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The Collision of Canadian and U.S. Sovereignty in the Area of Export Controls

Selma M. Lussenburg*

I. INTRODUCTION

This paper provides a Canadian perspective on those areas where potential conflicts may arise between business enterprises that carry on business in Canada and in the United States. Such conflicts tend to occur when interrelated corporate entities (i.e. subsidiary or other affiliate relationship) are subjected to conflicting legal requirements as a result of the extension of sovereignty beyond national boundaries. Extra-territorial application of export control laws has tended to be based on economic and foreign policy considerations. Those caught in the middle tend to be business enterprises whose primary objective is the expansion of trade or exports. These enterprises in many instances have been unaware of the extended scope of, for example, U.S. export control laws. The question of extra-territorial application of laws may also arise when a Canadian company, dealing at arm's length with a U.S. company, is required to sign a contract which contains a submission clause. Such clauses require the Canadian company to commit to adhering to existing and future U.S. export control laws and orders from U.S. export control authorities regarding the disposition of the products beyond Canada's border. All too often the Canadian contracting party is unfamiliar with the broad scope of U.S. export control legislation. U.S. goods incorporated into products in Canada or the manufacture of Canadian goods using U.S. technology destined for Cuba is the most notorious example.

In the context of Canadian sovereignty and export controls, two primary pieces of Canadian legislation must be considered. These are the Foreign Extraterritorial Measures Act (FEMA) which provides the Canadian government with authority to block the extra-territorial application of foreign anti-trust law and to block foreign trading directives and orders which adversely affect Canadian interests. The second is the Export and Import Permits Act (Export Act) which regulates

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1 R.S.C., ch. F-29 (1990) (Can.).

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the export of products from Canada and gives effect to Canada's international strategic commitments and foreign policy issues. While the Export Act is a statute with which many Canadians are familiar, the FEMA is relatively speaking less known. To date only limited action has been taken pursuant to the FEMA; such action, however, has been the source of controversy within the Canadian and the U.S. business community.

This paper will provide a brief overview of the primary provisions of the FEMA, the United States Order enacted pursuant to the FEMA, and it will discuss the implications of this confrontation of American and Canadian law for Canadian businesses trading with Cuba as well as the nature of Canada's export control regime and Canada's anti-boycott policy and legislation.

II. THE CUBA PROBLEM: CLEAR CONFLICT OF SOVEREIGNTY

The enactment in October 23, 1992 of the U.S. Cuban Democracy Act of 1992 and, in particular, section 17.06(a)(1) of the National Defense Authorization Act for the Fiscal Year 1993 (Cuba Act) brought to the foreground the conflict of sovereignty in the area of export controls. In this context the conflict centers on the differences in Canadian and American trading policy with respect to Cuba, and especially the extra-territorial application of the American-Cuban embargo program. While the United States has restricted trade with Cuba and with nationals thereof and has restricted financial transactions in which Cuba and nationals thereof have an interest since 1960, the Bush Administration extended the scope of existing restrictions to a complete ban of all trade with Cuba. The Clinton Administration has supported the Bush Administration's position.

U.S. legislation now prohibits trade and financial transactions not only between U.S. nationals and Cuba but also between U.S.-owned or controlled firms in third countries and Cuba. The latter prohibition was imposed by revoking the licensing mechanism set out in the Cuban Asset Control Regulations (Cuba Regulations), which previously permitted foreign subsidiaries of American nationals to continue to trade with Cuba within certain defined parameters. In direct contrast to the Canadian position, as a result of the Cuba Act, U.S.-owned and controlled firms in third countries are now prohibited under American law from exporting to and importing from Cuba any commodities irrespective of the strategic importance of the goods, the degree of independence exercised by the affiliate of the American corporation, the sourcing or

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5 The parameters are summarized infra Part IV(A).
transformation of the product in the third country, and the foreign policy of the third country. Canadian policy and legislation supports and promotes trade with Cuba.

This has had significant repercussions in Canada. The Canadian government has historically and continues to support Canadian trading activities with Cuba. In direct response to the Cuba Act, the Canadian government on the recommendation of the Attorney General of Canada and the Secretary of State for External Affairs issued the Foreign Extraterritorial Measures (United States) Order, 1992 (United States Order) on October 9, 1992. The United States Order blocks in Canada the extra-territorial application of the Cuba Act which prohibits, under United States law, trade with Cuba originating in Canada by any firm that is U.S.-owned or controlled.

The enactment of these two pieces of legislation in two different jurisdictions has placed the American officers and directors and management of U.S. corporations whose Canadian subsidiaries trade with Cuba and the Canadian subsidiary’s officers, directors and management in a difficult position with respect to conducting trade with Cuba particularly where an established trading relationship exists and new initiatives are underway or likely to arise.

III. THE FOREIGN EXTRATERRITORIAL MEASURES ACT

The enactment of the FEMA was in reaction to often expressed frustration with the extra-territorial application of U.S. export control laws. The FEMA is similar to blocking legislation enacted in other jurisdictions.

The thrust of FEMA is two-fold: it permits the Canadian government to limit the production and disclosure of documents and to block the extra-territorial application of foreign legislation or trading directives in circumstances where Canadian trading interests are adversely affected or Canadian sovereignty is infringed; and, it enables the Canadian government to restrict the application of foreign antitrust law.

A. Restriction of Production of Documents

FEMA provides that where, in the opinion of the Attorney General, a foreign tribunal has exercised, is exercising or is proposing or is likely to exercise jurisdiction or powers of a kind or in a manner that has adversely affected or is likely to adversely affect significant Canadian interests in relation to international trade or commerce involving a

* SOR/92-584 (1992), 126-22 C. Gaz. Part II.
* e.g., in the United Kingdom, The Protection of Trading Interests Act, 1980, ch. 16 (Eng.) and similar legislation in Australia.
* This includes any court, body, authority or person having authority to take or receive information.
business carried on in whole or in part in Canada or that otherwise has infringed or is likely to infringe Canadian sovereignty, the Attorney General may by order prohibit or restrict the production or disclosure of records\(^9\) to a foreign tribunal where such documentation is in the possession or in the control of a Canadian citizen or person resident in Canada.\(^{10}\) The Attorney General's powers extend to prohibiting or restricting the giving of information by Canadian citizens or residents of Canada before or for the purposes of a foreign tribunal in relation to the contents or identification of records in the possession or control of a Canadian citizen or person resident in Canada. The Attorney General thus has the power to "block" the application of subpoenas or other orders to produce evidence by foreign tribunals.

Subject to the existence of an order to restrict production or disclosure of documents, an order may be made by a superior Canadian court to issue a warrant to seize such records and to deliver them to the court or a person designated for safekeeping.\(^{11}\) The latter is only permitted where the Attorney General makes application to the court and the court is satisfied that the provisions of the order may not be complied with if the documents are not seized. This then permits the Canadian government to block or limit the foreign tribunal's capacity to obtain records to support the action before that tribunal.

\textbf{B. Blocking Orders}

The Attorney General of Canada (only with the concurrence of the Secretary of State for External Affairs) may make an order in circumstances where a foreign state or foreign tribunal has taken or is proposing or is likely to take measures affecting international trade or commerce of a kind or in a manner that has adversely affected or is likely to adversely affect significant Canadian interests in relation to international trade or commerce involving business carried on in whole or in part in Canada or that otherwise has infringed or is likely to infringe on Canadian sovereignty.\(^{12}\) That the concurrence of the Secretary of State for External Affairs is required is reflective of the fact that such orders may have significant foreign policy and trade ramifications. It is pursuant to this provision of FEMA that the United States Order was made.\(^{13}\) Prior to the enactment of the United States Order, Canada and a number of the United States' major trading partners

\footnotesize{\textsuperscript{9} The definition of "records" is extensive and includes any correspondence, memorandum, book, plan, map, drawing, film, microform, sound recording, videotape, machine readable record. \textsuperscript{10} R.C.S., ch. F-29, § 3(1) (1900) (Can.). \textsuperscript{11} Id. at § 4. \textsuperscript{12} Id. at § 5. \textsuperscript{13} A similar order was issued on October 15, 1992 (and made effective October 14, 1992) in the United Kingdom: The Protection of Trading Interests [US Cuban Assets Control Regulations] Order 1992. The substance of the United States Order is discussed infra Part IV(A).}
lobbied against the adoption of the Cuba Act. Once diplomatic overtures failed, Canada took action pursuant to this provision of FEMA.

The Attorney General is authorized to issue an order which can prohibit any person in Canada from complying with such measures or with any "directives, instructions, intonations of policy or other communications" relating to such measures from a person who is in a position to direct or influence the policies of the person in Canada. The application of the Order is not restricted to citizens or persons resident in Canada but extends to anyone who is physically present in Canada, irrespective of nationality. The Attorney General may require a person receiving such directives, instructions, intonations of policy or other communications to notify him of such communications. Measures taken or to be taken by a foreign state or foreign tribunal include "laws, judgments and rulings" made or to be made by the foreign state or foreign tribunal and directives, instructions, intonations of policy and other communications issued by or to be issued by the foreign state or foreign tribunal.

C. Penalties

A contravention of an order made pursuant to Sections 3 or 5 (described above) renders the person liable to conviction of an indictable offense and/or to a fine not exceeding $10,000 or to imprisonment for a term not exceeding 5 years or both or to conviction of an offense punishable on summary conviction and liable to a fine not exceeding $5,000 and/or to imprisonment for a term not exceeding two years or both. It is a precondition to prosecution under this provision that the order must have been served on the person against whom an action has been brought. FEMA provides for personal service on individuals or service on the manager, secretary or other executive officer in the case of corporations. Where a "class" of persons is involved (i.e., Canadian subsidiaries of U.S.-owned or controlled corporations), a superior Court may authorize service in such a manner as it deems appropriate. In the case of the United States Order, service was effected by means of substituted service through advertisements in Canadian newspapers. No proceedings may be made with respect to an offense under FEMA without the consent of Attorney General.

IV. THE UNITED STATES BLOCKING ORDER

On October 9, 1992, in direct response to the anticipated promulgation of the Cuba Act, the United States Order was issued. The

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14 FEMA, R.S.C., ch. F-29, §§ S(1)(a)-(b) (1990) (Can.).
15 Id. at § 7.
16 Id.
United States Order blocks in Canada the extra-territorial application of the Cuba Act. In 1990, the Canadian Government issued a similar order, but that order did not become operative because President Bush vetoed the relevant U.S. legislation.\(^\text{17}\) When it became apparent that President Bush would not veto the Cuba Act, the Canadian Government for the first time issued a blocking order under FEMA that has come into effect.

A. Background and Previously Existing Regime

The United States has historically restricted the trading activities of U.S. nationals with Cuba. In response to pressure from its trading partners, in 1974, the United States amended the Cuban Asset Control Regulations to establish a licensing mechanism to permit certain transactions between U.S.-owned or controlled firms in third countries and Cuba where local law or local policy favored trade with Cuba.\(^\text{18}\) While the text of this legislation has varied over the past 17 years, Canadian subsidiaries of U.S.-owned or controlled firms traded with Cuba either through the licensing mechanism or as a result of Canadian diplomatic intervention. United States trade with Cuba has historically been a sensitive issue and from time to time the pressure to prohibit even indirect trade by foreign subsidiaries of U.S.-owned or controlled firms has been intense, as was the case in 1990 and most recently in 1992. The decision by President Bush to approve legislation substantially the same as legislation he vetoed in 1990 is the result of election pressures and the power of Cuban-American voters who support a ban on trade with Cuba.

It is relevant to summarize the U.S. licensing mechanism which previously existed to understand the impact of the Cuba Act in Canada. The Cuban Regulations already limited exports by Canadian subsidiaries of U.S.-controlled or owned firms, but as in essence the scope was limited to U.S. origin goods, U.S. financing and strategic goods, they were not perceived to be extra-territorial in nature and did not offend Canadian sovereignty to the same degree as the Cuba Act. The licensing mechanism “permitted” Canadian subsidiaries of American nationals to export products produced in Canada provided that such products were non-strategic, that no U.S. origin technical data (other than maintenance, repair and operations data) would be trans-


\(^{18}\) 31 C.F.R. § 515 (1974). This intended to be only a summary of the U.S. position in this regard for the purpose of the following discussion. For a more in depth presentation, see John Ellicott, *Sovereignty and the Regulation of International Business in the Export Control Area*, 20 CAN.-U.S. L.J. 133-144 (1994).
ferred, and that if U.S. origin parts and components were included in the commodity, the inclusion thereof had been authorized by the Department of Commerce. A similar provision applied with respect to spares to be re-exported to Cuba in connection with a transaction for which a "license" had been granted. In addition, there was a requirement that no U.S. dollar accounts be involved, no financing or other credit be provided by the subsidiary and that payment be made on normal trade terms. American legislation precluded active participation by U.S. nationals in the trading activity of the Canadian subsidiary. Any assistance or participation by the U.S. parent firm or an officer or employee thereof in the negotiation or performance of the transaction which was the subject of an application for license was not acceptable and constituted grounds for denial of the license application or the revocation of an existing license. The legislation required the affiliate to be independent in the conduct of the Cuban trade related transactions in matters including, but not limited to, decision making, risk taking, negotiation, financing or the arranging of financing and the performance of the contract. While still an "infringement" of Canadian sovereignty, the impact of the pre-existing regime on American controlled Canadian businesses trading with Cuba was limited. In essence it imposed an additional administrative burden on such companies, but recognized Canadian sovereignty.

B. The Canadian Context

In contrast to the United States, subject to limited exceptions, Canada has maintained a strong trading relationship with Cuba and has consistently resisted efforts by third parties to restrain commercial initiatives of Canadian firms in Cuba or with Cubans. The Department of External Affairs has taken the position that Canada will continue to maintain normal trade relations with Cuba. Of Cuba's hard currency trading partners, Canada is the largest importer of Cuban products and the fourth largest exporter. Significant Canadian exports to Cuba include agri-food products (i.e., wheat, maize, fish, fowl), industrial products (i.e., air conditioning equipment and parts), paper products and telecommunications equipment.

The Cuba Regulations "permitted" Canadian subsidiaries of American nationals to export goods manufactured wholly in Canada or processed goods originating outside of the United States. The United States Order and the provisions of the FEMA pursuant to which the


20 Government of Canada, Department of External Affairs.

21 Id.
United States’ Order was made are reflective of the concept of Canadian control or independence. The threshold for the application of this provision of the FEMA is whether the measures affect international trade or commerce in a manner that adversely affects “significant Canadian interests . . . involving business carried on in whole or in part in Canada.”22 Canadian interests in Canada must be adversely affected. Canada thus cannot be used to circumvent the otherwise legitimate export controls of other countries. It will not sanction or act as the conduit for the illegal re-export of foreign produced goods which cannot be exported from the country of origin. However, where goods are produced domestically or reprocessed or transformed in Canada, the Canadian government (subject to its international commitments, such as COCOM)23 will not permit third country trading policy to dictate whether such goods can be exported; foreign ownership of the Canadian manufacturer or processor is insufficient reason for such trading policy to apply as it is Canada’s view that these are Canadian goods.

In the context of Canadian-Cuba trade, as a matter of practice, any export from Canada destined for Cuba requires the Canadian exporter to certify that no U.S. origin goods are being exported to Cuba.24 United States origin goods may only be re-exported from Canada with an export permit.25 If the product to be re-exported was of U.S. origin good, the practice of Customs and Excise, Canada was to require the Canadian exporter to provide evidence of the United States export permit. If no export licence had been issued, then generally speaking, the re-export from Canada would not be permitted as this represented in effect a re-export of U.S. goods without further processing or transformation.

C. The Order

The Canadian Government issued the United States Order on the basis that the Cuba Act has and will have a significant adverse affect on Canadian businesses in relation to international trade and commerce carried on in whole or in part in Canada and on the basis that the Cuba Act constitutes an infringement of Canadian sovereignty. The Canadian government estimated that this extra-territorial application of United States law could adversely affect approximately Cdn. $30

22 FEMA, R.S.C., ch. F-29 (1990) (Can.).
23 Canada participated with its NATO partners (except Iceland) along with Australia and Japan in the Coordinating Committee for Multilateral Strategic Controls [hereinafter COCOM]. COCOM members establish international lists of strategic goods and technologies, the export of which are controlled to COCOM proscribed destinations. For a further discussion of COCOM and its demise see infra Part VII(F).
24 This statement is found on the B13 export form used by Customs and Excise, Canada. See also the Export Permit Regulations, § 8.
25 Export Act, R.S.C., § 7 (1985) (Can.).
million of Canadian trade with Cuba annually as well as restrict potential opportunities for trade growth between Canada and Cuba.⁴⁶

The United States Order requires that every corporation registered or incorporated under Canadian law that carries on business in whole or in part in Canada and every officer of such corporation “who receives, in respect of any trade or commerce between Canada and Cuba, any directives, instructions, intimations of policy or other communications relating to an extra-territorial measure of the United States from a person who is in a position to direct or influence the policies of the corporation” must notify the Attorney General of Canada. An extra-territorial measure is specifically defined as the Cuba Act and thus the United States Order’s application is limited in scope.

The net effect for Canadian corporations that are owned or controlled by U.S. nationals is to require such corporations to ignore the fact that licenses will no longer be issued under the Cuba Regulations and to continue to trade with Cuba as if a license had been issued. Customs and Excise (Canada) will no longer demand evidence of U.S. export licenses, but will continue to ensure that only the products manufactured or produced in Canada or, if of U.S. origin, products transformed or reprocessed in Canada will be exported. The requirement to certify that no U.S. origin goods are included will remain the same.

Canadian corporations are required to report to the Canadian Government the receipt of any instructions from the United States aimed at regulating trading activities with Cuba, and a failure to do so renders the corporation and its officers and directors liable to prosecution. The United States Order is limited to corporations, their officers and directors. It does not extend to partnerships or natural persons.

V. IMPLICATIONS FOR CANADIAN SUBSIDIARIES AND CONFLICT OF SOVEREIGNTY

U.S.-owned or controlled Canadian corporations which have dealings with Cuba find themselves in an unenviable position when the conflicting legislation is considered. It is clear that in Canada, to the extent the Canadian subsidiaries’ trading activities with Cuba were permitted before the enactment of the Cuba Act, Canadian law requires such subsidiaries to continue to operate as if the Cuba Act does not exist. However, when the Canadian subsidiary continues with its Cuban trading activities, the U.S. parent company and its directors and officers are likely to be in breach of the Cuba Act and are thereby exposed to prosecution. If the Canadian subsidiary receives instructions from its American parent to cease its trading activities or voluntarily ceases its trading activities because of the obvious repercussions in the United States, such action is likely to result in a breach by the Cana-

⁴⁶ Government of Canada, Department of External Affairs.
dian company, its directors and officers of Canadian law. In addition to imposition of penalties and possible imprisonment, prosecution of the American parent corporation in the United States may result in the corporation being “black-listed” by the U.S. government. This means that U.S. government procurement contracts that may have been previously available are no longer likely to be available. Depending on the number of contracts with the American Government, this may be a more serious penalty than the actual fine.

While a large number of incidents involving a conflict between Canadian and American trade policy with respect to Cuba have in the past been resolved through diplomatic intervention, it is unclear whether this will be possible under the new regulatory regime as both countries appear to be intent on enforcing their respective laws. Prior to the enactment of the Cuba Act, Canada and a number of Western nations were unsuccessful in lobbying American authorities to avoid the application of the Cuba Act. Thus, it is unlikely that American nationals in breach of the Cuba Act as a result of the action of their Canadian subsidiaries will receive a sympathetic hearing.

The confrontation of American law and Canadian law is particularly problematic for individuals who serve as directors of both the Canadian corporation and the American corporation. The position of the Canadian government is clear and that is that it expects that Canadian subsidiaries of American nationals that have traditionally engaged in trading activities or are engaged in trading activities or are considering trading activities with Cuba to continue to do so. As soon as a Canadian director crosses the Canadian-American border to attend a directors’ meeting or to attend to other legitimate business in the United States, he is subject to the potential arrest by American authorities for a failure to comply with American law. Similar considerations apply to Americans who are directors of the U.S. parent corporation and directors of the Canadian subsidiary. To the extent that prosecutions occur in the United States, the Canadian Government may, under FEMA, restrict the production of documents situated in Canada which would assist in the American prosecution.

Is the answer that American directors of Canadian subsidiaries must resign to avoid possible prosecution in the United States? And vice versa for Canadians that serve on the boards of the American parent corporation? This is merely a cosmetic solution as it does not address the reality of the business relationship. The American parent may not be prepared to cede control of all operations to Canadian management. While there is no need in some cases to have parental controls, in other situations it is inevitable and sometimes desirable.

Situations where established trading relationship exists or negotiations suddenly break off are likely to be the subject of investigation by the Canadian Department of Justice and indeed some have been the
subject of investigation. Canadian management must carefully consider any decision to change established business or trading relationships with Cuba and should ensure that the commodities traded with Cuba are of "Canadian" and not American origin.

Any U.S. controlled Canadian corporation engaged in trading with Cuba will have to review carefully the ramifications of complying either with American law or Canadian law. It does not appear to be possible to do both. Multinationals considering trading with Cuba should analyze their international trading activities and form of business organization prior to commencing trading with Cuba. If possible, multinationals should structure their multinational trading in such a manner as to avoid the interposition of an American parent and to avoid indirect or direct American control of entities which are trading with Cuba. In some instances steps should be taken to reorganize existing intercorporate holdings. This will at least limit the problem to situations where Americans are the ultimate owners and not merely a conduit in a chain of intercorporate holdings.

VI. EXPORT CONTROLS

While the primary area of conflict between Canada and the United States at the present time relates to trade with Cuba, it is useful to briefly summarize Canada's export control regime.

Canada's exports (and imports) are controlled through the Export Act and related legislation which includes a trade sanctions regime and until recently included the Coordinating Committee for Multilateral Strategic Export Controls (COCOM) regime. While the latter used to play a significant role in the regulation of Canadian exports, due to the disintegration of the Soviet Bloc and other trade liberalizing measures, the COCOM regime has been replaced by a system of national controls. The primary focus thus in the text that follows is on the export control regime.27

VII. THE EXPORT CONTROL REGIME

Canadian exporters and businesses seeking to undertake expansion must weave their way through a relatively outmoded system of export controls whose origins, both nationally and internationally, date back to World War II and the Cold War. This continues to occur, despite substantial changes in the international economic and political environment over the last decade and an increase in the importance of the export market for Canadian companies. Reflective of the growing im-

27 This paper will not address import controls. Canada does have substantial legislation which deals with import controls which is regulated through the Export Act and related regulations.
portance of export markets for the Canadian economy, International Monetary Fund data recently released, illustrates that, although Canada’s economy accounts for 2% of global production, it accounts for 3.1% of world trade in goods and services.  

The regulatory framework over export of goods pivots around two interrelated pieces of legislation. The first is the Export Act and the regulations thereunder, and the trade sanctions regime. Of greatest importance is the regime established by the Export Act and the Export and Control List which now embodies what remains of the COCOM regime.

A. Export Controls, Generally

Canada’s domestic regime for export controls has always been associated with national economic and strategic interests. The current regime finds its origins in the years following World War II, when Canada and the other Western countries initiated measures to prevent the transfer of goods and technology to the former Soviet Union and its allies in the Eastern Bloc. Although these restrictions have been relaxed in recent years, the legislative mechanisms established then remain the tools with which Canadian exporters must function in the global economy today.

The basic premise of the Export Act and its regulations is to create a two-fold series of controls for domestic exports. The first level of export control addresses the types of products that can be exported the second seeks to control the destination to which goods are shipped irrespective of the type of product. Export controls are administered by the Export and Import Controls Division of the Department of External Affairs (Canada).

B. Export Control List

This first limitation is expressed generally in section 3 of the Export Act. Section 3 permits Canada to limit exports on the basis of the national security and to maintain domestic supply. It also creates the Export Control List. This list is an item by item description of the types of products on which an export controls are imposed.

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30 For a more detailed discussion see J.G. Castel et al., *The Canadian Law and Practice of International Trade* (1991) [hereinafter *Castel et al.*].

31 *Export Act*, R.S.C., ch. E-19 (1985) (Can.). “3. The Governor in Council may establish a list of goods, to be called the Export Control List, including therein any article the export of which the Governor in Council deems it necessary to control for any of the following purposes. . . .”
Control is exercised through the issuance of export permits. All products on the Export Control List require an export permit before export. The Export Control List is arranged according to a system of groupings. The first three groupings run parallel with the classifications of products and technology under what was the COCOM regime. These categories are: Group 1: Industrial List;\(^{32}\) Group 2: Munitions List,\(^{33}\) and Group 3: Atomic Energy List.\(^{34}\) Further Groups include Group 4: Nuclear Non-Proliferation List, which includes atomic energy material, and dual applications equipment and technology; Group 5: Miscellaneous Goods List, which encompasses diverse products ranging from endangered wild fauna and flora, medical products, automatic weapons and U.S. origin products; Group 6: Missile Technology Control Regime List and Group 7: Chemical and Biological Weapon Non-Proliferation List; and Chemicals for the Production of Illicit Drugs List.

In addition, Canada exercises controls separately over the export of automatic firearms by limiting such exports to countries with which Canada has intergovernmental deference, research, development and production arrangements.

C. **Area Control List**

The second mechanism for controlling the export of products and technology is the Area Control List. The focus is on the destination of the export.\(^ {35}\) If the destination of the exported good is one of the countries on the Area Control List, then that product cannot be exported from Canada without a permit pursuant to section 13 of the Export Act. Essentially, this mechanism assumes that the destination of the good is *per se* a reason for the restriction of its export, regardless of the nature of the good and its potential applications under any circumstance.

The Area Control List until recently has been dominated by countries from the former Eastern Bloc during the majority of its existence. Since 1989, the number of countries on the list has been reduced substantially, with only seven countries listed as restricted destinations today. These countries are all states which in the very recent past (or even present) have had political and/or military conflict with Canada:

(a) Libya, listed since 1986 due to its participation in international

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\(^{32}\) This consists of goods and technologies which have both civilian and military application.

\(^{33}\) This consists of munitions, military, naval or air stores.

\(^{34}\) This consists of atomic energy materials and equipment. These first lists have now been substantially modified as a result of the phase-out of the COCOM regime.

\(^{35}\) Section 4 of the Export Act provides: "4. The Governor in Council may establish a list of countries, to be called an Area Control List, including therein any country to which the Governor in Council deem it necessary to control the export of any goods." Export and Import Permits Act, R.S.Q., ch. E-19, § 4 (1985) (Can.).
terrorist activities;
(b) Yugoslavia, listed in 1991 because of U.N. sanctions;
(c) Haiti, listed in 1991 because of the overthrow of the civilian government by the military; 36
(d) Croatia and Bosnia-Herzegovina, listed in 1992 because of the on-going civil war in that area; and, finally,
(e) Angola, listed in 1994 because of United Nations sanctions 37

Until recently South Africa was on the Area Control list because of the South African government's support of apartheid. 38

D. Export Permits

The export control regime is administered in part through the issuance of export permits. There are two types of export permits: General Export Permits, which apply to goods that are on the Export Control List or Area Control List but are not considered by the Canadian Government to be of such sensitivity as to require extensive review, and Individual Export Permits. An example of a General Export Permit is General Export Permit No. 25, which applies to goods destined for Bosnia-Herzegovina. Although Bosnia-Herzegovina is on the Area Control List, a General Export Permit allows specific types of humanitarian goods to be exported: food, medical supplies and clothing.

Goods perceived to have substantive strategic value receive closer scrutiny before export. For such goods Individual Export Permits must be applied for on a case-by-case basis. Each additional export of the goods requires a new application, the granting of which remains entirely discretionary. Exporters should anticipate that the issuance of an individual export permit will take a minimum of 4 to 6 weeks and depending on the product or the destination it may take months.

36 These measures were implemented pursuant to the Special Economic Measures Act, S.C., ch. 17, (1992) (Can.). Various regulations have been adopted by the Canadian Government relating to sanctions on Haiti. These include the Special Economic Measures (Haiti) Regulations, 1993, the Special Economic Measures (Haiti) Permit Authorization Order, 1993 as well as the Special Economic Measures (Haiti) Regulations, the Special Economic Measures (Haiti) Ships Regulations, the Special Economic Measures (Haiti) Permit Authorization Order and the Special Economic Measures (Haiti) Permit Authorization Order (ships). As recently as June of 1994 Canada reiterated its support of economic sanctions as reflected in the Special Economic Measures (Haiti) Regulations, 1993, Amendment of August of 1994. In light of the recent agreement concluded by President Clinton's emissary with the Haitian Militia, it is anticipated that economic sanctions will be lifted against Haiti.

37 With respect to Angola, see Order-in-Council PC-1994-366.

38 PC 1994-217 of July 19, 1994, SOR/94-513 removes South Africa from the Area Control List as a result of the election of the first multi-racial government in South Africa. In addition, a general Export Permit will no longer be required in connection with the export of goods to South Africa.
E. The COCOM Regime Replaced

The COCOM, founded in 1949, consists of all NATO members except Iceland, Japan and Australia. Canada has been a member since 1950. The original purpose of COCOM is to control exports of strategic goods and technologies to the former Eastern Bloc countries, as well as other Communist countries like China and North Korea.

The COCOM regime has been replaced by other international agreements restricting nuclear proliferation and weapons use and by national controls as a result of the redefined strategic relationships in the wake of the demise of the former Eastern Bloc. Consequently, COCOM's response was to lower the degree of control on certain products, like computer technology, while at the same time revising the list of Proscribed Destinations in order to take into account new perceived threats to the strategic interests of member countries. In November 1993, COCOM members determined that the considerations which had necessitated the establishment of the COCOM arrangement were no longer present and as a result, the COCOM arrangement was terminated on March 31, 1994. Although it had been anticipated that new rules would be released in Canada in April of 1994, these were not released until August of 1994. The changes were effected by way of amendment to the Export Control List. What has been agreed is that the former members of COCOM will exercise national controls over goods that were previously on the Export Control List. In effect, those items listed as Groups 1, 2 and 3 on the COCOM list will no longer be subject to control (but will be governed by other international agreements). Those items under the Group 4, Nuclear Non-Proliferation, Group 6, Missile Systems and Group 7, Chemical Weapon Precursors, Biological Agents and Related Equipment will continue to be controlled. In addition, Group 8 of the COCOM list which includes chemicals used in the production of illicit drugs will be now controlled under the guidelines established by the Chemical Action Task Force as well as subject to regulation under Group 5, Miscellaneous Goods.

F. Trade Sanctions

Trade sanctions can be imposed by Canada on an *ad hoc* basis through three mechanisms. The first mechanism is the enactment of federal legislation specifically for that purpose. This does not occur frequently because of the time required to draft and pass such legislation. Sanctions can also be imposed under the *United Nations Act.* This Act provides the Canadian Federal government with the necessary authority to implement United Nations resolutions in Canada. This has

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rarely been used. Examples of implementation of economic and trade sanctions pursuant to the United Nations Act include the sanctions enacted with respect to Iraq in 1990. The Iraq regulations prohibit the export from Canada knowingly of any goods to any person in Iraq, either directly or indirectly.

The third legislative basis, pursuant to which the federal government may enact trade or economic sanctions which can effect international distribution, is the Special Economic Measures Act. This Act authorizes the federal government to impose sanctions when there has been a "grave breach of international peace and security" or when Canada must fulfill its international commitments. The sanctions imposed against Haiti were enacted under this legislation.

The significance of international sanctions is that business enterprises should be aware of Canada’s international political commitments and, to the extent that Canada has taken a position of opposing exports to specific jurisdictions, then manufacturers, distributors and exporters should be sensitive to this and carefully review their existing distribution practices. Until the recent relaxation of controls on the export and import of goods from and to South Africa, it was good example of such sanctions. Sometimes products imported from the United States, for example, may be subject to one level of export control in the United States and another (not necessarily similar) level of export control in Canada. The re-export of the finished product is complicated thereby.

G. U.S. Origin Goods

U.S. origin goods are the subject of separate and special treatment under Canada’s export control regime. Pursuant to the Export Act and the Export Control List the trans-shipment or reshipment of U.S. origin goods through Canada can be problematic because the U.S. maintains restrictions on the destination of its exports as part of its trade policy regulation. Under Item 5400 of the Export Control List, the export of U.S. origin goods to third countries requires an export permit. Usually, it is sufficient to specify on the export form that the goods are not of U.S. origin. The mere fact that a particular good is of U.S. origin does not mean that the good cannot be exported. There is a General Export Permit in existence which allows the re-export of U.S. origin goods to all but the countries on the Area Control List and certain proscribed destinations. These include destinations such as Vietnam, North Korea and Cuba. The reference to Cuba should, however, be qualified by the Canadian government’s position discussed.

42 Special Economic Measures Act, supra note 36; See for example the numerous regulations enacted pursuant to this statute with respect to Haiti listed in supra note 36.
43 General Export Permit No. 12.
above as reflected in the United States Order. 44

VIII. ANTIBOYCOTT LAWS

Antiboycott legislation is usually extra-territorial in its application and seeks to regulate commercial transactions beyond domestic borders. It is thus relevant to briefly touch upon certain restrictive U.S. legislation and Canadian antiboycott legislation which may impact on Canadian business arrangements. The Canadian position with respect to antiboycott laws is that it can give rise to conflict or concern in international transactions where, for example, the primary contractor is a United States company and a significant portion of the U.S. company's contractual commitments are subcontracted to a Canadian company. In this context, it is not unusual to find that the U.S. company will seek to impose upon Canadian companies an obligation to adhere to U.S. antiboycott rules which may not be wholly consistent with the Canadian position. United States' antiboycott laws seek to prevent United States companies or their subsidiaries from acceding to international boycotts against states, companies or persons. 45

A. The United States

There are two statutes in the United States which create antiboycott measures. 46 The first is the Export Administration Act, 47 which comprises a complex and detailed set of rules which prohibit the participation in boycotts, and also govern a company's ability to enter into and provide information that assists in the promotion of international boycott legislation. This legislation is administered by the U.S. Commerce Department. The second is the Internal Revenue Code 48 which is administered by the U.S. Treasury Department.

The reach of this legislation is broad, and is extra-territorial in its application. Under the Export Administration Act, the scope of the legislation covers "U.S. persons," which is defined to include foreign subsidiaries of U.S. companies that are "controlled in fact" and are acting in "U.S. commerce." 49 The relevant provisions of the Internal Revenue Code apply to U.S. taxpayers and their "controlled groups," a term that includes "majority-owned or controlled subsidiaries and sister

44 See supra Part IV.
46 This is not intended to be an exhaustive review, U.S. authorities should be consulted on this issue.
47 Section 8 of the Export Administration Act, 15 C.F.R. § 769 (1985).
48 I.R.C. § 999, also referred to as the "Rubicoff Amendment."
49 Moore & McGlone, supra note 45, at 54; 15 C.F.R. § 769.1(b).
companies the majority of which are owned by the same five or fewer persons.\textsuperscript{50}

U.S. antiboycott legislation prohibits a U.S. company or its subsidiary from providing information that is requested under international boycott legislation, including information regarding a company's business dealings with the state of Israel, as well as information regarding the ownership of a company's shares, or its directors or officers. Many of this legislation potentially conflicts with Canadian law.

U.S. antiboycott legislation generally does not apply to unrelated foreign agents or unrelated intermediaries since these are not "U.S. persons." The issue of whether a business enterprise may become a company "controlled in fact" or party of a "controlled group" will depend on the particularities of the relationship.

B. Canada

In Canada, boycott clauses are subject at the federal level to the 1978 Canadian Government Policy\textsuperscript{51} on international economic boycotts and at the provincial level (Ontario), to the Discriminatory Business Practices Act (Ontario) (the Ontario Act).\textsuperscript{52} In Canada, the issue of antiboycott clauses arises most frequently in the context of trade with certain Middle Eastern countries that prohibit trade with Israel.

C. Federal

- Permitted Boycott Undertakings

In Canada, boycott undertakings may be "classified" as primary, secondary and tertiary.

Primary boycott undertakings are permitted and do not constitute offensive behavior under the Canadian Policy. An example of a primary boycott undertaking would be the refusal of a Saudi contracting party to accept any goods or components of the boycotted country (i.e. Israel), either directly or indirectly. In this context, a Canadian business enterprise shipping goods to Saudi Arabia may comply with shipping document requirements that require certification with respect to country of origin, the name of the carrier and the route of shipment. Such information must be supplied in positive, non-exclusionary terms except for specific details with respect to the name of a carrier, shipment route etc. A negative statement or certification - i.e. that the goods are not of Israeli origin is not acceptable. These are referred to as "negative statements of origin." Sometimes when the Canadian business is a subcontractor, this Canadian restriction can be problematic.

\textsuperscript{50} Moore & McGlone, \textit{supra} note 45, at 54. I.R.C. § 993(a)(3).

\textsuperscript{51} This is reproduced and discussed in Castel et al. \textit{supra} note 30, at pages 423-430.

\textsuperscript{52} R.S.O., ch. D.12 (1990) (Ontario).
• Prohibited Boycott Undertakings

Secondary, tertiary and umbrella boycott undertakings are generally speaking not permitted, unless a specific clause limiting such undertakings is included.

A secondary boycott is a boycott which in general terms would require a business, as a pre-condition of doing business in a country, i.e. Saudi Arabia to limit its commercial activities with respect to another country, i.e. Israel. This offends Canadian policy because it involves a relationship and transaction separate and distinct from the transaction in question and is deemed to interfere with the business enterprise's commercial freedom.

A tertiary boycott undertaking is one that requires a contracting party to certify that goods or services are not procured in whole or in part from a particular jurisdiction - usually Israeli enterprises. It is the Canadian Government’s position that such undertakings could limit the ability of the business enterprise to do business with other Canadian businesses and consequently, such behavior is unacceptable.

Umbrella and general boycott undertakings which require Canadians to abide by the laws and regulations of the country in which they wish to do business (i.e. Saudi Arabia) or to general rules of boycott, may be unacceptable. In order to receive support from the Canadian government, companies wishing to provide such a general undertaking must include in the contract or supporting documentation a provision along the following lines:

... that in meeting the terms of this contract, the [sellers] are not required to discriminate against any person on the basis of race, religion or national or ethnic origin, and are not required to refuse to purchase from or sell goods and/or services to any other Canadian company agency or individual, sell Canadian goods and/or services to any country, or purchase goods and/or services from any country, except that it would be the right of the purchaser to refuse to accept goods, components and/or services of specified non-Canadian origin that would be prohibited entry if imported directly...

A failure to abide by the Federal Policy will result in a denial of government support and assistance with respect to the transaction. In addition, the name of contravening enterprises are published in semi-annual reports tabled in Parliament. A failure to report such activity is subject to a maximum monetary penalty of $500 and three months in jail. Under the Corporations and Labour Unions Return Act, the sanction is a daily fine of $50 for each day of late reporting.

D. Ontario (Provincial)

The Ontario Act is less restrictive than the Federal Policy. Its purpose is to prevent discrimination in Ontario on various grounds including geographical location of persons engaging in business.

The Ontario Act prohibits engaging in discriminatory business practices. Discriminatory business practices include a provision in a contract which would require a business enterprise to agree to refuse to do business with persons, businesses, etc., from Israel. In addition, a provision in the contract which would require the business enterprise to agree to refuse to engage in business with Israelis or with persons that engage in business with Israelis or products and services of Israeli origin.

The Ontario Act, like the Federal Policy, prohibits “negative statements of origin.” The Ontario Act also prohibits seeking (or agreeing to seek) any information for the purpose of engaging in a discriminatory practice.

The Ontario Act imposes a positive obligation on recipients of requests (oral or written) to engage in a discriminatory business practice to disclose such requests to the Director under the Ministry of Consumer and Commercial Relations Act (Ontario). Enforcement provisions include orders to cease the discriminatory business practice and undertakings. A person who incurs loss or damage as a result of a discriminatory business practice has the right to compensation for the loss or damage and to punitive or exemplary damages from the person who committed the contravention. In addition, any person against whom an order (to cease a discriminatory business practice) is made or who is convicted under the Ontario Act, is ineligible to enter into a contract to provide goods or services to the Government of Ontario and its related agencies for a period of five years from the date of the Order or of the conviction.