interpret the relevant provisions of the Agreement in accordance with the customary rules of interpretation of public international law.

In fact, a leading expert on antidumping law, David Palmeter, argues that, if the rest of Article 17.6(ii) is itself interpreted in light of these customary rules, then the panels will not operate as deferentially as the United States expects since, under international law rules of treaty interpretation, the only permissible interpretation of international law is the correct or proper interpretation![26]

The Possibilities for Canada

To show the possibilities for WTO dispute settlement in Canada-US disputes with respect to countervail and antidumping, I have considered the binational panel proceedings completed up to and including *Softwood Lumber* in which Canada was the complainant or main complainant, identified the main issues that were in dispute concerning the soundness of US agency decisions, and isolated those provisions in the WTO agreements that might have been invoked to resolve those issues under the

Table 1: *Issues in Dispute in Chapter 19 Binational Panel Proceedings with Canada as Complainant, 1989–94*

Case	Determination[a]	Issue	Applicable WTO Law
Raspberries	AD/dumping	Justification for ignoring home market sales in determination of dumping	Dumping Agreement, Article 2.2 and accompanying fn. 2
Paving Equipment (6th admin. review)	AD/dumping	Use of best available information to calculate dumping margin in absence of timely response from petitioner	Dumping Agreement, Articles 6.1, 6.8
Steel Rails	CVD/subsidy	Specificity; treatment of equity infusions and loan guarantees	Subsidies Agreement, Articles 1.(a)(1)(i), 2.1(c), 14
	CVD/injury	Factors affecting determination of injury and weight attached thereto	Subsidies Agreement. Articles 15.5, 15.7
Pork	CVD/subsidy	Specificity; evidence of subsidization	Subsidies Agreement, Articles 2.1(c), 2.4
	CVD/injury	Factors affecting determination of injury and weight attached thereto	Subsidies Agreement, Articles 5, 15.5, 15.7
Magnesium	CVD/subsidy	Specificity; definition of countervailable subsidy	Subsidies Agreement, Articles 1, 2.1(c), 14
	CVD/injury	Definition of "like product" for purposes of injury determination	Subsidies Agreement, Article 15.1 and accompanying fn. 46
Live Swine	CVD/subsidy	Specificity: definition of countervailable subsidy	Subsidies Agreement, Article 2.1(c)
Softwood Lumber III	CVD/subsidy	Specificity; definition of countervailable subsidy	Subsidies Agreement, Articles 1.1(a)(1)(ii) and (iii), 1.1(b), 2.1(c), 14(d)
	CVD/injury	Requirement that causal relationship be established between subsidization and injury; factors to be considered in so finding	Subsidies Agreement, Article 15.5

[a] AD stands for *antidumping*, CVD for *countervailing duty*.

WTO process had those agreements been in force at the time.

The results, presented in Table 1, suggest that, in each dispute, the current WTO agreements would have provided legal benchmarks against which the coherence and evidentiary basis of US agency decisions could have been evaluated and the legal controversies between Canada and the United States resolved.

This analysis is not exhaustive since I have canvassed only what I consider the main issues in each case and the main provisions of the WTO agreements that would be applicable today. But the *prima facie* case for the utility of WTO dispute settlement emerges clearly.

Conclusion

Given my assessment of Chapter 19 dispute settlement in the FTA and the NAFTA, I suggest the following three-track strategy for settling trade disputes with the United States over the application of antidumping and countervailing duties to Canadian exports.

Use the NAFTA process for routine cases. In relatively routine or uncontroversial cases, the binational panel process of Chapter 19 appears to be working quite well. In these cases, which typically do not involve large dollar amounts or major conceptual issues in legal interpretation, the process has been useful in providing

Canadian exporters who wish to challenge US agency determinations a remedy speedier than that previously available through appeal to the US Court of International Trade.

Moreover, the legal and economic analysis in these decisions is generally and justifiably regarded as high. (This last observation may now have to be qualified due to the NAFTA text's emphasis on the appointment of judges, rather than trade law experts, to panels. Chapter 19 panels that have reported to date were constituted under the FTA rules, which allowed for the appointment of trade specialists to these bodies.)

The Chapter 19 process seems to have worked particularly well in antidumping actions.[27] Moreover, as noted earlier, the Uruguay Round Agreement on Dumping provided fewer bases for challenging US agency determinations under WTO rules than does, for example, the Agreement on Subsidies.

These observations argue for Canada's continuing to use the binational panel process for most antidumping cases and for countervail cases that are fairly routine and politically uncontroversial. This strategy makes particular sense since using government resources to take such cases to the WTO seems wasteful, given that what are mostly at stake are particular commercial interests, rather than broad questions of trade law and policy.

Negotiate improvements to the NAFTA process. As the accession of new members to the NAFTA is negotiated, Canada should press for changes to address some of the weaknesses identified in this *Commentary* with respect to the existing binational panel process. For example, as proposed by Gastle and Castel,[28] Canada might argue for the replacement of *ad hoc* binational panels by a permanent tribunal of experts, which would provide the opportunity to give greater coherence and legitimacy to panel rulings. It is likely, however, given the trend visible with respect to the NAFTA itself, that the United States would insist the members of such a tribunal be generalist judges, not trade experts.

Another desirable reform, which would obviate the possibility of decisions being divided along national lines, would be to specify that the membership of Chapter 19 panels be multinational, rather than binational. This change would also increase the available pool of panelists in many cases, reducing conflict-of-interest problems, and would work increasingly well as more countries accede to the hemispheric free trade area.

Another possibility, suggested by Davey,[29] is to reduce the roster of possible panelists to a

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relatively small number of individuals who would be prepared to invest a considerable amount of time in hearing these matters, creating greater legitimacy and coherence.

Still another suggestion that has sometimes been mooted is establishing a permanent appeal tribunal, perhaps constituted not unlike the Appellate Body of the WTO, that would hear challenges to the legal interpretations of the panels. Under the NAFTA changes already discussed in this *Commentary*, the extraordinary challenge procedure may take on the character of an appeal. Therefore, replacing ECCs with a permanent appeal body may be an attractive proposition for Canada. Certainly, such an institution might well provide greater legitimacy to panel jurisprudence in the eyes of Americans.

Use the WTO process in complex cases. Most important, in complex cases with major stakes for the Canadian economy — especially subsidies cases in which the various benchmarks in the WTO Agreement on Subsidies particularly invite multilateral review — the United States' NAFTA partners may be better off simply not using the Chapter 19 process, and taking disputes to the WTO. This would be particularly the case in matters, such as *Softwood Lumber*, that involve high trade politics and considerable conceptual controversy.

Notes

I am grateful for comments on an earlier version by Stephen Clarkson, Larry Herman, Petros Mavroidis, Daniel Schwanen, Michael Trebilcock, and two other reviewers who wish to remain anonymous. All shortcomings are my own.

1 See Canada, Department of External Affairs, *Canadian Trade Negotiations* (Ottawa: Supply and Services Canada, 1986).

2 See T.M. Boddez and M.J. Trebilcock, *Unfinished Business: Reforming Trade Remedy Laws in North America*, Policy Study 17 (Toronto: C.D. Howe Institute, 1993). Of course, Canada also lost some panel decisions reviewing *Canadian* agency determinations, although in lesser proportion.

3 This brief summary of the procedure is based on the lengthier discussion in M.J. Trebilcock and R. Howse, *The Regulation of International Trade* (London; New York: Routledge, 1995), pp. 402–406.

4 A good, brief discussion of the standard of review is to be found in C.M. Gastle and J.-G. Castel, "Should the North American Free Trade Agreement Dispute Settlement Mechanism in Anti-Dumping and Countervailing Duty Cases Be Reformed in Light of Softwood Lumber III?" *Law and Policy in International Business* 26 (1995): 821. (Hereinafter, Gastle and Castel, "Dispute Settlement Mechanism.")

5 Boddez and Trebilcock, *Unfinished Business*, p. 153.

6 See, for example, G.N. Horlick and F.A. DeBusk, "The Functioning of FTA Dispute Resolution Panels," in L. Waverman, ed., *Negotiating and Implementing a North American Free Trade Agreement* (Vancouver: Fraser Institute, 1992).

7 J.M. Mercury, "Chapter 19 of the United States-Canada Free Trade Agreement 1989–1995: A Check on Administered Protection," *Northwestern Journal of International Law and Business* 15 (1995): 525, 529.

8 M.P. Ryan, "Court of International Trade Judges, Binational Panellists, and Judicial Review of U.S. Antidumping and Countervailing Duty Policies," *Journal of World Trade* 103 (1996): 119.

9 See W.J. Davey, *Pine and Swine* (Ottawa: Centre for Trade Policy and Law, 1996), p. 297.

10 As strongly reflected in Judge Wilkey's dissent in the extraordinary challenge. See *In re Certain Softwood Lumber Products from Canada*, No. ECC-94-1904-01USA, 1994 FTAPD LEXIS 11 (Binational Review) (August 3, 1994), 177–178.

11 See Gastle and Castel, "Dispute Settlement Mechanism," pp. 837–846.

12 *National Corn Growers Ass'n.* v. *Canada (Import Tribunal)*, [1990] 2 SCR 1320; *Bell Canada* v. *Canada* (CRTC), [1989] 1 SCR 1722.

13 *NAFTA Implementation Act*, HR Rep. No. 361, 103d Cong., 1st Sess. 75-76 (1993), as quoted in Gastle and Castel, "Dispute Settlement Mechanism," p. 838.

14 Davey, *Pine and Swine*, p. 279.

15 Proposed Regulations, para. 355.43(b), 54 *Fed. Reg.*, p. 23379.

16 In the Matter of Certain Softwood Lumber Products from Canada, Decision of the Panel, (May 6, 1993), U.S.A.-92-1904-01, p. 28.

17 See United States, Department of Commerce, International Trade Administration, Determination Pursuant to Binational Panel Remand (Washington, DC, September 17, 1993).

18 See William Nordhaus, Submission to the Binational Panel on Softwood Lumber; and William Nordhaus and Robert Litan, Submission to the Binational Panel on Softwood Lumber.

19 Another ground of the extraordinary challenge was that two of the Canadian panelists had undisclosed conflicts of interest. The majority of the ECC rejected this claim.

20 *In re Certain Softwood Lumber Products from Canada*, pp. 177–178.

21 See Gastle and Castel, "Dispute Settlement Mechanism," pp. 878–881.

22 Article 1902(d)(ii) of the NAFTA prohibits amendments that are inconsistent with the "object and purpose" of Chapter 19 and the NAFTA as a whole. "Object and purpose" are here ambiguously defined, on the one hand, as "fair and predictable conditions for the progressive liberalization of trade" and, on the other hand, as "maintaining effective and fair disciplines on unfair trade practices." While this provision might be available to challenge for instance an amendment that purported to create new procedural obstacles to bilateral panel review, it could hardly be invoked against changes to the substance of US trade remedy law since, under NAFTA Article 1907, the substance of this law is explicitly a matter for further discussions.

23 R. Hudec, D. Kennedy, and M. Sgarbossa, "A Statistical Profile of GATT Dispute Settlement Cases; 1949–1989," *Minnesota Journal of Global Trade* 1 (1993): 1–113.

24 Unpublished research by John Mercury, Faculty of Law, University of Toronto, 1994.

25 The Agreement on Subsidies does not dictate the use of a particular way to determine the amount of benefit a subsidy confers, but the method must take into account the factors listed that go to adequacy of compensation in the case of government provision of goods and services, and the method must itself be provided in legislation. Whether any given method properly reflected the guidelines in Article 14(d) would be an issue of interpretation of the facts. But any method that ignored or dismissed the matters analyzed by the Nordhaus study would likely fall afoul of the guidelines.

26 D. Palmeter, "A Commentary on the WTO Anti-Dumping Code," *Journal of World Trade* 30 (1996): 63–64.

27 As Davey observes, for example, in *Pine and Swine*, p. 135.

28 Gastle and Castel, "Dispute Settlement Mechanism."

29 Davey, Pine and Swine, chap. 12.

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