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FTAA: A dangerous NAFTA-GATS hybrid

Canada's initial offer threatens vital interests

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Summary

On February 14, 2003 Canada publicly released its "ititial offer" to cover services and investment under the Free Trade Area of the Americas (FTAA). Canada's so-called offer is merely a list of draft reservations copied almost entirely verbatim from Canada's list of NAFTA reservations drawn up in 1994.

These draft reservations, together with previously-obtained drafts of the services and investment chapters,[1] indicate that the Canadian government is pursuing an FTAA that combines some of the worst features of the NAFTA investment chapter and the GATS services provisions.

The Canadian government clearly supports – despite some public rhetoric to the contrary – incorporating many of the most controversial features of the NAFTA investment chapter into the FTAA, including:

- investor-state dispute settlement,
- broad expropriation-compensation provisions,
- minimum standard of treatment rules, and
- performance requirements prohibitions.

Moreover, the draft FTAA services chapter also includes some significant "NAFTA-plus" provisions drawn from the GATS. For example:

- The FTAA services chapter (Article 7, Market access) would prohibit monopolies in all covered sectors, and
- the FTAA services chapter (Article 5) would apply national treatment to subsidies (by contrast, subsidies are exempted from NAFTA's national treatment rule).

The impacts of these NAFTA-plus features drawn from the GATS would be compounded by the approach, strongly supported by Canada, that the FTAA services chapter be "top-down."

Combining these tough NAFTA-plus provisions with a top-down approach dictates that Canada take a fresh, serious look for potentially non-conforming measures and develop appropriate new reservations. Incredibly, however, Canada's initial offer does not include *any* new reservations designed to protect Canadian measures that are inconsistent with these "NAFTA-plus" features. For example, there is no reservation exempting Canada Post's monopoly from the FTAA.

Moreover, Canada's experience with NAFTA's investment chapter has been negative. (Investors have challenged a broad range of important Canadian public policies. There have been at least 8 investor-state cases against Canada and in each decided case the investor's claim has been at least partially upheld.) These serious problems with NAFTA investor-state also suggest that Canada should take a different approach to reservations than was taken under NAFTA. For example, Canada's NAFTA reservation for health and social services has been strongly criticized, including most recently by expert research for the Romanow commission. Nev-

ertheless, Canada's FTAA reservation for health and social services is a carbon copy of the flawed NAFTA reservation.

In short, despite the new challenges posed by NAFTA-plus services provisions in the draft FTAA and the existing problems with NAFTA investor-state, Canada's "initial offer" simply recycles its outdated and flawed list of NAFTA reservations. This borders on incompetence and contempt for important public interests.

Background:

Canada's "initial FTAA offer in services and investment" is simply a preliminary list of reservations that replicates, with very few changes, Canada's list of NAFTA reservations.

The list of proposed FTAA reservations, which were posted on the DFAIT web site (http://www.dfait-maeci.gc.ca/tna-nac/ftaa_neg-en.asp) on February 14, 2003, assumes that both the investment and services chapters will be "top-down," that is, that all sectors and government measures are covered unless they are specifically exempted.

Reservations are country-specific exceptions. They exclude only the listed measures of the country making the reservation. Following the NAFTA model, there are two types of proposed reservations, unbound (Annex II) and bound (Annex I).

Annex I, or bound, reservations exempt existing, non-conforming measures. Such measures could only be changed to make them less FTAA-inconsistent. If a measure were changed, or eliminated, the protection afforded by the Annex I reservation would also disappear. In other words, as is the case in NAFTA, they would be subject to a ratchet effect.

Annex II, or unbound reservations, usually apply to sectors not specific measures. They are intended to provide the flexibility to introduce new, otherwise non-conforming, measures. They are not subject to a ratchet effect. New, otherwise inconsistent, measures can be introduced in these sectors *so long as they meet the terms of the reservation*.

As the federal government's note explaining the initial offer indicates, the proposed reservations only provide protection against certain articles (national treatment, MFN, local presence, performance requirements ***and/or*** Senior management and board of directors). For example, in Canada' proposed approach, it is not possible to reserve measures against challenge under the controversial expropriation or minimum standard of treatment provisions. All measures in any sector (with the probable exception of national security measures) would be fully exposed to such challenges.

Discussion:

"NAFTA-plus" services provisions

As noted, there are significant differences between the substantive provisions of the NAFTA services chapter and the proposed FTAA text. The FTAA draft contains bracketed language which, for example, reflects GATS-style prohibitions on market access restrictions (Article 7, Market access) that, among other things, prohibit monopolies in covered sectors. The draft FTAA chapter would also extend national treatment to subsidies. Neither of these provisions are part of the NAFTA, yet Canada's proposed list of reservations does not include any additional protection against these more restrictive obligations. (Although much of the FTAA services chapter is bracketed, it is almost certain that any FTAA would include, at a minimum, all existing GATS obligations. Every country in the FTA negotiations is already a GATS signatory.)

Moreover, because Canada explicitly adopts a top-down approach to the FTAA services and investment chapters, the impact of the GATS-style provisions would be more sweeping than under the GATS. Under the

GATS, market access rules and national treatment rules apply only to listed services (a bottom-up approach). To take just one obvious example, there is no proposed FTAA reservation for Canada Post's monopoly over letter-mail services even though monopolies would clearly be prohibited in all sectors. Nor is there any reservation protecting Canada's flexibility to provide subsidies exclusively to Canadians. Canada's proposed FTAA reservations are clearly inappropriate and inadequate.

The draft FTAA services chapter also includes restrictions on non-discriminatory domestic regulation modeled after the GATS controversial Article VI. It is not a foregone conclusion that these restrictions would be part of a final FTAA services text. But if they were, and they were applied on a top-down basis, they would pose a very serious threat to a vast range of public interest regulations. There is nothing in the proposed list of Canadian reservations that would protect Canadian public interest regulations against challenge under such provisions.

In the case of services, Canada could have sidestepped the risks of investor-state challenges simply by going along with the majority position that investment (commercial presence) in services should be dealt with under the services chapter (which is not subject to investor-state). Supporting a positive list approach would also provide greater flexibility to exclude sectors such as health, education, social services, postal services and culture from the services provisions. Instead, Canada has insisted on a top-down, negative-list approach and its proposed reservations are made on that assumption.

The draft FTAA reservations list

Annex II

The Annex II reservations are almost identical to those in NAFTA. The very few differences include:

- The draft telecommunications reservation is somewhat narrower, probably reflecting domestic regulatory changes since 1994.

- The draft air transportation reservation is somewhat broader, apparently replacing I-C-32 an annex I reservation under NAFTA. The proposed FTAA reservation would provide protection for future measures, while NAFTA's I-C-32 protects only existing measures.

Annex I

The Annex I list is also nearly identical to that contained in NAFTA.

The only significant difference is more illusory than real. Canada asserts that its initial offer pertains to federal measures alone: "This document is premised on the non-application of the investment and cross-border trade in services provisions of the Agreement to measures of sub-national entities." Based on previous Canadian experience, this qualification is a ploy to avoid a jurisdictional squabble with the provinces (or to provide both levels of government 'political cover') until the deal is signed, sealed and delivered.

The FTAA's investment and services chapters will almost certainly apply to subnational measures. At the appropriate moment, Canada (in concert with the US and with or without the consent of Canadian provinces and territorial governments) will likely propose a general reservation excluding all existing non-conforming provincial and local measures (as of the date the FTAA comes into effect) from certain key provisions of the FTAA. Canada's initial offers in the MAI were made with the same qualification and on the same premises.

Like the corresponding NAFTA general Annex I reservation, the FTAA general reservation would not protect the future policy flexibility of provincial and local governments. Only existing, non-conforming meas-

ures would be exempted and then only from certain provisions on the FTAA investment and services chapters (for example, there are no federal reservations against the controversial expropriation provisions.) Subnational governments would, however, benefit from the cover provided by Canada's Annex II reservations, which do protect future policy flexibility to some extent (see discussion below for shortcomings of the Annex II reservations).

The health and social services reservation (Annex II-C-9)

In explaining the offers, the federal government claims that "the Government's position on health, social services and public education has always been very clear: they are not negotiable." But the FTAA offers rely on the flawed NAFTA-style Annex II-C-9 reservation. The problems with Annex II-C-9 (raised most recently by the Romanow Commission report) include:

- Canada's proposed sectoral reservation for health care only applies to health services "to the extent that they are social services established or maintained for a public purpose" (Annex II-C-9). One very serious shortcoming of this wording is that as the private element in the financing or delivery of a health service increases, the protection afforded by the reservation diminishes.

- As noted above, the proposed reservation doesn't apply to several of the FTAA's most problematic provisions, including those dealing with expropriation and compensation, minimum standards of treatment and performance requirements.

- "This piece-meal and qualified approach creates real vulnerability to NAFTA challenges and investor claims." (Steven Shrybman)[2]

- The exposure of the education sector is even more extreme. Canada's proposed reservation only applies to "public education." Private education is fully exposed. Merely protecting "public education" as opposed to "education:"
  - risks "possible spillovers on the public [education] system... if Canada liberalized services and investment in some private [education] services" in the sector,
  - fails to recognize "the mix of public/private sectors in the [education] system," and
  - fails to recognize "the importance of maximizing governments' policy flexibility for present and future [education] system reforms."[3]

- Reservations, as derogations to a treaty, will be interpreted narrowly by dispute panels.

- A serious drawback of reservations is that if any future federal government withdraws, or trades away, a reservation, then it can never be reinstated. By contrast, general exceptions can only be changed by agreement of all parties to a treaty and consequently are far more permanent and durable than reservations.

Canada's trade negotiators have apparently learned nothing from the problems with NAFTA's investment chapter nor from concerns about trade treaty risks to health and other public services. All they've done is cut and pasted the NAFTA reservations into the proposed FTAA.

Canada has proposed the very same reservations as in the NAFTA, despite some very significant concerns that have been raised about the effectiveness of these reservations, including Annex II-C-9. It is important to stress that this is a *Canadian* offer; Canadian negotiators are free to put forward anything they want. They should be able to do much

better than simply slavishly copying the flawed NAFTA reservations.

As *Putting Health First,* a research report prepared for the Romanow Commission, argued: "Canada should not rely exclusively on country-specific exceptions for health, which have significant shortcomings and should only be regarded as stopgap measures. Instead, Canada should pursue generally agreed exceptions or safeguards—permanent features of treaties that are far more likely to endure over time. Canadians deserve permanent protections for health care that are embedded in the very foundation of its international trade and investment agreements."[4]

Cultural diversity

Canada's approach to culture in the FTAA implicitly emphasizes the greater flexibility and durability of a general exception applying to the entire agreement and to every signatory.

> "In addition, additional exceptions that would apply to the entire Agreement and to every signatory can also be negotiated during the course of the negotiations. For example, as is the case in Canada's existing bilateral agreements, Canada's objective is to ensure a cultural exception that maintains maximum flexibility to pursue cultural policy objectives. Canada is also using the occasion of the FTAA negotiations to promote recognition of the importance of preserving cultural diversity and to build support for a binding international instrument in this regard. Canada has therefore tabled language to this effect for inclusion in the Preamble to the Agreement."[5]

The proposal for preambular language would clearly, in itself, not be sufficient to achieve maximum flexibility. But seeking a general exception that fully safeguards the flexibility not just to pursue but to *meet* cultural policy objectives — while at the same time building support for a binding international instrument protecting and promoting cultural diversity, that is negotiated outside the FTAA — is a better strategy than relying exclusively on country-specific reservations.

The Romanow commission recommended a similar approach to protecting Canada's health care system when it called on the federal government to: "Take clear and immediate steps to protect Canada's health care system from possible challenges under international law and trade agreements and to build alliances within the international community."[6]

Endnotes

1. The November 1, 2002 drafts of the FTAAA services and investment chapters are available at http://www.dfait-maeci.gc.ca/tna-nac/ftaa_neg-en.asp.
2. Steven Shrybman, *A Legal Opinion Concerning NAFTA Investment and Services Disciplines and Bill 11: Proposals by Alberta to Privatize the Delivery of Certain Insured Health Care Services,* March 2000.
3. These points are drawn from a presentation by Jake Velinga of Health Canada emphasizing the importance of broadly reserving "health" rather than "public health." They highlight, by analogy, the shortcomings of the decision to reserve public education rather than education, more broadly. See Jake Velinga, International affairs, Health Canada, presentation to the WHO forum on GATS and Health, Jan. 9-11, 2002, available at http://unstats.un.org/unsd/tradeserv/docs/who2002/who2002index.htm.
4. *Putting Health First*, Canadian Centre for Policy Alternatives Consortium on Globalization and Health, October 2002, available at www.policyalternatives.ca.
5. See *Cultural Diversity in the FTAA—Canada's position*, available at http://www.dfait-maeci.gc.ca/tna-nac/ftaa_neg-en.asp.
6. Commission on the Future of Health Care in Canada, *Building on Values: The Future of Health Care in Canada*, p. 233 (Ottawa, November 2003).

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