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Discussion

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DISCUSSION AFTER THE SPEECHES OF MATTHEW P. SCHAEFER AND JAMES P. MCILROY

QUESTION, PROFESSOR KING: Is this the type of thing where suddenly there will be an eruption because some bad thing happened that the provinces or states did? Is that going to excite people? We know it is a problem. Everybody agrees it is a problem. But what is going to bring it to a head?

ANSWER, MR. MCILROY: Maybe I can take a quick stab at that. At their meeting last year, the Canadian Premiers addressed this issue, and I understand they will be coming forward with some kind of a paper suggesting how the provinces can become more involved in the international trade negotiation process, which means they are exploring that first option that I mentioned.

I do not think the problem is fully being addressed. I think the provinces seem to be taking a lead on it. I would like to thank Matt for also pointing out another problem, which was the fact that the Canadian provinces just did not come forward with any kind of offers on the GATT procurement code. I think there are a lot of people wondering why that did not happen. I think the key point is that in Canada we have two problems: we have the problem of judicial authority, along with the problem of political authority. You folks in the United States are dealing with the issue of unanimous consent. You do not need it. In Canada we are still not sure whether we need unanimous consent. I think we need a couple more real problems to emerge before this issue comes to the floor. But, as I say, the Annex I issue was bungled last year. The latest one is the failure that provinces conform. We have procurement code offers. So there is a pattern starting to emerge. I would say within the next two to three years this should be addressed.

COMMENT, PROFESSOR SCHAEFER: You see this in the linkages area in the environmental community. We saw that the last panel does not really understand the trade community. I think you also see that, between state and provincial governments, governors tend to be more outward-looking. They have been involved in export programs. They see the political benefits of jobs much more readily than some other elected and un-elected state officials. And I think it is just going to take an enhanced awareness on behalf of some of the other state

officials of just how important this is. I do not know how you go about doing that. Like I said, it may take a crisis or it may just take time.

QUESTION, MS. LORRAINE EDEN: I am struck by the comparison between the ability of Canada and the United States to negotiate international tax treaties and the problems in international trade treaties.

It seems Canada has both the right and the ability to implement an international tax. At least there has not been the same problem at the federal level in terms of establishing bases and rates and withholding taxes. Yet there is the problem at the trade level. Maybe it is simply because these things have not gotten into the cross-border area the way they have at the trade level.

I think about the same thing in the United States. For example, California faced the worldwide tax in the *Barkley's Bank* case, where both the Clinton Administration and the Bush Administration were really reluctant to get involved. It seemed to me they were caught because the U.K. was saying on one side, we are going to withhold benefits to you under the U.S./U.K. tax treaty, and at the same time they really wanted to support California's right in this. I wondered if you had given any thought about the same thing regarding federal/state in terms of the tax treaty versus trade.

ANSWER, PROFESSOR SCHAEFER: Actually the taxation issues specifically related to the GATS were some of the more controversial in the Uruguay Round from the state perspective because GATS does not address most direct taxation. It only addresses indirect sales tax. GATS, on the other hand, does address direct taxation. So there is some concern about what GATS means for unitary taxation practices like the one in California. There is an exception. I believe it is in Article 14 of the GATS for apportionment formulas. But there was still concern after reading the exception. And then the chairman of the negotiating group in GATS created an interpretation in an unofficial document. But, there was still concern after that.

So what you will find is that the statement of administrative action states that unitary taxation is okay under the GATS. It is attached to the U.S. implementing bill that makes the statement of administrative action the authoritative interpretation of the GATS for purposes of any action by the federal government against a state to enforce the Uruguay Round agreement.

So the tax administrators and the tax community were aware that this might be an end-run because what happens in most U.S. tax treaties is that sub-federal jurisdictions are exempted from it. The U.K./U.S. treaty nearly died until there was a reservation put in for the sub-federal jurisdictions.

The other thing I would question, in terms of other forums, is the multilateral investment agreement going on in the Organization for Economic Cooperation and Development (OECD). Are they going to list specific reservations and how do they handle sub-federals? Well, it did not even work out in NAFTA. Are they going to attempt to do the same thing in the OECD under the Multilateral Agreement on Investment (MAI), list specific state and provincial exemptions from the MAI or are they going to have to grandfather all existing nonconforming measures without specific identification? The same issue is going to arise.

COMMENT, MR. HERMAN: You are right about Article 1206 and Annex I, but I would not make too much of it. It was purely pragmatic. The problem was that the provinces started listing everything, and a solution was found that dealt with it pragmatically. I would not read too much into that.

As for the federal/state issues, under treaty law when a federal state, absent a federal/state clause, ratifies an international treaty, the state is bound to it. A question arises with the subunits. Neither of you mentioned four important GATT cases: gold coins un-adopted, two pending provincial liquor board cases, and what you call *Beer II*, the U.S. equivalent of the liquor board cases.

In all four cases, the GATT dealt with provincial or state laws, laws that were inconsistent with GATT. They treated those laws as if the provinces and the states were bound in every sense as the federal government was bound. In other words, while it was raised in the gold coins case and in the first provincial marketing boards case, the panel said we do not care if we are talking about provincial laws or measures, we are going to construe those laws in the same way we would construe them as if they were passed by a unitary state. So I would argue that in trade agreements, the issue of state adherence as separate entities is irrelevant. The fact is that the federal state is bound, and that, in turn, binds the subunits. At least that is what the four GATT cases tell us.

COMMENT, MR. McILROY: We talked about this earlier. You try to get your pianos into the market and you cannot. You have a right to retaliate, and at the end of the day you feel pretty good about the retaliation, but your pianos still are not being sold.

I think that in a case where a province says to the feds that they are not changing their law, you can hammer the federal government. Your client is still in a position where the provincial government can state they are not bound by what the government of Canada negotiated; the government of Canada, may be on the hook, but so what?

I think we are going to see something interesting in these Chapter

11 investment disputes, if they ever go anywhere. If an arbitration panel says "yes, that is a violation," and the province says, "so what, we are not paying," Ottawa will have to write a check for an action over which it is responsible, and over which it has no authority. I think that Ottawa is going to become reluctant to put itself on the hook. This GATT procurement code issue is a very good example. That is basically where you say to the provinces if you want to sign on, sign on. Look at the environmental agreement. The last time I looked at the NAFTA side agreement on the environment, do you know how many provinces had signed on? Alberta and Quebec, two provinces.

I sense that what has already happened with the United States and with the discussions with the E.U. on GATT procurement is that the next time we all shuffle to the table and sit down, the E.U. is going to tell Canada, then maybe they should not be sitting at the table because everyone is there to talk about subunits, and Canada does not have much of a track record in delivering their subunits, so maybe they should sit out this session. I do not think we are there yet, but I do see a pattern emerging.

I agree with you that it was a good pragmatic solution to the Annex I problem. I guess what concerns me is that they had two years and an extra three months, and they still could not deliver the goods. That worries me. I think there is a systemic problem there. Is it that the provinces do not want to do it? Is it that the provinces do not have the horses to do it? I think the states are very good at export promotion, as are the provinces. That has been their game. But trade policy is a new game for them. Do they have the horses, and do they have the people in place? I do not know. Right now I do not think they do.

I am not saying that the sky is falling and that we should all be running around like Chicken Little. All I am trying to say is that there has been a shift in the paradigm. I do not think the bureaucracies have shifted. I do not think that the provinces are equipped to deal with these problems. And I think at some point the feds are going to get reluctant to start signing on to these things. I totally agree with you. As far as a panel is concerned, a provincial law is covered by a treaty. But when the time comes for retaliation, whom do you hammer? The problem is that it is going to be Ottawa.

COMMENT, MR. HERMAN: I do not want to prolong this. The only point I would make is in *Beer I*, which, I think, is worthy of a detailed study. In *Beer I*, in the implementation phase, the Province of Ontario did not fully implement its obligations. The United States retaliated and applied quotas on the import of Ontario-brewed beer, not Canadian-brewed beer. So, they could be quite selective. Ontario, in turn,

stopped buying Stroh's beer, and they were quite selective, too. The point is there was a way in which this was worked out because Ontario products were targeted specifically in the withdrawal of benefit.

COMMENT, MR. McILROY: What would have happened if they had targeted Quebec beer? I think then you would have had an interesting case.

COMMENT, MR. HERMAN: Yes.

COMMENT, PROFESSOR SCHAEFER: In fact, on this issue of retaliation, often it is difficult to target it for better jurisdiction. The United States was worried about this and shipping beer through other provinces, for one thing.

The European Union in the GATT Superfund case thought Lloyd Bentsen was responsible for an extra tax on imported petroleum, so they tried to target Texas products. They selected beef and a couple other things. But it is tough to do in a lot of cases. And the other thing that might happen is, say, there is a state that is found in violation. You do not want to target them; you want to target the state from where the Senate majority leader is so you get the bill introduced.

COMMENT, MR. O'GRADY: I would just make a quick commentary on this Schedule I thing. It seems to me that filling out the schedule and providing the information, which somebody at some point must have thought was important, is much more connected to the process of completing the negotiation of the treaty; that is, as they say in British constitutional cases, in pith and substance. It is much more a function of the federal power than any power the province might have to implement. So you would have thought that if the federal government was prepared to stand up to the provinces, which, of course, we know it is not, it would have said, look, you are required to do this and we will either take you to the Federal Court, which they would not do, I guess, or we will commission a professor or two and do it ourselves. You can tell us if you disagree, but otherwise we are going to file it. Perhaps the federal government was not properly fulfilling its role in the scheme of things.

COMMENT, MR. McNAB: I do not want to disagree with the premise that there are problems identified between getting the provinces and states to agree to or to implement obligations that have been negotiated by the federal government, but I think we might be reading a bit too much into the case of the provinces not coming forward with government in terms of offers. As I understand it, this was sort of the icing on the cake, as far as the United States was concerned, to try to get the large purchasers of a great number of services and equipment around the table. At the same time, the United States, again, as I understand it, was not ready to change the small business set-aside. So I think that focus was reflected in the decision of the provincial governments not to come forward with some of their offers.