

2012

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### Recommended Citation

Sarah Bridges, *NAFTA Updates and American Trade News Highlights for Summer 2012*, 18 LAW & BUS. REV. AM. 627 (2012)  
<https://scholar.smu.edu/lbra/vol18/iss4/13>

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# NAFTA UPDATES AND AMERICAN TRADE NEWS HIGHLIGHTS FOR SUMMER 2012

*Sarah Bridges\**

## I. NAFTA UPDATES

### A. DECISION RENDERED – MOBIL INVESTMENTS CANADA INC. V. CANADA

**U.S.** oil companies Mobil Investment and Murphy Oil Corporation (Mobil and Murphy respectively) beat Canada in a two-to-one NAFTA panel decision issued on May 22, 2012.<sup>1</sup> The panel's holding that obligations imposed on the companies by a Canadian province for spending on research and development breached Article 1106 of the North American Free Trade Agreement (NAFTA or the Agreement) ended a five-year suit surrounding offshore operations in Newfoundland.<sup>2</sup> The companies do not see the victory as "unqualified," however, as the panel rejected the companies' claims that the Canadian government violated Article 1105, which mandates that investors be treated with "fair and equitable treatment and full protection" by member countries.<sup>3</sup>

Mobil and Murphy initiated suit based on breaches by Canada of specific commitments it made when it entered NAFTA in 1994 regarding the Canada-Newfoundland Accord Implementation Act (the Act) and offshore oil and gas operations.<sup>4</sup> At the time the Agreement was made, certain laws and regulations then in place in the member countries violated provisions of the Agreement. As such, Article 1108 provided certain "exceptions" to allow such laws to continue, subject to some

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1. *ExxonMobil, Murphy Oil Beat Canada in NAFTA Case*, HUFFINGTON POST (June 1, 2012, 3:31 PM), [http://www.huffingtonpost.ca/2012/06/01/canada-nafta-exxon\\_n\\_1562996.html](http://www.huffingtonpost.ca/2012/06/01/canada-nafta-exxon_n_1562996.html).

2. *Id.*; Request for Arbitration, Mobil Inv. Can. Inc. v. Can., ICSID Case No. ARB(AF)/07/4, ¶ 49 (Nov. 1, 2007).

3. Laura Payton, *Oil Companies Win NAFTA Fight Over Local Investment*, CBC (June 1, 2012, 4:56 PM), <http://www.cbc.ca/news/politics/story/2012/06/01/pol-nafta-ruling-offshore-oil.html>; North American Free Trade Agreement, U.S.-Can.-Mex., art. 1105, Dec. 17, 1992, 32 I.L.M. 289 [hereinafter NAFTA].

4. Request for Arbitration, *supra* note 2, ¶ 49.

limitations.<sup>5</sup> Article 1108 allowed the member states to list out any non-conforming measures maintained at a federal, state, or local level that they wished to remain in effect. It further provided that certain NAFTA provisions, including Article 1106, did not apply to those measures or to continuations or amendments thereof, provided, however, the amendments did not “decrease the conformity of the measure, as it existed immediately before the amendment.”<sup>6</sup>

In turn, Canada listed the Act in Annex I, partially excluding it from the control of the Agreement.<sup>7</sup> The Act provides that in order to begin an oil and gas development project, an operator must submit a “benefits plan” to the Minister of Mines, Energy, and Resources, detailing that preference will be given to Canadian goods and services during the project.<sup>8</sup> The plan must also provide for the operator to make expenditures “for research and development to be carried out in the province.”<sup>9</sup> The Act survived the Agreement under Article 1108 and continued without remarkable issue until 2004.

Mobil asserted that in November of 2004, new guidelines for these research and development expenditures were adopted that forced operators to spend an assessed amount—sometimes millions of dollars—on research and development.<sup>10</sup> Even if funds were not spent on research, the new guidelines required the companies to pay their assessed fees into a fund. This was a significant alteration to the previous version of the Act, which did not specify amounts to be spent and allowed the operators to determine the amount based on current needs, what was already available in Canada, and the circumstances.<sup>11</sup> Mobil asserted this amendment increased the Act’s nonconformity with Article 1106 of the Agreement, in violation of Article 1108. Specifically, Mobil asserted that the amendment made the Act in greater violation of the subsection of that article forbidding any demand by a member country that an investor give preferential treatment to its goods or services.<sup>12</sup> In addition, Mobil claimed the amendment was in violation of Article 1105(1) of the Agreement, which provides that investments made by investors should be afforded “fair and equitable treatment and full protection and security” by the member countries.<sup>13</sup>

Mobil filed its required notice of intent to file suit on August 2, 2007, seeking rescission of the nonconforming amendment and estimated dam-

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5. NAFTA, *supra* note 3, art. 1108.

6. *Id.*

7. NAFTA, *supra* note 3, Annex 1, at I-C-26.

8. *Id.*

9. *Id.*

10. Notice of Intent to Submit a Claim to Arbitration Under NAFTA Chapter 11 by Mobil Inv. Can. Inc., Mobil Inv. Can. Inc. v. Can., ICSID Case No. ARB(AF)/07/4, ¶¶ 2-3 (Aug. 2, 2007) [hereinafter Notice of Intent to Submit a Claim by Mobil].

11. *Id.* ¶ 4.

12. NAFTA, *supra* note 3, art. 1106.

13. *Id.* art. 1105(1).

ages of \$40 million.<sup>14</sup> Murphy followed suit the next day, estimating its damages at \$10 million.<sup>15</sup> The suits were consolidated and heard before a three-member panel in the International Centre for Settlement of Investment Disputes. Canada argued the guidelines should be permitted because they were within industry norms; they were flexible, based on rollover provisions and an operator's ability to pay the required fees through subcontractors and during both exploration and production; they resulted in payments that were conservative and common in other countries; and they required payments that were a fair estimate of what oil and gas companies operating in Canada would typically spend.<sup>16</sup>

Reports of the ruling stemmed first from the U.S. Investment Arbitration Reporter website, but the official ruling has not yet been released, as final publication of the award must await approval of redactions of confidential business information on both sides.<sup>17</sup> The panel ruled the Act was indeed in violation of Article 1106 of the Agreement, but that it did not violate fair treatment under Article 1105.<sup>18</sup> The dissenting panelist was Canada's one nominee, who dissented in the portion of the judgment against the Act's amendments, but not against the portion of the judgment that was in Canada's favor.<sup>19</sup> While damages have still not been awarded, there is speculation the 2-1 split and the panel's determination that the amendments did not violate Article 1105 will result in an amount lower than the \$50 million requested.<sup>20</sup>

#### B. NEW FILING: PANEL REVIEW REQUESTED – U.S. DEPARTMENT OF COMMERCE'S FINAL DETERMINATION REGARDING BOTTOM-MOUNT REFRIGERATOR/FREEZERS FROM MEXICO

Samsung Electronics Mexico and LG Electronics Monterrey Mexico filed requests for panel review with the U.S. Section of the NAFTA Secretariat in late April 2012, pursuant to Article 1904 of the Agreement.<sup>21</sup> The companies seek review of the International Trade Administration's determination that imports of bottom-mount combination refrigerators from Mexico were being sold in the United States at less than fair value.<sup>22</sup>

Review of antidumping and countervailing duty determinations are addressed in chapter 19 of the Agreement, which "established a mechanism to replace domestic judicial review of final determinations in antidumping

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14. Notice of Intent to Submit a Claim by Mobil, *supra* note 10, ¶ 4, 39.

15. Notice of Intent to Submit a Claim to Arbitration Under NAFTA Chapter 11 by Murphy Oil Co., Mobil Inv. Can. Inc. v. Can., ICSID Case No. ARB(AF)/07/4, ¶ 4, 39 (Aug. 3, 2007).

16. Counter Memorial of the Gov't of Can., Mobil Inv. Can. Inc. v. Can., ICSID Case No. ARB(AF)/07/4, ¶¶ 104-24 (Dec. 1, 2009).

17. Payton, *supra* note 3; Jarrrod Hepburn, *Canada Loses NAFTA Claim*, IA REP. (June 1, 2012), <http://www.iareporter.com/articles/20120601>.

18. Payton, *supra* note 3; Hepburn, *supra* note 17.

19. Payton, *supra* note 3.

20. *Id.*

21. Notice of Request for Panel Review, 77 Fed. Reg. 26252 (May 3, 2012).

22. Notice of Final Determination, 77 Fed. Reg. 17422 (Mar. 26, 2012).

and countervailing duty cases involving imports from a NAFTA country with review by independent binational panels.”<sup>23</sup> In the United States, final determinations such as these are made by the International Trade Administration of the Department of Commerce (ITA).<sup>24</sup> Pursuant to NAFTA procedure, a panel will be formed to review the ITA’s final determination to ensure that it is within antidumping or countervailing duty laws of the United States.<sup>25</sup> A panel formed in such situations may do one of two things: uphold the final determination, or remand it to the investigating authority.

In this case, the ITA investigated sales during all of 2010 and issued its Preliminary Determination on November 2, 2011.<sup>26</sup> The investigation was conducted to determine whether bottom-mount combination refrigerators from Mexico were being sold in the United States at less than fair value, as provided in section 735 of the Tariff Act of 1930.<sup>27</sup> The ITA’s final report determined the companies concerned were indeed selling at less than fair value. In addition, with respect to the merchandise exported from Mexico by Samsung Electronics Mexico, the ITA determined there were “critical circumstances,” meaning that importers in the United States likely had knowledge of the dumping and the substantial injury that could be done by it; nevertheless, there were massive imports of the concerned product within a short period of time.<sup>28</sup>

The panel review, which the NAFTA Secretariat lists in “active” status,<sup>29</sup> and associated proceedings will be governed by the Rules of Procedure for Article 1904 Binational Panel Review as published in the Federal Register.<sup>30</sup> The panel review will be limited to questions of fact or law, including whether the ITA had jurisdiction to make its final determination, which the complainants allege in their panel filings.<sup>31</sup> In an interest-

23. Notice of Request for Panel Review, 77 Fed. Reg. 26252.

24. *Overview of the Dispute Settlement Provisions*, NAFTA SECRETARIAT, <http://www.nafta-sec-alena.org/en/view.aspx?conID=615> (last updated May 30, 2011).

25. Notice of Request for Panel Review, 77 Fed. Reg. 26252.

26. See Notice of Preliminary Determination of Sales at Less Than Fair Value, Postponement of Final Determination, and Affirmative Critical Circumstances Determination: Bottom Mount Combination Refrigerator-Freezers From Mexico, 76 Fed. Reg. 67688, 67690 (Nov. 2, 2011).

27. Notice of Final Determination of Sales at Less Than Fair Value and Affirmative Critical Circumstances Determination: Bottom Mount Combination Refrigerator-Freezers From Mexico, 77 Fed. Reg. 17422, 17422 (Mar. 26, 2012).

28. *Id.* Section 735(a)(3) of the Tariff Act provides that “critical circumstances” exist if there is a reasonable basis to suspect the following: (1) there is a history of dumping and resulting material harm caused by the subject merchandise, or the person importing the product knew or should have known that the exporter was selling it at less than its fair value and that injury was likely to result; and (2) there have been massive imports of the concerned goods over a relatively short time period. Tariff Act of 1930 § 735(a)(3), 19 U.S.C. § 1673d (West 2012).

29. *Status Report of Dispute Settlements*, NAFTA SECRETARIAT, <http://www.nafta-sec-alena.org/en/StatusReportResults.aspx> (last updated Dec. 15, 2012) (set “Panel Status” to “Active” and “Filing Year” to 2012 to generate the report).

30. North American Free Trade Agreement: Rules of Procedure for Article 1904 Binational Panel Reviews, 59 Fed. Reg. 8686, 8686 (Feb. 23, 1994).

31. 59 Fed. Reg. at 8689.

ing twist in this case, the International Trade Commission (ITC) recently published an independent determination regarding bottom-mount combination refrigerators.<sup>32</sup> That investigation, triggered by a petition filed with the ITC by Whirlpool Corporation, found the below-value sale imports from Mexico did not materially injure, threaten, or retard an industry in the United States.<sup>33</sup> While the ITC is an independent source that uses its investigations to combat unfair trade practices, it takes its authority from the same Tariff Act that concerned exporters are allegedly violating,<sup>34</sup> and its report will likely aid the exporters in their upcoming NAFTA panel review.

## II. AMERICAN TRADE NEWS HIGHLIGHT – SOFTWOOD LUMBER DISPUTES

In a rare defeat in one of many disputes regarding exports of softwood lumber from Canada, the United States lost against Canada in arbitration surrounding the Softwood Lumber Act (SLA).<sup>35</sup> Despite this holding, the Deputy Assistant U.S. Trade Representative asserts that not only is the fair pricing of timber in the strong interest of the United States, but that Canada “provided publicly-owned timber harvested in its interior to softwood lumber producers for prices far below market value.”<sup>36</sup>

The decades-old dispute over Canadian exports of softwood lumber has been evaluated as akin to a sibling rivalry, resulting in review over the years by the U.S. Department of Commerce, the World Trade Organization, and NAFTA.<sup>37</sup> The dispute revolves around Canadian subsidies of softwood lumber, which is categorized as its name would indicate—easy-to-saw lumber, such as pine.<sup>38</sup> The historical disputes are lengthy, involved, and illustrate frustration on many levels on both the U.S. and Canadian sides. For example, three NAFTA cases filed by Canadian exporters, originating as early as July of 2002, lasted until mid-2007. Even then, these cases were only resolved due to jurisdictional issues—and the NAFTA panel’s decision still spanned 174 pages.<sup>39</sup>

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32. Bottom Mount Combination Refrigerator-Freezers from Korea and Mexico, 77 Fed. Reg. 28623, 28623 (May 15, 2012).

33. *Id.*

34. Peter S. Menell, *The International Trade Commission’s Section 337 Authority*, 2010 PATENTLY-O PAT. L.J. 79, 79-80 (2010), available at <http://www.patentlyo.com/files/menell.itc.pdf>.

35. Press Release, Office of the U.S. Trade Representative, Statement by the Office of the U.S. Trade Representative in Response to Decision in Third Softwood Lumber Arbitration (July 18, 2012), available at <http://www.ustr.gov/about-us/press-office/press-releases/2012/july/ustr-statement-response-softwood-lumber-arbitration>.

36. *Id.*

37. *Indepth: Softwood Lumber Dispute*, CBC (Aug. 23, 2006), [http://www.cbc.ca/news/background/softwood\\_lumber](http://www.cbc.ca/news/background/softwood_lumber).

38. *Id.*; Office of the U.S. Trade Representative, *supra* note 35.

39. *Canfor v. United States*, Secretariat File No. USA-CDA-2002-1904-03, Notice of Arbitration by Canfor (July 9, 2002); *Canfor v. United States*, Secretariat File No. USA-CDA-2006-1904-05, Decision on the Preliminary Question by the Arbitral Tribunal (June 6, 2006) (a consolidated arbitration).

As a result of these disputes, Canada and the United States entered into the SLA in 2006.<sup>40</sup> In exchange for the U.S. agreement to lift duties so long as lumber prices stayed above a certain range, Canada pledged to impose export measures on softwood lumber when its price fell below a certain level.<sup>41</sup> Canada may not circumvent those export measures by giving grants or other subsidy-type assistance to the exporters.<sup>42</sup> In its request for arbitration, the United States alleged Canada improperly graded public timber as “grade 4,” the grade at which timber is mostly unusable, allowing it to sell the timber to Canadian lumber producers at a very low price of twenty-five cents a unit.<sup>43</sup> Further, the United States assert that the amount of timber from public lands that Canada assessed at “grade 4,” and thus sold to its producers below premium, has increased dramatically since the enactment of the SLA.<sup>44</sup>

A two-week trial ensued wherein a panel reviewed the four claims of the United States: (1) Canada advised local log graders to rely on their own “local knowledge” to conduct tests, using a system of untested practices to result in lumber being improperly graded;<sup>45</sup> (2) Canada sanctioned the use of “kiln warming” on the timber, which makes inconsistencies easier to detect, resulting in lower grades;<sup>46</sup> (3) Canada encouraged new formulas and methods for log scaling, namely “bucking” and “sweeping,” that resulted in lower grades;<sup>47</sup> and (4) Canada made revisions to its scaling manuals, removing a provision that previously excluded imperfections below a certain size from consideration when grading.<sup>48</sup> In holding for Canada, the panel noted that it believed Canada’s actions, including its new techniques and policies, were actually to improve accuracy of grading, that even if the new methods did not accomplish that task they were not sufficient to be said to “circumvent” the agreement, and there was not a sufficient causal connection between the country’s actions and the increase in “grade 4” timber to hold Canada liable.<sup>49</sup>

Despite its disappointment in the ruling, the Office of the U.S. Trade Representative vowed to “continue vigorously enforcing the SLA and other U.S. trade agreements,” also pledging continued review of Cana-

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40. Office of the U.S. Trade Representative, *supra* note 35.

41. Softwood Lumber Act of 2008, 19 U.S.C.A. §§ 1683-1683g (2008) (see U.S.C.A. Popular Name Table for acts of Congress for U.S.C.A. codification).

42. Office of the U.S. Trade Representative, *supra* note 35; United States v. Canada, LCIA Case No. 111790, Request for Arbitration by the United States, ¶ 20 (Jan. 18, 2011).

43. United States v. Canada, LCIA Case No. 111790, Request for Arbitration by the United States, ¶¶ 25-28 (Jan. 18, 2011) (note the price for lumber-quality timber in Canada at the time ranged from two to ten Canadian dollars).

44. *Id.* ¶¶ 29-30.

45. United States v. Canada, LCIA Case No. 111790, Final Award, ¶ 281 (July 26, 2012).

46. *Id.* ¶¶ 309-11.

47. *Id.* ¶¶ 342-43.

48. *Id.* ¶¶ 375-76.

49. *Id.* ¶¶ 370, 381, 429.

dian pricing practices under the SLA.<sup>50</sup> The SLA was expanded for an additional period in 2012, making its terms effective through 2015.

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50. Office of the U.S. Trade Representative, *supra* note 35.





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