While Canada must be prepared to walk away from NAFTA talks if the U.S. insists on abandoning the Dispute Settlement Mechanism of Chapter 19, Paul Moen writes that other trade remedies might emerge from a creative approach to the talks. *Shutterstock photo*

Trade Remedies Under NAFTA:
STILL TIME FOR CANADA TO PIVOT TO OFFENCE

Paul Moen

While Canada has characterized the Chapter 19 dispute settlement provision of NAFTA as a bottom-line condition in the ongoing renegotiations, the United States has identified its elimination as equally imperative. While use of the mechanism has waned in recent years and some younger trade deals eschew trade remedies altogether, negotiator and trade expert Paul Moen suggests three possible ways to a compromise.

Canada must be prepared to walk away from talks if the United States insists on abandoning the dispute settlement mechanism for trade remedies in any new NAFTA. Its real and symbolic importance in underpinning the rule of law in NAFTA cannot be overstated. Just as certain U.S. claims about the unconstitutionality of the process were debunked during the original Free Trade Agreement (FTA) negotiations, similar arguments must be marshalled today. And as outlined below, Canada and

Mexico should also seize this opportunity to present several bold proposals on reforming trade remedies in the NAFTA zone.

On July 17, the United States Trade Representative (USTR) released its document outlining the U.S. priorities for renegotiating the NAFTA. In a section titled, "Trade Remedies," the USTR explicitly identifies elimination of the current dispute settlement mechanism. That goal is reinforced with the addition of the language that the U.S. will look to "preserve the ability of the United States to rigorously enforce its trade laws, including the anti-dumping, countervailing duty, and safeguard laws." Conversely, Canada and Mexico vigorously defend the dispute settlement mechanism and view it as essential to any new deal. With that, the battle lines on trade have been clearly drawn. But a closer examination of trade remedies in NAFTA might help parties bridge this big gap.

Trade remedies such as anti-dumping and countervailing measures are designed to protect domestic producers from imports that are priced below market or even below the cost of production. If unfair dumping or subsidies cause or threaten harm to competing businesses, governments may impose duties to offset the injury, which are then subject to rules-based dispute settlement under NAFTA and/or the World Trade Organization (WTO). Dispute settlement acts as a check and balance on the inherent protectionist bias of trade remedies. But the historical commitment of the United States to both NAFTA and WTO dispute settlement for anti-dumping and countervailing duty is now in doubt.

When Canada and the United States first launched free trade negotiations in 1986, Canada sought to exempt its exports from increasingly capricious U.S. trade remedies—especially in areas of pork, beer, steel and, of course, softwood lumber. When this proved unacceptable to the United States and prompted Canada to walk away from a deal at the eleventh hour, creative negotiators achieved an agreement on process. The result was a binding bi-national panel dispute settlement mechanism under Chapter 19, replacing domestic judicial review of government trade remedy action. The solution was rightly heralded by Prime Minister Brian Mulroney and other trade negotiators as a major step forward for the rule of law in Canada-U.S. trade.

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The Chapter 19 process was made permanent in NAFTA, and has generally worked well for Canada in providing incentives for negotiated settlements in sensitive areas such as softwood lumber. But a confluence of factors—including a populist backlash against trade, a series of adverse panel decisions and claims of unconstitutionality under U.S. law—are all underpinning the Trump administration's hard push to eliminate Chapter 19 in the current renegotiation.

In contrast, Mexico has stated its defence of Chapter 19. And Canada's foreign affairs minister, Chrystia Freeland, formally set out her government's six core negotiating objectives for NAFTA to make the trade agreement modern, progressive and appropriate to the concerns of the 21st century. Included in this list of objectives deemed to be in Canada's national interest alongside culture and supply management is "a process to ensure anti-dumping and countervailing duties are only applied fairly when truly warranted." It was a carefully worded objective.

Most commentary on the Canadian position has focused on how Chapter 19 is a "line in the sand" for which the Trudeau government would be prepared to walk away from talks. Some commentators have argued that Chapter 19 has run its course. For example, Robert Wolfe, professor emeritus at Queen's University School of Public Policy, argues that Canada has only litigated three cases in the past decade under Chapter 19 and that highly-integrated continental supply chains discourage litigants taking such action.

But one reason that the United States has not used Chapter 19 much likely has more to do with a lack of U.S. exporter competitiveness into the Canadian market vis-à-vis Chinese and other exporters. And with the NAFTA zone even more integrated than it was during the original FTA negotiations, the policy rationale to seek a mutual exemption from trade remedies is even stronger and appeals to the self-interest of the United States not to impose undue harm on its own producers and consumers. Let us build from here.

First, Canada and Mexico could resurrect Canada's original position in the FTA negotiations by seeking a trilateral mutual exemption from the application of each other's anti-dumping and countervailing duty actions. Trade remedies are blunt instruments in a continent characterized by seamless and sophisticated global supply chains. Indeed, safeguard action—a trade remedy measures taken to address certain import surges—is already exempted on a *prima facie* basis under NAFTA, which could be extended to anti-dumping and countervailing duty measures.

Looking around the world, Australia and New Zealand eliminated trade remedies action between their two countries as far back as 1993 under the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZERTA). ANZERTA not only elimi-

nates trade remedies but also empowers competition tribunals with jurisdiction over events in the other country where the competition issue covers both countries. Interestingly, the Canada-Chile Free Trade Agreement, as amended in 2017, does away with trade remedies.

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Second, given that the United States, Canada and Mexico all need to address third-country illegal dumping and subsidization, there may be a political incentive for the U.S. to agree on a common approach to manage trade remedies on products imported into the NAFTA zone. In its stated NAFTA renegotiation objectives, the USTR calls for promoting "cooperation among the trade remedies administrators of the NAFTA countries" and an "early warning import monitoring system for agreed sensitive products from non-NAFTA countries."

Given the high-profile trade remedy cases of imports from Asia, including Korea and China, these objectives could provide an added policy and political incentive for the United States, Canada and Mexico to negotiate a common regime to deal with dumping by non-NAFTA countries. Some business groups in Canada have highlighted this issue in their NAFTA submissions, and the initiative could find support among steel producers and unions on both sides of the border.

Third, as an interim step to move towards this goal, Canada and Mexico could propose a measure to temper the protectionist impact of trade remedies. One solution is a technical "lesser duty" rule in the application of domestic trade remedy law, which could consider the downstream impact of anti-dumping and countervailing duty action on workers and consumers on both sides of the border. The European Union has a "community interest" provision that looks at the downstream impact of imposing anti-dumping and countervailing duties. It is time for three countries that share the world's largest trading relationship to follow suit and consider the adoption of a similar public interest provision in NAFTA. Here is how it could work.

In the application of anti-dumping and countervailing duty law, there tends to be a mismatch between the offence and the corresponding penalty. In almost all cases, the duty levels exceed the extent of the harm. This gives domestic producers a windfall of protection, imposes higher costs on users and consumers, and results in a net loss to the economy.

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For example, in several rounds of the Canada-U.S. softwood lumber dispute, the U.S. consistently imposed anti-dumping and countervailing duties that overprotect U.S. lumber producers and unnecessarily raise the cost of residential construction and the price of homes for U.S. consumers. U.S. producer interests politically outweigh those of the construction industry and of consumers at large, despite Canada's challenging U.S. duties and winning repeatedly under NAFTA and WTO panels.

Applying the "lesser duty" rule would reduce duties to the level actually required to offset injury and would help move stakeholders toward the position of understanding that trade remedies are protective measures that impose more costs than benefits on the economy maintaining punitive duties. In the case of softwood lumber, the Trump administration might even be receptive to a lesser duty principle, given the branding of the president as a champion of the little guy for home buyers and construction workers, rather than sacrificing their interests to U.S. lumber producers.

For its part, the Trudeau government recently dramatically reduced the anti-dumping duty on drywall imports from the United States. Balanced against Canada's domestic (albeit foreign-owned) producers of drywall were the downstream users of drywall—namely contractors and others in the construction industry—many of whom were locked into long-term supply agreements. In the end, the government reduced the level of duty to an amount that would give succor to the downstream users, builders and potential home-owners, while still maintaining a level of duty which would compensate domestic producers for harm suffered.

Given the moving pieces in the current NAFTA talks, the highly-integrated nature of the NAFTA economy and our common cause in addressing illegal dumping and subsidies from other regions of the world, Canada, the United States and Mexico should use this opportunity to pivot to higher ground by proposing bold initiatives that might just work in a Trumpian 'art of the deal' world. P

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