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North American Free Trade & Investment Report

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Biweekly report on legal & financial issues affecting direct investment and cross-border trade in Mexico, the U.S., and Canada

Mexico: Public-Private Partnerships

Infrastructure Wanted: And What Will Mexico Do Now?

By Jorge Jiménez
(López Velarde, Heftye y Soria)

Although for some years now Mexico has been working to improve its infrastructure, turning the country into a network that can support a stronger and more dynamic economy in the years to come still demands a considerable growth of all types of infrastructure, from public utilities, water treatment, water supply, roads, hospitals, to ports and other facilities for the energy industry. To increase the pace and range of such development demands a strong participation of the private sector, both domestic and foreign, in the ownership and operation of the infrastructure.

See ***Mexico****, page 3*

Canada: Competition

International Cooperation and Recent Merger Settlements in Canada

By Mark Katz and Jim Dinning
(Davies Ward Phillips & Vineberg LLP)

Several recent mergers illustrate the extent to which the Canadian Competition Bureau (the "Bureau") is committed to cooperating with foreign competition authorities when assessing international mergers affecting Canada, particularly with respect to the design of remedies. These mergers also illustrate the spectrum of approaches that the Bureau may adopt when negotiating suitable remedies, ranging from a unique "Made in Canada" resolution to complete reliance on the remedies negotiated by foreign authorities.

See ***Mergers****, page 12*

HIGHLIGHTS

Vol. 19, No. 22
December 15, 2009

Mexico's PPP Law is expected to bring a material change in the way infrastructure projects are currently done in Mexico. The bill is taking some time to be processed, but is slated to be approved in the upcoming Congressional session early in 2010. It is expected to have the majority vote of the lawmakers of PRI and PAN parties.
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NOTE TO READERS:
Only one issue is published in December. We will resume our twice monthly schedule with the January 15, 2010 issue.

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MEXICO

Taxation

Mexican Regulations Address Tax Certification Process

By PricewaterhouseCoopers Mexico

The Official Gazette published new laws for 2010 on December 7, 2009. Additionally, on that date, the Executive published the Regulations to the Federal Tax Code which contain the qualifications for independent accountants who issue tax certifications and reports. One such regulation specifies that an independent accountant who provides tax advisory services to a taxpayer-client being certified is not independent with respect to the certified report. In principle, these provisions become effective January 1, 2010.

It should be noted that this regulatory provision against independent accountants providing tax advisory services to certain clients is neither in the body of law nor contained in the Tax Code itself. In the past, this provision was the subject of proposed legislation but it was not approved by Congress. Accordingly, this new independence requirement goes beyond the current law and, as such, we do not expect that it will be effective in prohibiting the provision of tax advisory services by independent accountants to clients for whom they issue certified reports. This regulatory provision does not affect the financial statement certification by the independent public accountant.

We have been in contact with both the authorities and with members of Congress who have expressed their willingness to resolve this apparently unintended effect of limiting the activities of the independent accountant.

Nevertheless, this matter is being addressed by the accounting profession through the Mexican Institute of Public Accountants and a formal position should be expected in the near term.

***Mexico**, from page 1*

A few years ago, and consistent with international trends, Mexico started testing the European models of the so-called Public-Private Partnerships (known in the industry as PPPs). The model is conceptually simple: in order to provide public services, the State contracts on a long-term basis the provision of such service by a private third party. The State oversees, supervises and evaluates the performance of the service, quality levels and efficiency. The cost of development of the infrastructure is borne by the private developer, and is amortized by the State along the life of the project, with the possible transfer of the assets to the State at the end of the term of the contract.

At the state level, some local governments (for example, Jalisco, Chiapas, Veracruz, Tabasco and Tamaulipas) adopted specific laws to implement PPPs. Under such state laws, state governments have successfully developed state hospitals and water treatment facilities, to name a few. The federal government, on the other hand, adopted back in 2004 certain rules to facilitate the implementation of PPP projects. With such rules, the federal government started developing projects; however, structures that have proven to be successful in other jurisdictions found restrictions in their implementation in Mexico, as PPP projects continued to be subject, in many instances, to traditional government procurement laws and regulations which are very inflexible, and not conducive for this type of projects.

Facilitating Development Requires a New Framework

To pass these hurdles, and to accelerate the development of what needs to be undergoing in terms of the National Infrastructure Plan, President Calderon submitted to Mexican Congress a bill for the enactment of a new law that would provide significant support and a whole

new framework for the development of infrastructure under PPPs.

The new statute proposed by Calderon to Congress makes a carve-out from the government procurement laws, and sets forth entirely different principles to govern these projects. Among such principles, the governmental entity or agency supporting the project would be given significant latitude for setting forth terms and conditions for the relevant contract, which would be mostly governed by general contract law. Currently, contracts are subject to limitations of the government procurement laws, such as inflexibility for adjustment of costs or for amendments, capricious early terminations, among others. Also, to make the projects workable, the statute recognizes that an adequate allocation of risks among the government and the sponsors is key to the successful development. In crafting the project to ensure its financial, technical and legal feasibility, the parties are expected to have significant latitude to do such risk allocation properly.

What Role Will be Played by Foreign Investors?

Existing Mexican laws and the broad array of Free Trade Agreements and investment treaties that conform the Mexico's treaty network, have left very limited sectors in which foreign investment is not entitled to participate or has limitations in percentage of participation. Other than those sectors (which in many cases can be overcome with a regulatory authorization from the National Commission on Foreign Investment (*Comisión Nacional de Inversiones Extranjeras*), foreign investors can be expected to be very active in developing PPPs on water, roads, ports, hospitals, waste treatment, education, municipal services and others.

The proposed PPP Law is expected to bring a material change in the way infrastructure projects are currently done in Mexico.

But not only are the foreign investors able to participate; under bilateral investment, NAFTA and the treaties with the European Union and Japan, Mexico provides investors from its main commercial partners with a series of investment protections that give an additional cushion to these investments, such as the right to national treatment, free repatriation of capital, prompt payment upon expropriation or *de facto* expropriation at commercial value, and investor-State arbitration in case of disputes and violations to the treaty protections. Infrastructure developers that are foreign investors are thus afforded attractive conditions to develop their projects from the investment protection standpoint.

What Projects Would be Developed as PPPs Under this New Framework?

In general terms, federal government entities and agencies would be allowed to develop under a PPP scheme any type of infrastructure they require, provided that the type of infrastructure does not have a limitation in being owned and/or operated by a private party. They would be able to structure the provision of any service or the construction of a required facility, road or the like as a long-term service agreement. Likewise, state and municipal projects where federal funding is available may piggy-back on this statute for their development. This is important considering that the National Investment Fund (*Fondo Nacional de Infraestructura*) contributes federal funds to many local projects (for example in water treatment) to make them financially feasible.

On the other hand, consistent with the importance being recognized to the private sector for building infrastructure, the bill assumes a fundamental sharing of responsibility in the creation of projects, by entitling the private sector to propose infrastructure projects for development under PPP structures. A developer is required to prepare technical, financial, social and legal feasibility studies, review availability of land and real estate rights required, propose a contractual structure and compensation schemes, and structure the deal. The government is then required to assess the proposal. If it decides to launch the project, it will be subject to competitive tender, but the proponent of the project would be given (i) a certain advantage in comparison to other bidders when assessing their bid, and (ii) the right to recover from the party that ultimately develops the project all the development costs incurred during the feasibility and project proposal stage. This is intended to significantly foster the initiative of the private sector to propose projects that can ultimately be developed by the proponent.

Would the Bill Allow Internationally Proven Structures to Work?

While time will tell whether it works, the bill is certainly designed to accommodate the main concerns of developing infrastructure, including financing the projects. Some of the most important features are the following:

- **Land acquisition.** To provide more efficiency in the development of the projects, the bill contemplates more streamlined procedures for acquisition of land and rights of way that constitute a vital part of infrastructure development. The bill shifts from the traditional use of government appraisals, to commercial bank appraisals for the determination of the compensation payable in an expropriation, which appraisals can even consider (a) the increased value that the land will have when the project is completed, (b) rights and benefits of third parties such as possessors, lessees, (c) the acquisition of a complete property rather than a portion, even if only a portion is needed, if the remaining tract would be of limited or no use to the owner. The bill also contemplates abbreviated procedures for expropriation, and the specific regulation of negotiations with landowners.
- **Permits and concessions.** The statute would recognize the importance of permits and concessions for the development of these projects through long-term contracts, and thus proposes a special regime where all permits required for the project would be granted at least for the term of the project or 40 years, thus providing considerable regulatory certainty to the developer, and will be issued as part of the bidding process for the project.
- **Collateral for financing.** Long-term projects involving the construction of facilities are likely to be developed under project finance structures. The statute contemplates the ability of the service provider to provide as collateral the assets and rights of the project to the lenders.
- **Step-in rights of lenders.** Similarly, the statute contemplates that the developers will be able to allow full step-in rights to the project lenders to cure or avoid defaults and to prevent any negative impact to the flow of revenues of the project for paying a financing package.
- **Amendments with respect to improvements.** The PPP Law will foresee the possibility that during the long life of a contract for a project of this type, a variety of circumstances may occur which may require the original contract or the project to be modified, from new technologies that allow a change in the manner in which the service is provided, to a change in the circumstances under which a service is required by the government or the community. Mechanisms to adjust the contract and the compensation to the service provider under such circumstances will be allowed.
- **Balanced contracts.** In structuring a project, one of the major factors should be whether a contract provides for a balanced deal. The statute has as a fundamental premise that a contract that is not well-balanced will affect the long-term quality of service. For example, as part of the balance, the service provider is expected to be able to make adjustments due to changes in law.
- **Dispute resolution.** To assist in a balanced risk assessment of the project, financial feasibility and overall balance, the law contemplates the resolution of disputes with respect to the project through commercial arbitration. With respect to technical disputes, the appointment of independent experts is contemplated.

The bill is taking some time to be processed, but is slated to be approved in the upcoming Congressional session early in 2010. It is expected to have the majority vote of the lawmakers of PRI and PAN parties.

Will this be Moving Forward? What Would be Next?

The proposed PPP Law is expected to bring a material change in the way infrastructure projects are currently done in Mexico. Because of that, the bill is taking some time to be processed, but is slated to be approved in the upcoming Congressional session early in 2010. It is expected to have the majority vote of the lawmakers of PRI and PAN parties.

Upon being enacted, the Ministry of Finance and Public Credit (*Secretaría de Hacienda y Crédito Público*) will need to issue rules governing how projects will be assessed in terms of their feasibility; however, upon enactment of the PPP Law the government will be free, even without such rules, to start using such mechanism. We may thus expect projects to start moving under this structure in 2010.

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UNITED STATES

Trade

Trends in International Trade Policy: What to Expect in 2010

By Ken Weigel, Jeff Schwartz, and Eric Shimp
(Alston & Bird LLP)

The following are some of the trends in international trade from a U.S. perspective that we see going into 2010.

Trade Actions

Globally, initiations of antidumping investigations rose 52.6 percent in the third quarter of 2009 compared to the same *period* in 2008. Year-to-date data indicate a 30 percent rise in antidumping investigation requests by domestic industries in 2009 over the comparable period in 2008. Initiations of safeguard investigations are on a similar pace for 2009, which will rank as the second-busiest year for safeguard cases since the remedy was formally adopted by the WTO in 1995.[1]

Anticipate both trade and investment policy to proceed in fits and starts over the next year, as the looming 2010 elections will elicit caution from the administration and Congress alike.

On the other hand, while U.S. companies continue to file trade remedy cases, the overwhelming majority are against imports from China. Typically, Chinese producers and exporters have not marshaled the same resources in fighting dumping charges as producers *and* exporters in market economy countries. This has resulted in a change in the practice in the United States.

Imports

Countries, particularly the United States, continue to push for new enforcement and regulatory initiatives for imports prior to them reaching their borders. Beginning in January 2010, the United States will begin to enforce the requirements of the Importer Security Filing, otherwise known as the "10+2" filing requirement This new requirement will increase the information required before a good is exported to the United States and will also increase the potential for penalties and liquidated damages being assessed against importers. Overall, the burden and cost of importing into the United States will increase.

Trade Policy

Anticipate both trade and investment policy to proceed in fits and starts over the next year, as the looming 2010 elections will elicit caution from the administration and Congress alike.

Trade policy in the Obama administration continues to suffer from paralysis. Core Democratic constituencies, including organized labor and environmental NGOs, have taken a lead role in a prolonged "review" of U.S. trade policy seeking to reorient the market access and regulatory objectives of U.S. trade negotiations.

The Democratic 111th Congress, too, heavily influenced by "fair trade" members, has sought to claw back congressional authority over trade, adding a degree of complexity to trade policy formulation. The *review*, coupled with congressional objectives and the administration's packed domestic agenda of health care, climate change and financial re-regulation, has drastically limited the ability of the U.S. Trade Representative to engage with trade partners. Tentative attempts at trade diplomacy through the WTO Doha Round and the nascent Trans-Pacific Partnership have been met with serious skepticism by foreign governments who doubt the administration's commitment to trade liberalization. The White House will likely continue in this holding pattern for the indefinite future.

U.S. investment policy, too, remains under review, as the administration has convened public and private sector interests to redesign the U.S. Model Bilateral Investment Treaty (BIT). Advisors remain deadlocked over differences on key policy areas, such as expropriation,

sovereign regulatory independence and investor-state dispute settlement. Here, too, labor and environmental interest groups have taken a lead role in seeking fundamental policy changes. The debate has had a stultifying effect on the ability of the administration to pursue already-launched BIT negotiations with India and China, and has prevented the initiation of new treaty talks with economies such as Brazil.

Most major world economies—the EU, China, Japan, India and Brazil—continue to vigorously negotiate bilateral and regional free trade agreements. In contrast, in 2009, the United States has refused to undertake meaningful new negotiations or to ratify concluded agreements. This inactivity by the United States is already yielding changes in global market access that harm the export and investment opportunities for U.S.-based companies, farmers, ranchers and investors.

Export Controls

The United States is vigorously enforcing its export controls. The active involvement of the National Security Division within the U.S. Department of Justice will likely result in increased criminal prosecutions in the export control area. U.S. attorneys' offices throughout the country have received export control training, and reports indicate higher degrees of cooperation among export regulation enforcement personnel at the Departments of State and Commerce and investigation and prosecution personnel within the Department of Justice.

From a regional perspective, the enforcement emphasis remains on detecting and punishing unauthorized exports of products and technology to China and Iran.

The prospects for Congress enacting new sanctions legislation directed at Iran appear good at this stage.

Export agencies are continuing to migrate to electronic systems for processing licenses and other types of filings. Export licenses for dual-use items must be submitted to the U.S. Department of Commerce electronically, with few exceptions. Most types of licenses for defense articles and defense service exports must be submitted electronically to the U.S. Department of State, which is also seeking public comment on several other types of filings that the department intends to permanently migrate to electronic formats.

The Obama administration has initiated a broad review of current U.S. export control laws and regulations aimed at achieving a substantial makeover of both the dual-use and defense trade control regimes. The review is significant in that it would be the first official effort to reassess the structure and content of U.S. export controls on an across-the-board basis that addresses separate regimes under differing statutory authorities administered by the Department of Commerce's Bureau of Industry and Security (BIS) and the Department of State's Directorate of Defense Trade Control (DDTC).

National Economic Council (NEC) Chairman Larry Summers and National Security Advisor Jim Jones are orchestrating the White House review, while Defense Secretary Robert Gates is also taking a very active role. In a separate but related development, Congress is developing legislation to reform dual-use export controls administered by BIS, although the scope of such reform is far from clear at this early stage. It is possible that the administration will initiate some measures under existing regulatory authority without waiting for new legislation.

In an early suggestion of what might emerge from this review, Secretary of Commerce Gary Locke this fall hinted at easing or removing license requirements for dual-use exports to "allies and partner nations," presumably the countries who participate in multilateral control regimes with the United States.

Conclusion

In 2010, the United States is likely to remain on the sidelines in the trade policy area; nonetheless, trade policy activity will continue internationally and take the lead away from the United States. Companies will be required to consider and work on trade policy initiatives outside the United States. Imports will face increased regulatory burdens for security purposes, while exports will be scrutinized for compliance and more export violations prosecutions will occur.

1 http://people.brandeis.edu/~cbown/global_ad/monitoring/Bown-World-Bank-Global-Antidumping-Database-Oct-2009-Executive- Summary.pdf

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CANADA

Government Procurement

Foreign Bidders on Canadian Federal Contracts Lose the Protections of the Agreement on Internal Trade

By Brenda C. Swick
(McCarthy Tétrault LLP)

In a surprising decision, the Supreme Court of Canada recently held, in *Northrop Grumman Overseas Services v. Canada (Attorney General)*,[1] that an unsuccessful bidder on a procurement conducted by the Federal Government must be "Canadian supplier" in order to have standing to bring a complaint before the Canadian International Trade Tribunal ("CITT") based on the Agreement on Internal Trade ("AIT").

This decision has far-reaching consequences for foreign bidders on Federal Government contracts.

This decision has far-reaching consequences for foreign bidders on Federal Government contracts:

1. A non-Canadian[2] supplier whose contract is not covered by the NAFTA or the WTO Agreement on Government Procurement (WTO-AGP) procurement provisions has no recourse to the CITT at all but only normal judicial review (see point 4 just below). That supplier's Canadian competitors do, though, have recourse under the AIT, the NAFTA and the WTO-AGP, as well as under normal judicial review.

2. If, however, NAFTA and AGP are not excluded, that foreign supplier can go to the CITT but can only invoke the protections of NAFTA and WTO-AGP, but not those of the AIT.

3. Non-Canadian bidders on Federal Government contracts, if they are not covered under the NAFTA or the WTO AGP, ought to ensure that their bids are made through and fulfilled by their Canadian subsidiary or a Canadian entity with a "place of business in Canada" in order to take advantage of the fair bidding protections in the AIT and to have standing to complain about the award before the CITT.

4. If the goods are excluded from the scope of coverage under the NAFTA and WTO AGP, the foreign supplier now only has recourse to the Federal Court by way of judicial review of the contract award.[3] This recourse is limited, and the remedies are much more restrictive by comparison to that available through the CITT.

5. The consequence of limiting standing under the AIT to Canadian suppliers is a double bifurcation of the bid complaint system.

a. Canadian suppliers have standing to make AIT-related complaints to the CITT but their non-Canadian competitors cannot.

b. Successful non-Canadian suppliers are now required to intervene to defend their awards in proceedings before the CITT but would not have an equal right to pursue remedies before it if they were unsuccessful.

6. Such a bifurcated bid complaint system will result in conflicting decisions and increased costs.

7. The procurement obligations in the trade agreements now confer different rights. A non-Canadian supplier will no longer be able to rely on the protections afforded under the AIT which are in certain aspects different and more demanding than those of the NAFTA or WTO AGP.

8. The SCC decision itself may be seen as a "discriminatory measure" subject to challenge under the NAFTA and WTO Agreement on Procurement.

Background

Procurement Review in Canada

The NAFTA[4], the WTO AGP[5] and the AIT[6] (and now the *Canada-Chile Free Trade Agreement*) each establish their own rules to provide suppliers equal opportunity to compete with Canadian suppliers for contracts involving

designated classes of goods and services purchased by prescribed Federal government departments, agencies and Crown corporations. Each also imposes procedural disciplines aimed at promoting transparency, predictability and competition in public sector procurements.

These agreements require the signatories to maintain an independent bid challenge authority to enforce the procurement obligations contained in these agreements. The CITT is Canada's bid challenge authority. It was designated to handle complaints alleging breach of any of the agreements mentioned above. Its role is to ensure that the procurements covered by NAFTA, the AIT, the AGP or the CCFTA are conducted in an open, fair and transparent manner and, wherever possible, in a way that maximizes competition. On occasion, a potential supplier may have reason to believe that a contract has been or is about to be awarded improperly or illegally, or that it has been in some way wrongfully denied a contract or an opportunity to compete for one. The CITT mechanism provides, at least until now, a one-stop opportunity for redress for potential suppliers concerned about the propriety of the procurement process relating to contracts covered under these agreements.[7]

Supreme Court of Canada Decision

The Department of Public Works and Government Services Canada ("PWGSC') issued a request for proposals for the procurement of military goods, in particular, 36 Advance MultiRole Infrared Sensor ("AMIRS") targeting pods for the Department of National Defence's CF-18 Hornet aircraft and 13 years of in-service support for the pods. Northrop Grumman Overseas Services Corporation ("Northrop Overseas"), a Delaware corporation wholly owned by Northrop Grumman Corporation, submitted a bid. The contract was awarded to Lockheed Martin Corporation for USD 89,487,521 for the AMIRS pods and USD 50,357,649 for the in-service support. Northrop Overseas filed a complaint with the CITT alleging that PWGSC had failed to evaluate the bids properly, violating Article 506(6) of the AIT. It alleged that PWGSC had failed to evaluate bids in accordance with the Evaluation

There is no further appeal from the Supreme Court of Canada, and the only way to cure the obviously discriminatory and doubly bifurcated system of procurement review now in place is for Parliament to make clear that its intention really is that all bidders should play by, and be protected by, the same rules.

Plan, which set out the procedures and methodology for evaluating bids, including the score to be awarded for different aspects of each bid. Northrop Overseas alleged that it was not awarded points to which it was entitled and that Lockheed was awarded points to which it was not entitled. In so doing, Northrop Overseas argued that PWGSC violated Article 506(6) of the AIT, which requires procurements covered by the AIT to identify clearly the criteria by which bids will be evaluated.[8]

PWGSC challenged Northrop Overseas' standing to file a complaint based on a breach of the AIT on the grounds that it was not a "Canadian supplier". The issue of standing was appealed to the Supreme Court of Canada.

Standing before the CITT for procurement complaints is governed by section 30.11(1) of the *Canadian International Trade Tribunal Act*, ("CITT Act") which provides that "a potential supplier may file a complaint with the tribunal concerning any aspect of the procurement process that relates to a designated contract and request the Tribunal to conduct an inquiry into the complaint". Northrop Overseas argued that the contract for the supply of targeting pods for the CF-18 aircraft plus in service support for 13 years is a contract designated in Article 502 of the AIT.[9]

The SCC rejected Northrop Overseas's argument that the only requirement for standing is to be a "potential supplier" under a "designated contract".[10] The SCC found that, in the case of the AIT, in order for the contract to be a designated contract, the supplier must be a "Canadian supplier" in a procurement contract by a Canadian government or entity.[11] The Court went on to hold that only suppliers "with an office in Canada"[12] qualify as Canadian suppliers.

On the basis that Northrop Overseas did not have a place of business in Canada, the SCC found that it was not a "Canadian supplier" and not entitled to invoke the provisions of the AIT before the CITT, or anywhere else for that matter.[13]

The Supreme Court was influenced in interpreting the AIT and the CITT Act by what Canada had agreed to in the NAFTA and the WTO-AGP. In rejecting the Northrop Overseas's argument that non-Canadian suppliers have standing to bring complaints based on the AIT, the Court noted that the contract for military goods at issue was not a "designated contract" under the NAFTA or the WTO-AGP because its subject matter did not fall within the scope of either of those trade agreements.[14] By contrast, it noted that AIT does apply to all procurements by PWGSC or DND and that the goods were not excluded from the AIT.[15] Had Northrop Overseas's argument prevailed, it would have gained rights under the AIT despite the United States Government not being a party to the AIT and notwithstanding that this type of military equipment is specifically excluded from the scope of coverage under the NAFTA and WTO AGP. In the Court's view, allowing Northrop Overseas to do through the back door what it could not do through the front door would have undercut such an exclusion negotiated by the Government of Canada.[16]

The Supreme Court of Canada has thus decided that the provinces and Canada, which negotiated the AIT to gain for their tax-paying citizens the benefits of competition in procurement, really only meant to have that benefit apply to intra-Canadian competition.

It has also decided that, though Parliament deliberately chose to send all procurement challenges to a single authority, the CITT, some can go there and some cannot, and those that do go there can invoke this protection or that depending on the Canadianness of the complainant.

There is no further appeal from the Supreme Court of Canada, and the only way to cure the obviously discriminatory and doubly bifurcated system of procurement review now in place is for Parliament to make clear that its intention really is that all bidders should play by, and be protected by, the same rules.

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1 *Northrop Grumman Overseas Services Corp. v. Canada (Attorney General)*, 2009 SCC 50, Nov. 5, 2009.

2 The Supreme Court of Canada was ambiguous as to what it had in mind by "Canadian" and by "non-Canadian".

3 This is particularly relevant in the area of military procurement. Under both the NAFTA and WTO AGP, military procurement is treated differently from many other categories of procurement. Whereas all procurements by certain federal government departments are covered by these agreements, for the Department of National Defence, the only procurements covered by the NAFTA are those for the goods listed at its Annex 1001.1b-1. And the only procurements covered by the WTO AGP are those listed in its Annex 1. In *Northrop Grumman Overseas*, the goods at issue, "Fire Control Systems", were listed in neither.

4 Under the NAFTA, Canada agreed to provide suppliers of the United States and Mexico equal opportunity to compete with Canadian suppliers for contracts involving designated classes of goods and services purchased by prescribed Canadian government departments, agencies and Crown corporations. It guarantees national treatment and non-discrimination to goods originating in Canada, the United States and Mexico, as well as to the suppliers of such goods and service suppliers in these countries. It also imposes procedural disciplines aimed at promoting transparency, predictability and competition in public sector procurements. These procurement protections apply to Canadian government procurements with a value equal to or greater than certain monetary thresholds. The monetary thresholds applicable to procurements by government departments and agencies are $76,500 for goods, services or any combination thereof and $9.9 million for construction services contracts. (As between Canada and the United States, the monetary threshold for the procurement of goods by departments and agencies is $28,200.) The monetary thresholds applicable to procurements

by Crown corporations are $382,800 for goods, services or any combination thereof and $12.2 million for construction services contracts.

5 Under the WTO AGP, Canada agreed to provide suppliers of the signatory countries equal opportunity to compete with Canadian suppliers for contracts involving designated classes of goods and services purchased by specified Canadian government departments, agencies and Crown Corporations with a value equal to or greater than certain monetary thresholds. The applicable monetary thresholds are $217,400 for goods, services or any combination thereof and $8.3 million for construction services contracts. The AGP has its own set of disciplines for public procurements, not all of which mirror those contained in the AIT and NAFTA.

6 Under the AIT (an agreement among Canada and all its provinces and territories), Canada agreed to provide suppliers with equal access to federal government procurement for contracts for designated classes of goods and services purchased by prescribed government departments and agencies and Crown corporations. Insofar as the federal government is concerned, the AIT applies to procurements with a value equal to or greater than $25,000, in cases where the largest portion of the procurement is for goods, and a value equal to or greater than $100,000, in cases where the largest portion of the procurement is for services, including construction services contracts. The Northrop decision holds that the word "supplier" should be read to mean only "Canadian supplier".

7 CITT Publication: Procurement Review Process: A Descriptive Guide 2009. http://www.citt.gc.ca/publicat/guide_e.asp

8 *Northrop Grumman Overseas Services Corp. v. Canada (Attorney General)*, 2009 SCC 50, Nov. 5, 2009. http://scc.lexum.umontreal.ca/en/2009/2009scc50/2009scc50.html, paras. 2 and 3.

9 *Ibid*., paras. 13 and 14.

10 Section 30.1 of the CITT Act defines a "potential supplier" as a "bidder or prospective bidder on a designated contract". A "designated contract" is defined as "a contract for the supply of goods or services" to a government institution and "that is designated or of a class of contacts designed by the regulations". Section 3(1) of the CITT Regulations further provides that a "designated contract" is one described in the NAFTA, the WTO Agreement on Government Procurement, or the AIT and now the Canada-Chile Free Trade Agreement. In order to gain access to the CITT complaint procedure, the subject-matter of the procurement must be within the scope of one of the trade agreements.

11 *Northrop Grumman Overseas Services Corp. v. Canada (Attorney General)*, 2009 SCC 50, Nov. 5, 2009. http://scc.lexum.umontreal.ca/en/2009/2009scc50/2009scc50.html, para. 32.

12 It is not clear that a company with an office in Canada is Canadian, or that one without such an office is necessarily non-Canadian, but that appears to be what the Supreme Court of Canada has decided for purposes of the AIT.

13 *Northrop Grumman Overseas Services Corp. v. Canada (Attorney General)*, 2009 SCC 50, Nov. 5, 2009. http://scc.lexum.umontreal.ca/en/2009/2009scc50/2009scc50.html, at para. 30.

14 For the DND, the only procurements covered by the NAFTA are those for goods listed at its Annex 1001.1b- 1, and the only procurement covered by the WTO-AGP are those listed in its Annex 1. "Fire Control Systems" were not listed in either Annex 1001.1b-1 or Annex 1 and therefore neither of these agreements applied to the procurement at issue.

15 See Annex 502.1A of the AIT.

16 *Northrop Grumman Overseas Services Corp. v. Canada (Attorney General)*, 2009 SCC 50, Nov. 5, 2009. http://scc.lexum.umontreal.ca/en/2009/2009scc50/2009scc50.html, paras. 41 and 47.

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***Mergers**, from page 1*

Background

The Bureau's most complete statement on international merger cooperation is set out in its *Information Bulletin on Merger Remedies in Canada* (the "Remedies Bulletin"). The Remedies Bulletin recognizes that the increasing number of global mergers enhances the need for communication, coordination and cooperation among competition authorities around the world. These goals may be achieved through the exchange of information (often facilitated by waivers granted by the merging parties or other affected persons), cooperation in investigations and coordination of remedies.

The Remedies Bulletin notes that coordinating remedies helps avoid problems that may arise when a remedy in one jurisdiction is not acceptable in another; can lead to a more effective resolution than would be attained through a piecemeal solution; and reduces uncertainty for businesses. At the same time, competition authorities are ultimately responsible for ensuring that mergers do not lessen competition within their jurisdiction's borders. As a result, different authorities may require different remedies.

With continued growth in global mergers, the trend towards cooperation between the Bureau and foreign competition authorities is sure to continue.

In light of these conflicting considerations, there is a spectrum of remedial outcomes available to the Bureau when reaching settlements with parties to international mergers. At one end of the spectrum, the Bureau may enter into a consent agreement with the merging parties requiring unique remedies not mandated in other jurisdictions. At the other end, the Bureau may rely wholly on the remedy agreed to in another country, when the foreign authority's resolution effectively addresses competition issues in Canada. The Remedies Bulletin states that this is most likely to happen when the assets subject to divestiture (or when the conduct that must be carried out as part of a behavioural remedy) are located outside of Canada. In the middle of the spectrum, the Bureau may enter into a consent agreement requiring remedies that are the same as or largely similar to those required abroad.

"Made in Canada" Remedies

In November 2009, the Bureau announced that it had entered into a consent agreement with Agrium Inc. to resolve competition concerns related to Agrium's proposed acquisition of CF Industries Holdings Inc. Both bidder and target are major international fertilizer companies. The Bureau's review determined that the transaction would likely lead to a substantial lessening and/or prevention of competition in the wholesale supply of certain nitrogen fertilizer products in the provinces of Alberta and Saskatchewan. The remedy package agreed to by the Bureau and Agrium addresses this likely substantial lessening and/or prevention of competition in the event that Agrium is ultimately successful in its substantial bid for CF Industries.

The Bureau's press release concerning the proposed transaction notes that it cooperated closely with the U.S. Federal Trade Commission ("FTC") during the course of its review. However, no remedy has yet been announced by the FTC and the focus of the Bureau's remedy appears to be purely domestic.

Similarly, earlier in 2009, the Bureau reached a consent agreement with Suncor Energy Inc. and Petro-Canada pertaining to their proposed merger (now completed). The agreement requires the parties to divest 104 retail gas stations in the province of Ontario and to sell storage and distribution network capacity in the Greater Toronto Area for 10 years. Remedies were not required in the U.S., where the transaction was granted "early termination" by the FTC.

Reliance on Foreign Authorities' Remedies

At the other end of the remedies spectrum, the Bureau announced in April 2009 that commitments made by BASF SE to U.S. and European competition authorities also resolved the Bureau's concerns about the effect of BASF's acquisition of Ciba Holding AG on competition in Canada for the supply of indanthrone blue and bismuth vanadate pigments. These pigments are used in products such as paints and automobile coatings.

The divestitures announced by BASF formed part of BASF's agreements with the FTC and the European Commission's Competition Directorate to divest Ciba's global indanthrone blue and bismuth vanadate businesses. No separate consent agreement was entered into in Canada, even though some of the divested assets (including intellectual property rights and customer accounts) were located in Canada.

Similarly, in conjunction with Dow Chemical Company's proposed acquisition of Rohm and Haas Company,

the Bureau concluded in January 2009 that the merger would likely result in a substantial lessening or prevention of competition in Canada for the supply of certain acrylic acid products (used to create polymers), acrylic latex polymer products (used as inputs to make paints and coatings, cement additives, and caulks and sealants in construction products) and hollow sphere particle products (used to give gloss and opacity to paper). However, Dow's agreement with the FTC addressed these issues and the Bureau concluded that no further remedy agreement was required in Canada.

Similar Remedies in Canada and Abroad

In late October 2009, the Bureau entered into a consent agreement with Schering-Plough Corporation and Merck & Co., Inc. concerning their proposed merger. The agreement imposed three major requirements on the merging parties. First, Schering-Plough was required to divest a new drug currently in development for the treatment of chemotherapy-induced and post-operative side effects which will compete with a similar product already offered by Merck. Second, Merck was required to divest its interest in animal health company Merial Ltd. to its joint venture partner, Sanofi-Aventis. Third, any contemplated future combination of the assets of Merial with the animal health business of the combined Merck/Schering-Plough entity will be subject to prior review and approval by the Bureau.

The Bureau's press release noted that it cooperated closely with the FTC in its review. In fact, the Canadian consent agreement requires essentially the same remedies as those required by the FTC, which itself noted that it cooperated with its counterparts in Canada, Australia, Europe, Israel, Mexico and New Zealand during the course of its investigation. (However, the Canadian and American settlements differ from the outcome of the European Commission's review, which did not require any further remedies following Merck's divestiture of its interest in Merial.)

The remedies announced by the Bureau in connection with Pfizer Inc.'s acquisition of Wyeth were also largely similar to those secured by the FTC. Specifically, the parties agreed with both the Canadian and U.S. authorities to divest a number of animal pharmaceutical and vaccine products to Boehringer Ingelheim Vetmedica, Inc., although there were slight differences in the products subject to divestiture, *e.g.*, certain equine products under development do not appear to be subject to the Canadian consent agreement. The Bureau also required that Pfizer amend the terms of its existing arrangement with Paladin Labs Inc. governing the distribution, marketing and sale in Canada of a hormone replacement product, which was not part of the FTC settlement.

Conclusions

With continued growth in global mergers, the trend towards cooperation between the Bureau and foreign competition authorities is sure to continue. For obvious reasons, this cooperation will also continue to extend to the negotiation of remedies. As can be seen from the examples summarized above, the Bureau utilizes a spectrum of approaches to the design of remedies in international mergers, depending upon the extent to which specific "made in Canada" elements are required. On the whole, the goal seems to be to adopt the most efficient course possible, although one may question why in certain cases the Bureau has required a separate consent agreement to be concluded in Canada even though the remedy it negotiated was essentially the same as required by other jurisdictions (e.g., the Schering-Plough/Merck transaction).

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Trade

Looking Back and Moving Forward: Key Developments in Canadian Trade Controls and Economic Sanctions During 2009

By John W. Boscariol
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As 2009 draws to an end, it is an opportune time to review the changes to Canada's economic sanctions and trade controls over the past year in order to ensure compliance programs are fully up-to-date and risks of contravention and enforcement action are minimized.

Because of the significant financial and reputational impact that contraventions in this area can have, it is important that any company doing business internationally, whether in the goods, services or technology sector, ensure appropriate compliance and due diligence measures are in place. These include: maintaining compliance manuals; appointing responsible compliance officers; screening customers, end-users and suppliers; providing training programs; conducting internal audits; establishing disclosure procedures; and reviewing contracts and other legal documentation on a regular basis.

One of the most significant sections of the Export Controls Handbook is its written procedures on voluntary disclosures. It provides that disclosures of non-compliance with the Export and Import Permits Act (EIPA) may be made to the ECD in writing and specifies the information required.

The most significant developments of the past year in the area of Canadian economic sanctions and trade controls are discussed below.

Amendments to Canada's Export Control List

Canada's *Export Control List* (*ECL*) identifies the goods and technology that require a permit prior to being exported or transferred from Canada. On April 30, 2009, the *ECL* was amended, bringing into force a new version of the *Guide to Canada's Export Controls*.

New items were added to Group 1 of the *ECL* (dual-use), including in the advanced materials, materials processing, electronics, telecommunications, navigation and aerospace categories; Group 2 (munitions); Group 3 (nuclear); Group 6 (missile control), including in the propulsion, propellant, materials, instrumentation, launch support, testing, and stealth categories; and Group 7 (chemical and biological weapons). Controls were also removed or revised in Groups 1, 6, and 7.

Details on the specific additions, removals and revisions to items on the *ECL* can be found on the website of the Export Controls Division of Foreign Affairs and International Trade Canada (ECD) at: http://www.international.gc.ca/controls-controles/about-a_propos/expor/guide.aspx?menu_id=72&menu=R

New Export Controls Handbook

In February 2009, the ECD issued, and in May 2009 reissued, its *Export Controls Handbook*, which replaces the guidelines contained in the *Guide to Canada's Export Controls* prior to the *Guide*'s amendment discussed above.

The *Handbook* includes similar administrative information but has been updated, is more detailed, and also contains an overview of Canada's economic sanctions programs. It provides more commentary for exporters on various topics, including: exporting controlled US goods and technology; distinguishing between consignees and end-users in complex cases; evaluating foreign clients, exports of goods temporarily imported, and exports by intangible means such as through services, telephone conversations and face-to-face meetings; and enforcement actions that may be taken by the Canada Border Services Agency (CBSA).

One of the most significant sections of the *Export Controls Handbook* is its written procedures on voluntary disclosures. It provides that disclosures of non-compliance with the *Export and Import Permits Act* (*EIPA*) may be made to the ECD in writing and specifies the information required. It also notes that the ECD will look "favourably upon disclosures if … satisfied that the exporter has fully cooperated and no further action is warranted." Depending on the circumstances, the ECD may refer matters to the CBSA or the Royal Canadian Mounted Police. Although this may offer some opportunity for comfort for exporters who have potential violations, they should also carefully consider whether a separate voluntary disclosure to the CBSA may also be appropriate, as that agency is responsible for the enforcement of related requirements under both the *Customs Act* and the *EIPA*.

A copy of the ECD's *Export Controls Handbook* can be found at: http://www.international.gc.ca/controls-controles/assets/pdfs/documents/ExportControlHandbook-eng.pdf

Changes to Canada's UN Sanctions Programs

During 2009, Canada amended a number of its regulations governing business with countries subject to United Nations Security Council sanctions, including the following:

1. North Korea — Canadian sanctions were amended effective July 30, 2009 to reflect the UN Security Council's strengthening of measures against North Korea. The amendments expand the embargo on arms and related technical assistance, prohibit certain financial transactions and the provision of services to vessels believed to be carrying sanctioned cargo, and expand the list of sanctioned items.

2. Rwanda — Measures that had previously imposed an arms embargo against Rwanda were repealed effective June 4, 2009.

3. Somalia — On March 12, 2009, Canada implemented new regulations regarding an arms embargo; a prohibition on technical, financial and other related assistance; and an asset freeze against designated persons.

4. Liberia — On January 29, 2009, sanctions were amended to provide exceptions to the existing arms embargo and to repeal the ban on imports of rough diamonds, round logs and timber products from Liberia.

Increasing Scrutiny of Transactions Involving Iran

There were strong signals during 2009 that Iranian-related transactions were being very carefully scrutinized for consistency with existing Canadian sanctions measures. Canadian authorities have been publicly expressing their concerns, particularly with the supply of nuclear-related items from Canada for use in Iran and the export or transfer of US-origin goods or technology to Iran through transhipment points located in the United Arab Emirates, Malaysia, Singapore and Hong Kong, among other countries.

In February 2009, Canada's Office of the Superintendent of Financial Institutions issued a Notice that any financial transactions involving Iran should be viewed as "potentially suspicious," and that financial institutions that have correspondent banking relationships with Iranian banks should be implementing "stringent enhanced due diligence measures." See: http://www.osfi-bsif.gc.ca/app/DocRepository/1/eng/issues/terrorism/fatf/2009_02_27_e.pdf

In April 2009, in what appears to be the first case of its kind, Canadian authorities arrested and charged a Toronto man with violating Canada's Iran sanctions and related legislations, including the *EIPA* and the *Customs Act*. It is alleged that he had sourced from the United States pressure transducers, which can have commercial or military applications, and attempted to export them from Canada to Iran for use in the uranium enrichment process for weapons-grade products. A trial is expected in 2010.

Continued Conflicts with US Trade Controls

Any effective compliance program for businesses operating across the United States-Canada border must address the consistencies and conflicts between US and Canadian export control and sanction regimes. In some cases, the controls will be similar or even identical. In other cases they may differ, while in yet others they actually create conflicting obligations such that compliance with one regime could result in violation of the other. Recently, difficulties have intensified as a result of increased US enforcement initiatives.

Canadian companies continued to struggle with conflicting control regimes regarding two areas in particular — doing business with Cuba, and working with goods and technology subject to US military controls.

During 2009, Canadian companies continued to struggle with conflicting control regimes regarding two areas in particular — doing business with Cuba, and working with goods and technology subject to US military controls.

An order issued under Canada's *Foreign Extraterritorial Measures Act* prohibits Canadian companies, including those that are US-owned or -controlled, from complying with various elements of the US trade embargo of Cuba. The order also requires Canadian companies to notify the Attorney General of any communications relating to the US embargo received from someone in a position to control their activities in Canada. As Canada is one of Cuba's largest trading partners and one of its most significant sources of foreign direct investment, Canadian companies, particularly those governed by US controls because they are owned or controlled by US entities, are increasingly subject to these conflicts.

The US *International Traffic in Arms Regulations* (*ITAR*), and in some cases the US *Export Administration Regulations*, can restrict the ability of foreigners in Canada, dual nationals, and even Canadian citizens if they were born in certain proscribed countries, to access *ITAR*-controlled technology or defence services. Compliance with these US rules by Canadian companies dealing with controlled goods and technology can lead to a violation of anti-discrimination obligations imposed by Canadian labour and human rights laws.

Any effective compliance program for businesses operating across the United States-Canada border must address the consistencies and conflicts between US and Canadian export control and sanction regimes.

Because of the differences — and in some cases, the conflicts — between the US and Canadian regimes, Canadian compliance programs need to be "homegrown" and not simply copied or obtained from US affiliates. These differences and conflicts must also be addressed when undertaking each of the key steps in developing and following a US-Canadian trade control compliance strategy, including when: drafting and executing compliance procedures; implementing training programs; conducting internal compliance audits; issuing communications and instructions to Canadian operations; determining what materials and information Canadians can access, including from US-based servers; and conducting meetings and telephone conversations involving these issues.

Current "Red Flag" Destinations

Any internal compliance system should provide for the effective screening of transactions against "red flag" destinations or parties. If any of these countries, entities, organizations or individuals are or may be involved, the activity should be carefully scrutinized for compliance with applicable Canadian trade controls and economic sanctions.

At the present time, your red flags should include Burma, Belarus, Sudan, Iraq, Lebanon, North Korea, Iran, Democratic Republic of the Congo, Côte d'Ivoire, Liberia, Somalia, Sierra Leone, Zimbabwe, and listed individuals and entities under Canadian measures targeting Al-Qaida and the Taliban and the *Suppression of Terrorism Regulations* and the *Criminal Code*. Cuba and Syria should also be added to this list if the proposed activity involves the export or transfer of US-origin goods or technology.

Canada maintains economic sanctions of various degrees in respect of all of these destinations. In many cases, the sanctions also target selected individuals and entities, and it is therefore necessary to maintain up-to-date lists of names that will form part of the screening process.

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