

25 July 1983

CANADA - ADMINISTRATION OF THE FOREIGN  
INVESTMENT REVIEW ACT

*Report of the Panel adopted on 7 February 1984  
(L/5504 - 30S/140)*

1. Introduction

1.1 In a communication dated 5 January 1982, the United States requested the government of Canada to consult under Article XXII:1 on the administration of the Canadian Foreign Investment Review Act. Among the issues which the United States wished to raise in the consultation was the practice of the government of Canada to enter into agreements with foreign investors according to which these are to give preference to the purchase of Canadian goods over imported goods and to meet certain export performance requirements. The communication was circulated to the contracting parties on 7 January 1982 (L/5280). Since the consultation did not lead to a solution, the United States, in a communication dated 19 March 1982, referred the matter to the CONTRACTING PARTIES in accordance with Article XXIII:2 (L/5308).

1.2 At its meeting on 31 March 1982 the Council agreed to establish a Panel and authorized its Chairman, in consultation with the two parties concerned and with other interested contracting parties, to decide on appropriate terms of reference and, in consultation with the two parties concerned, to designate the Chairman and the members of the Panel.

1.3 At the meeting of the Council on 2 November 1982 the Chairman of the Council informed the Council that these consultations had been held and that the following composition and terms of reference had been agreed:

Composition

Chairman: Mr. T.C. O'Brien

Members: Mr. J.N. Feij  
Mr. M. Ikeda

Terms of Reference

"To examine, in the light of the relevant GATT provisions, the matter referred to the CONTRACTING PARTIES by the United States concerning the administration of the Foreign Investment Review Act of Canada with respect to the purchase of goods in Canada and/or export of goods from Canada by certain firms subject to that Act; and to make such findings as will assist the CONTRACTING PARTIES in making the recommendations or rulings provided for in paragraph 2 of Article XXIII."

1.4 At the Council meeting, a number of delegations expressed doubts whether the dispute between the United States and Canada was one for which the GATT had competence since it involved investment legislation, a subject not covered by the GATT. They therefore reserved their position on the terms of reference (C/M/162, pages 25-26). The representative of the United States said that his government was not calling into question the Canadian investment legislation as such but was complaining about the two specific trade-related issues mentioned in the terms of reference. The representative of Canada said that, in the view of his government, the terms of reference ensured that the examination would touch only on trade matters within the purview of GATT. The Chairman suggested, and the Council so decided, that the terms of reference remain as they stood, that the reservations and statements made be placed on the record and that it be presumed that the Panel would be limited in its activities and findings to within the four corners of GATT.

1.5 The representatives of the contracting parties which had spoken on the matter in the Council were asked by the Chairman of the Panel, in letters dated 20 December 1982, whether they wished to have an opportunity to be heard by the Panel as provided in paragraph 15 of the Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (BISD 26S/213). Argentina asked to be given this opportunity and was heard by the Panel on 25 January 1983. (The views of Argentina are summarized below in paragraphs 4.1 and 4.2).

## 2. Factual Aspects

2.1 The following description of the factual aspects, particularly in paragraphs 2.3, 2.5, 2.7 and 2.12, contains much information about the Foreign Investment Review Act which is not directly at issue in this dispute but is useful in placing the dispute in its general context.

2.2 The Foreign Investment Review Act. In December 1973 the Parliament of Canada enacted the Foreign Investment Review Act. According to Section 2(1) of this Act, the Parliament adopted the law "in recognition that the extent to which control of Canadian industry, trade and commerce has become acquired by persons other than Canadians and the effect thereof on the ability of Canadians to maintain effective control over their economic environment is a matter of national concern" and that it was therefore expedient to ensure that acquisitions of control of a Canadian business or establishments of a new business by persons other than Canadians be reviewed and assessed and only be allowed to proceed if the government had determined that they were, or were likely to be, of "significant benefit to Canada".

2.3 Section 2(2) lists five factors to be taken into account in assessing whether a proposed investment is or is likely to be of significant benefit to Canada. These are:

- (a) The effect of the acquisition or establishment on the level and nature of economic activity in Canada, including, without limiting the generality of the foregoing, the effect on employment, on resource processing, on the utilization of parts, components and services produced in Canada, and on exports from Canada;
- (b) the degree and significance of participation by Canadians in the business enterprise or new business and in any industry or industries in Canada of which the business enterprise or new business forms or would form a part;
- (c) the effect of the acquisition or establishment on productivity, industrial efficiency, technological development, product innovation and product variety in Canada;
- (d) the effect of the acquisition or establishment on competition within any industry or industries in Canada; and
- (e) the compatibility of the acquisition or establishment with national industrial and economic policies, taking into consideration industrial and economic policy objectives enunciated by the government or legislature of any province likely to be significantly affected by the acquisition or establishment.

2.4 Written undertakings given by investors. The Act provides that investors may submit written undertakings on the conduct of the business they are proposing to acquire or establish, conditional on approval by the Canadian government of the proposed acquisition or establishment. The submission of undertakings is not required under the Act but, as the administration of the Act evolved, they are now routinely submitted in support of nearly all larger investment proposals. Many undertakings are the result of negotiations between the investor and the Canadian government. Undertakings given by

investors may deal with any aspect of the conduct of a business, including employment, investment, research and development, participation of Canadian shareholders and managers, productivity improvements as well as practices with respect to purchasing, manufacturing and exports. There are no pre-set formulas or prescriptions for the undertakings.

2.5 Purchase undertakings. Undertakings with respect to the purchase of goods have been given in a variety of forms:

- Some involve best efforts to seek Canadian sources of supply;
- some specify a percentage or amount of purchases of Canadian products;
- some envisage replacement of imports with Canadian-made goods in a specific dollar amount;
- some refer to the purchase of Canadian products, others only to the purchase from Canadian suppliers (whether of domestic or imported goods);
- some involve a commitment to set up a purchasing division in the Canadian Subsidiary; and
- some involve a commitment to consult with federal or provincial industry specialists in drawing up tender lists.

Undertakings on purchases are often but not always conditional on goods being "available", "reasonably available" or "competitively available" in Canada with respect to price, quality, and delivery or other factors specified by the investor.

2.6 Manufacturing undertakings. Some firms have given undertakings to manufacture in Canada products or components of a product used or sold by the firm.

2.7 Export undertakings. The undertakings involving the export of goods have been given in a variety of forms:

- Some involving development of natural resources are predicated on the development of offshore markets;
- some involve a specific export target, expressed as a percentage of output or sales, often to be achieved within a specified time frame;
- some involve assigning to the Canadian business exclusive rights to export either all its products to certain countries or specified products on a world basis;
- some involve a commitment by the investor to assist the Canadian subsidiary in selling its products in foreign markets; and
- some involve commitments that the Canadian business will not be restricted from seeking out and taking advantage of any export opportunities.

2.8 Statistics on the undertakings. The Act came into force on 9 April 1974 with respect to acquisitions and on 15 October 1975 with respect to new businesses. From April 1974 to September 1982, the Government of Canada has rendered decisions on 4,103 investment proposals, of which 2,448 were from the United States. Approximately 90 per cent of the reviewable investment

proposals on which the government has taken a decision have been judged to be of significant benefit to Canada and have, therefore, been allowed. The Panel asked questions about the frequency with which the various types of undertakings have been given. In order to answer these questions the Canadian government reviewed a sample of 181 investments allowed in the month of November in the years 1980, 1981 and 1982. (November was the latest month for which data were available). In this sample, 55 of the investors or 30 per cent of the total gave no undertakings relating to sourcing. The remaining 126 investors gave a total of 178 sourcing undertakings. (Some investors gave more than one sourcing undertaking). Of those 178 sourcing undertakings, 65 per cent referred to the purchase of goods and services from Canadian suppliers or words to that effect, 15 per cent referred to purchase of Canadian produced goods. The remaining 20 per cent were sourcing commitments of other kinds, e.g. to set up a Canadian purchasing division, or to consult with a government body to identify potential Canadian suppliers. This latter 20 per cent also includes undertakings relating solely to the purchase of services. 71 per cent of the undertakings to purchase in Canada or to purchase Canadian produced goods carried a qualification with respect to the availability of goods on competitive terms.

2.9 With respect to export undertakings in the same sample of 181 investments, 97 investors or 54 per cent of the total gave no export undertakings of any kind. The remaining 84 investors gave 96 export undertakings. (Again some investors gave more than one undertaking relating to exports). Of the 96 export undertakings, 32 per cent referred to a quantifiable level of exports, e.g. target value of exports or a percentage of output. The remaining 68 per cent were export undertakings of other kinds, such as an undertaking not to restrict the export activities of the Canadian business, or to actively pursue export opportunities.

2.10 Enforcement of the undertakings. Written undertakings given by firms are legally binding on the investor if the investment is allowed. According to Section 21 of the Act the Minister responsible for the administration of the Act may apply to the courts for a remedial order in the event an investor fails to implement undertakings he has given. The Minister responsible for the Act made the following statement in the Canadian Parliament in 1973 on the enforcement of undertakings:

"In normal circumstances the inability to fulfil undertakings will lead to discussions with the Minister and perhaps to the negotiation of new undertakings. Like any contract, an undertaking can be modified with the consent of both parties. If, however, the failure to comply with an undertaking is clearly the result of changed market conditions - for example, the undertaking to export frisbees is followed by the collapse of the frisbee market - the person would not be held accountable. It should be remembered, however, that some undertakings may be tailored to a range of market expectations."

2.11 All investments that are allowed subject to the Act are monitored by the government of Canada. If the investment involves specific undertakings the investor is asked at regular intervals for a progress report on the implementation of his undertakings. All undertakings are monitored at least once before the file is closed, normally after the fifth anniversary of the date on which the permission to invest was granted. If the investor's progress report reveals a variation from the undertakings, or non-fulfilment of them, the investor is asked to provide a more detailed explanation. Depending on the circumstances, performance of unfulfilled undertakings has so far always been either postponed or waived, or the undertakings have been replaced by revised undertakings. To date, the Minister responsible for the administration of the Act has not applied to the courts to enforce an investor's written undertaking.

2.12 Recent changes in the administration of the Foreign Investment Review Act. During the second half of 1982 some changes were introduced in the administration of the Foreign Investment Review Act, without entailing modifications in the Act itself. Among the most important changes was the decision to raise the threshold for the review of new investments or direct acquisitions under the small business procedures from Can\$ 2 million and 100 employees to Can\$ 5 million and 200 employees. The small business procedures do not require a full review, except under special circumstances. Approximately, 85 per cent of all proposals fall within the small business procedure.

### 3. Main Arguments

3.1 The United States requested the Panel to find that the written undertakings obtained by the Government of Canada under the Foreign Investment Review Act which oblige foreign investors subject to the Act

- (a) to purchase goods of Canadian origin in preference to imported goods or in specified amounts or proportions, or to purchase goods from Canadian sources;
- (b) to manufacture in Canada goods which would be imported otherwise

are inconsistent with Articles III:4, III:5, XI and XVII:1(c) of the General Agreement, and that the undertakings which oblige foreign investors

- (c) to export specified quantities or proportions of their production

are inconsistent with Article XVII:1(c) of the General Agreement, and that any such undertakings therefore constitute a prima facie case of nullification and impairment under Article XXIII of the General Agreement. The United States further requested the Panel to suggest that the CONTRACTING PARTIES recommend that Canada (a) make clear that it will not regard as binding, or seek to enforce in the context of the Foreign Investment Review Act, any undertaking of the kind found to be inconsistent with the General Agreement, and (b) that it cease eliciting and accepting such undertakings as part of investment proposals.

3.2 Canada requested the Panel to find that the purchase undertakings (paragraph 3.1(a)) given by foreign investors are not inconsistent with the provisions of Articles III:4, III:5, XI or XVII:1(c) of the General Agreement, that the export undertakings (paragraph 3.1(c) ) are not inconsistent with the provisions of Article XVII:1(c) and that, were the purchase and/or export undertakings to fall within the provisions of one or more of these Articles, they, would constitute measures within the provisions of Article XX(d). As to the manufacturing undertakings (paragraph 3.1(b)), Canada asked the Panel to find that these do not fall under the Panel's terms of reference.

3.3 Both parties agreed that the issue before the Panel was not the Foreign Investment Review Act itself or Canada's right to regulate the entry and expansion of foreign direct investments, but rather the consistency with the General Agreement of the purchase and export undertakings given by investors subject to the Foreign Investment Review Act.

- (a) Undertakings to purchase goods of Canadian origin in preference to imported goods or in specified amounts or proportions, or to purchase goods from Canadian sources

3.4 Article III:4. The United States contended that the written undertakings which oblige investors to purchase goods of Canadian origin in preference to imported goods or in specified amounts or proportions, or to purchase goods from Canadian sources (henceforth referred to as "purchase undertakings") violated Article III:4 because they constituted requirements giving less favourable treatment to imported products than to like products of national origin.

3.5 In the view of the United States even those undertakings that obliged a firm to purchase goods in Canada whenever "available", "reasonably available", or "competitively available" had the effect of according less favourable treatment to imported goods. Such undertakings prevented the investor from choosing freely between imported and domestic goods since they obliged him to opt in favour of domestic products whenever the availability condition was fulfilled. The provisos "reasonably

available" or "competitively available" were vague and involved value judgements regarding quality, reliability of supply and the like. A firm subject to an undertaking with such a proviso was therefore likely to purchase Canadian goods even when they were less attractive than imported goods in order to avoid possible conflict with Canadian officials monitoring compliance who have a different perspective and apply different value judgements on these matters. Undertakings to purchase from Canadian sources or suppliers (whether the products purchased were domestic or imported) would also result in less favourable treatment to imports than that given to Canadian products because in cases where a product was produced in both Canada and other countries such undertakings would oblige the investor to purchase imports from a Canadian "middleman" (the importer/distributor/retailer), thus forcing the investor to incur additional costs in the form of the middleman's profit if he decided to import, but leaving him free to purchase directly from a Canadian manufacturer, thereby avoiding the additional cost of the "middleman". Even more discrimination against imported products would result in instances in which Canadian sources and suppliers did not stock or distribute imported products sought by the investor.

3.6 Canada held that the purchase undertakings did not constitute laws, regulations or requirements within the meaning of Article III:4. There was no provision in the Foreign Investment Review Act, its regulations or any other Canadian act or regulation which stipulated that any undertaking shall be given by a firm as a condition of investment. While there was an overall requirement under the Act that a foreign investor demonstrate that his proposal, as an overall package, was, or was likely to be, of significant benefit to Canada, it was entirely up to him to choose the means to do this. Frequently, investors chose to offer purchase undertakings in support of their proposals. Canada further stated that the investment screening procedures were not intended nor applied so as to provide protection to Canadian manufacturers or to oblige companies to depart from commercially sound practices. Investors, having decided on their plans for conducting business in Canada, generally had no hesitation in giving undertakings which reflected these plans. Since both the investor and the Canadian government had to act in the context of markets in which the investor's competitors were not subject to undertakings, it was highly unlikely that purchase undertakings would either be offered or sought that departed significantly from the purchasing practices the investor would follow in the absence of the undertaking. Where undertakings were given, they reflected a decision by the investor about how he intended to conduct his business in Canada. Undertakings would only represent a cost to the investor if they did not reflect his business intentions. When investors gave purchase undertakings without any qualification as to the competitive availability of goods in Canada, it was usually because either the investor had already identified his sources of supply, or, given the nature of his business, purchases were ordinarily made locally. A review of the circumstances of the investment proposals specifically cited by the United States in their submission did not support the claim that the undertakings given in these proposals had to be regarded as requirements.

3.7 The United States replied that it was true that the Act itself did not require investors to offer undertakings, but, once given, the undertakings had to be regarded as requirements in the light of the circumstances in which they were offered and accepted and of their legally binding character. No private business would bind its future purchasing practices unless the achievement of some benefit or the avoidance of some penalty was made contingent upon that binding. The investors only offered undertakings in order to obtain the Canadian government's approval of their investment proposals. Moreover, there were many cases in which purchase undertakings were the result of negotiations in which Canada sought new or "improved" undertakings. The government of Canada itself had indicated that most of the work performed by the Foreign Investment Review Agency established under the Foreign Investment Review Act centred on the effort to define and to improve the terms of the original investment proposals<sup>1</sup>. Once the investment proposal had been approved, the undertaking became legally binding on the investor, who was then no longer free to modify his purchase undertaking without the permission

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<sup>1</sup>Proceedings of the House of Commons Standing Committee on Finance, Trade and Economic Affairs of 26 May 1981.

of the government of Canada, regardless of changed circumstances. In the current economy it was difficult to imagine that a company would not alter plans it had made more than a year before unless the alteration of those plans entailed a greater penalty than adherence to them. The threat of legal action and the potential effect of non-compliance on future requests for permission to invest was not lost on enterprises that had given undertakings. Canada replied that, although undertakings were not required, where an investment was allowed which contained undertakings it was both reasonable and necessary for the Canadian government to have a means by which remedial action could be taken in the event an investment was implemented in a manner inconsistent with the authority granted. Enforceability under the law simply held the investor, after he had given the undertaking, to doing what he said he would do. Enforceability served to discourage the presentation of grandiose or inflated statements by the investor of his intentions so as to secure approval of his proposal.

3.8 Canada, citing the panel reports in BISD 7S/60 and 25S/49 as precedents, stated that the word "requirements" in Article III had to be interpreted in conjunction with the terms "laws and regulations" and in this context it should be defined as a mandatory rule of general application applying across-the-board to a particular product or range of products. The undertakings, however, were private contractual obligations of a particular foreign investor. They applied to a specific investment and not to trade in goods generally. The United States replied that the exercise of many governmental functions, and the grant of many benefits within a government's power, could be viewed, or recast to appear, as "private contracts" between firms and the government. To find that such "private contracts" were not requirements within the meaning of Article III would be to invite contracting parties to do by "private contract" what the General Agreement did not permit to be done by laws of general application. There was no basis in the General Agreement or in previous panel reports for asserting that only across-the-board measures applying to purchases of all products of a certain category were subject to GATT obligations.

3.9 Canada stated that the word "requirements" in Article III:4 of the General Agreement should be interpreted in the light of Article 12 of the Havana Charter, which reads in part: "The Members recognize that ..., without prejudice to existing international agreements to which Members are parties, a Member has the right... to determine whether and to what extent and upon what terms it will allow future foreign investments, to prescribe and give effect on just terms to requirements as to the ownership of existing and future investments and to prescribe and give effect to other reasonable requirements with respect to existing and future investments". The drafting history of the General Agreement revealed that it was the intention of the drafters of the General Agreement that the extent of the rights and obligations under the General Agreement were to be consistent with, and defined within the broader context of, the Havana Charter. The draftsmen were working within a conceptual framework that encompassed both trade and investment, and rights and obligations with respect to both. GATT Article III was amended in 1948 to incorporate the text of the Havana Charter on national treatment. Canada was not arguing that the Havana Charter was in force but rather that one could not read into the General Agreement obligations which the drafters of the General Agreement had not intended it to contain. Given that it was agreed that the provisions of the Havana Charter were to be interpreted as a consistent whole, it was reasonable to conclude that the meaning of the word "requirements" in the Charter's national treatment provision corresponding to Article III of the General Agreement did not encompass "requirements as to ownership" or "other reasonable requirements" allowed under the Charter's investment provisions. Although the Chapter of the Charter dealing with investment was not incorporated into the General Agreement, it was one of the Chapters the general principles of which the contracting parties, in Article XXIX of the General Agreement, agreed to observe to the fullest extent of their executive authority pending the ratification of the Charter. It was therefore reasonable to assume that it had not been the intention of the drafters of the a General Agreement to include within the meaning of the words "requirements" in Article III of the General Agreement those "requirements" provided for under Article 12 of the Havana Charter. Thus, if the Panel were tending towards an interpretation that undertakings were requirements, which in Canada's view they were not, they would be requirements within the meaning of Article 12 of the Havana Charter.

3.10 The United States replied that Canada was asking the Panel to decide that a provision in a draft agreement which never entered into force be interpreted to override specific obligations of the GATT. The Havana Charter provisions on investment, had they entered into force, would most likely not have been interpreted to override the Charter's national treatment obligation. A broad range of requirements - for instance those relating to the employment of nationals, to management, etc. - could be imposed without conflict with the obligation to grant to imported products no less favourable treatment than to products of domestic origin. As a matter of common sense and normal interpretation of an international agreement, the requirements that were contrary to another specific obligation of the Charter would not have been interpreted to be a "reasonable" requirement within the meaning of the Charter's investment provisions.

3.11 The United States pointed out that, after the Charter had been abandoned, Article III had been amended but not to exempt trade-related requirements affecting foreign investors. Canada replied that Article III was last amended in 1948 whereas Article XXIX went into force in 1952.

3.12 Article III:5. The United States contended that purchase undertakings which obliged the investor to purchase in Canada a specified amount or a proportion of his requirements constituted internal quantitative regulations relating to the investor's processing and use of products and that they were therefore contrary to Article III:5. Canada stated that the Foreign Investment Review Act did not establish any internal quantitative regulations. In the relatively few cases in which investors had given purchase undertakings that referred to specific amounts or proportions of the investors requirements, the figures mentioned reflected the investor's expectations. Regulations were, in the view of Canada, subsidiary rules of general application promulgated by the executive pursuant to an existing legislative enactment. The word "regulations" in Article III:5 involved a rule of general application as was the case in the previous Panel reports which involved Article III:5 (BISD 11S/95 and 25S/49). The purchase undertakings were firm-specific and did not relate generally to the international trade of the goods in question; they could therefore not be regarded as "regulations" within the meaning of Article III:5. The United States replied that each undertaking obviously did not, by itself, have the same degree of effect as a general regulation applicable to an entire industry. But the effect of such undertakings was to restrict the internal market for various imported products by requiring individual firms to use specified amounts or proportions of Canadian products.

3.13 Article XI. The United States claimed that the purchase undertakings operated as restrictions on the importation of products into Canada and were therefore contrary to Article XI. In the view of Canada there was a fundamental distinction in the General Agreement between measures affecting the importation of products and measures affecting imported products. The former were regulated by Article XI which clearly spoke of "importation" and the latter by Article III which referred to "imported products". If Article XI were interpreted to cover also internal measures affecting imported products Article III would have no function. The United States said that, though Article XI was primarily aimed at traditional import quota systems, the language of the Article was broad enough to cover also other, similarly restrictive non-tariff barriers not implemented or enforced at the border. In the United States' view the purpose of the undertakings was to limit imports and reserve a portion of the internal market for Canadian products, which Article XI was intended to prohibit.

3.14 Article XVII:1(c). The United States asserted that the purchase undertakings prevented the investors from acting solely in accordance with commercial considerations and that they therefore violated Canada's obligations under Article XVII:1(c). Canada replied that Article XVII:1 only extended to state-trading and other enterprises the most-favoured-nation principle, and whether or not the investor was prevented from acting in accordance with commercial considerations was therefore irrelevant given the meaning of this Article. A careful research which Canada had undertaken into the drafting history had revealed no reference to national treatment in the discussions leading to the adoption of

Article XVII:1. Under Article 26 of the United States "Suggested Charter for an International Trade Organization of the United Nations", which served as a basis for the London Conference in October-November 1946, state-trading enterprises were to accord "non-discriminatory treatment, as compared with the treatment accorded to the commerce of any country other than that in which the enterprise is located." At the London Conference the non-discrimination obligation was reformulated to read: "... the commerce of other Members shall be accorded treatment no less favourable than that accorded to the commerce of any country, other than that in which the enterprise is located... ". The formulation of the non-discrimination obligation contained in Article XVII went back to a draft adopted at the 1947 Geneva Conference. If the drafting changes introduced then had been intended to include the national treatment obligation in the provisions on state-trading, this fundamental change would have been referred to in the extensive records of the drafting sessions. One reference to the Article on state-trading in the records of the Geneva Conference (E/PC/T/A/SR/10, page 34) confirmed in the view of Canada that this Article was understood to establish only a most-favoured-nation obligation: a delegate had said in a discussion on government procurement that the Article on state-trading referred only "to most-favoured-nation treatment and not to national treatment" and had then proposed that, in drafting rules on government procurement, "you have got to stick to most-favoured-nation treatment as you have in state-trading."

3.15 The United States stated that it disagreed with the Canadian interpretation for two reasons. First, paragraph 1(a) spoke of principles of non-discriminatory treatment. Were the most-favoured-nation principle the only principle intended to be covered, the word principle would not have been used in the plural. Second, paragraph 2 of Article XVII would be unnecessary if the most-favoured-nation principle of non-discriminatory treatment were the only principle covered by paragraph 1(a). Paragraph 2 permitted contracting parties to give less favourable treatment to imports in comparison to domestic products when purchasing for the consumption of the government. This exception from the national treatment obligation would be superfluous if the term "principles of non-discriminatory treatment" only covered the principle of most-favoured-nation treatment.

3.16 Canada said that Article XVII:1(b), and the principles of "commercial considerations" and "adequate opportunity to compete" it contained, were intended to define the most-favoured-nation treatment principle with respect to state-trading, contained in Article XVII:1(a). This was made clear by the opening clause of paragraph (b) which read: "The provisions of sub-paragraph (a) of this paragraph shall be understood to require...". The reference to "commercial considerations" in this context permitted a derogation from the most-favoured-nation principle; it did not impose an additional obligation of broad import, as the United States suggested. The obligation in Article XVII:1(c) was that a contracting party shall not prevent any enterprise from acting in accordance with the principles of XVII:1(a) and 1(b). The word principle was used in the plural because the most-favoured-nation obligation in the General Agreement involved a number of principles such as those set out in Article I, Article IV on screen quotas for films, and Article XIII concerning import quotas. In response to the argument that paragraph 2 of Article XVII would be unnecessary if the most-favoured-nation principle of non-discriminatory treatment were the only principle covered by paragraph 1(a), Canada stated that a reference in the Geneva Conference to the Article on state-trading (E/PC/T/A/SR/37, page 7) established that paragraph 2 of Article XVII did not involve the national treatment principle. Further evidence of the most-favoured-nation character of Article XVII was demonstrated by the fact that Article XVII:1(a) dealt with the purchases or sales of state enterprises involving either imports or exports. The terms "imports" and "exports" described the process of a product crossing a border and clearing customs. Once the product had entered or left the country, it was an "imported" or "exported" product. (Thus Article III spoke of "imported" products.) The scope of Article XVII was therefore limited to purchases or sales abroad by the state enterprise. It was not concerned with the treatment by the state-trading enterprise of imported or domestic products in its domestic market.

(b) Undertakings to manufacture in Canada goods which would be imported otherwise

3.17 The United States stated that undertakings which required a firm to manufacture goods in Canada with the purpose of substituting a domestically produced good for one that would be imported in the absence of the undertaking (henceforth referred to as manufacturing undertakings) violated Article III:4. Such undertakings reserved a portion of the internal market for products of domestic origin, to the exclusion of imported products. Undertakings obliging the investor to manufacture in Canada specified parts or components of a particular product were also inconsistent with Article III:5 because they constituted internal quantitative regulations relating to the mixture, processing or use of products which required that a specified amount or proportion of a product be supplied from domestic sources.

3.18 Canada stated that Article III:4 did not deal with the manufacture or production of goods and therefore did not apply to manufacturing undertakings. The undertakings to manufacture parts or components of particular products in Canada reflected the individual investor's intention and were firm-specific. They were therefore not "regulations" within the meaning of Article III:5. In the view of both parties, their arguments on the applicability or non-applicability of Articles XI and XVII:1(c) to purchase undertakings also applied to manufacturing undertakings (see paragraphs 3.4 - 3.16 above).

3.19 In the view of Canada the manufacturing undertakings were not only fully in conformity with its obligations under GATT but also outside the Panel's terms of reference. It therefore requested the Panel not to examine these undertakings.

(c) Undertakings to export specific amounts or proportions of production

3.20 The United States stated that Article XVII:1(c), which prohibited government interference with the operation of commercial considerations, was also applicable to undertakings to export specified amounts or proportions of production. The export levels of companies subject to such undertakings could not be assumed to be the result of a decision-making process based on commercial considerations. No enterprise would bind itself voluntarily to export fixed amounts or proportions of its production given the uncertainty of markets and conditions of competition. Once the undertakings were accepted, the investor could not adjust its export sales in accordance with commercial considerations, but was dependent on the consent of the Canadian government to make a change in the undertaking. He might therefore be forced to dump products abroad to meet his obligations.

3.21 Canada reiterated that Article XVII:1 only contained a most-favoured-nation obligation and could therefore not be applied to export undertakings, none of which made distinctions among contracting parties. Canada also rejected the contention that an investor might dump goods in order to fulfil an undertaking. This argument lacked credibility because export undertakings were given by the investors on the basis of their expectations of future export market prospects and in the knowledge of the flexible manner in which Canada monitored compliance with the undertakings.

(d) Article XX(d)

3.22 Canada contended that, in the event that the Panel were to consider the undertakings to be inconsistent with Articles III, XI or XVII, then they would fall within the exception provided for in Article XX(d) of the General Agreement. Within the meaning of Article XX(d), the Foreign Investment Review Act constituted a law which was not inconsistent with the provisions of the General Agreement and the administrative practices under that Act with respect to undertakings fell well within the scope of the types of measures envisaged under this Article as being necessary to secure compliance with this law. Under any scheme under which a state granted authority to a foreign investor to invest in its territory,

there had to be some means of ascertaining the nature of the investment for which authority was being granted and that the investment was implemented in a manner consistent with the authority granted. The written undertakings describing the intentions of investors served both these purposes. They were the means by which the investment for which authority was being granted was defined with some precision and, together with the monitoring procedures of the government, buttressed by Sections 19 to 22 of the Act, they were also the means by which the government ensured that investments were implemented within the terms of the authority granted.

3.23 If the government did not have the possibility to enforce undertakings the only recourse it would have in a case of non-implementation of the terms of the authority granted to invest would be to render the investment nugatory. This could entail economic hardship and loss of employment. The enforceability of undertakings and their flexible application provided a reasonable recourse for the government in cases of non-implementation of the proposal as allowed. Moreover, undertakings provided the government with a means of assessing, with confidence, that a proposed investment is, or is likely to be, of significant benefit. Undertakings may be provided with respect to any aspect of the proposed investment as set out in the criteria listed in the Act to be taken into account in assessing significant benefit. An investor's plans with respect to the use of Canadian goods and to exports may properly be considered in assessing the effect of a proposed investment. Many investors submitting proposals, including those involving services and distributorships, may have no other means than through purchase or export undertakings to demonstrate significant benefit. If purchase and export undertakings were not permitted, many potential investors would be denied an equitable opportunity to demonstrate significant benefit.

3.24 The measures the Canadian government took to secure compliance with the Foreign Investment Review Act were, insofar as they related to the purchase or sale of goods, identical in all respects to the measures pertaining to any other aspects of investments allowed under the law. The Canadian practices in this regard were therefore not disguised restrictions on trade within the meaning of the opening sentence of Article XX. The detailed explanation given on the need for undertakings also showed that the undertakings and related administrative practices were not disguised restrictions on trade.

3.25 The United States stated that the undertakings at issue were not necessary to implement the Foreign Investment Review Act and that they constituted disguised restrictions on foreign trade. Two of the conditions of the Article XX(d) exception were therefore not met. The Foreign Investment Review Act itself did not require any undertakings, not to mention undertakings requiring preference for purchase or use of Canadian products or adherence to export performance targets. The Act itself required only that investment proposals be submitted for review to determine whether the proposal was, or was likely to be, of significant benefit to Canada. The effect of the investment on the use of Canadian parts and components and on exports was only one of many factors to be taken into account by the government of Canada in assessing whether a proposal was, or was likely to be, of significant benefit to Canada. Eliciting or accepting binding undertakings to give preference to Canadian products or to meet export targets was therefore an exercise of administrative authority under the Act, rather than a measure necessary to secure compliance with the Act. The undertakings at issue also operated as disguised restrictions on international trade. A preference requiring purchase or use of domestically produced goods obviously restricted trade. Export performance requirements restricted trade by creating artificial export targets for products with which the industries of other contracting parties had to compete. The undertakings at issue, moreover, went far beyond what was necessary to address the concerns that had led to the enactment of the Foreign Investment Review Act.

#### 4. Position of Argentina

4.1 Argentina was heard by the Panel in accordance with paragraph 15 of the Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (see paragraph 1.5 above).

Argentina said that a distinction should be made between the purchase and export undertakings and their compatibility with the General Agreement on the one hand, and Canada's investment legislation as such on the other. While the former subject could be considered as falling within the competence of GATT, the latter clearly fell outside the purview of the General Agreement. In this connection Argentina recalled that it had been decided not to include the question of investments in the Ministerial declaration in November 1982. The question of GATT competence would need to be taken into consideration by the Panel in interpreting its terms of reference.

4.2 Argentina further said the dispute before the Panel involved two developed contracting parties. The provisions and arguments invoked against Canada were not necessarily those which could legitimately be invoked against developing countries, considering the protection which those countries had the right to grant under the General Agreement to their developing industries. Argentina asked the Panel to take this into account in its deliberations.

## 5. Findings

### (a) General

5.1 In view of the fact that the General Agreement does not prevent Canada from exercising its sovereign right to regulate foreign direct investments, the Panel examined the purchase and export undertakings by investors subject to the Foreign Investment Review Act of Canada solely in the light of Canada's trade obligations under the General Agreement. This approach is in accordance with the Chairman of the Council's conclusions at the close of the discussion of this question at the Council meeting of 2 November 1982.

5.2 In its statement before the Panel, Argentina also pointed out that the provisions and arguments invoked against Canada in this case were not necessarily those which could be legitimately invoked against less-developed contracting parties, given rights to protect national industries which these contracting parties enjoyed under the General Agreement. The Panel recognizes that in disputes involving less-developed contracting parties full account should be taken of the special provisions in the General Agreement relating to these countries (such as Article XVIII:C). The Panel did not examine the issues before it in the light of these provisions since the dispute only involved developed contracting parties.

5.3 The Panel considered that the examination of undertakings to manufacture goods which would be imported otherwise, as requested by the United States (paragraphs 3.1(b), and 3.17 to 3.19 above), was not covered by its terms of reference which only refer to "the purchase of goods in Canada and/or the export of goods from Canada". Accordingly the Panel did not examine this question.

### (b) Undertakings to purchase goods of Canadian origin in preference to imported goods or in specified amounts or proportions, or to purchase goods from Canadian sources

5.4 Article III:4. The Panel first examined whether the purchase undertakings are to be considered "laws, regulations or requirements" within the meaning of Article III:4. As both parties had agreed that the Foreign Investment Review Act and the Foreign Investment Review Regulations - whilst providing for the possibility of written undertakings - did not make their submission obligatory, the question remained whether the undertakings given in individual cases are to be considered "requirements" within the meaning of Article III:4. In this respect the Panel noted that Section 9(c) of the Act refers to "any written undertakings ... relating to the proposed or actual investment given by any party thereto conditional upon the allowance of the investment" and that Section 21 of the Act states that "where a person who has given a written undertaking ... fails or refuses to comply with such undertaking" a court order may be made "directing that person to comply with the undertaking". The Panel further noted that

written purchase undertakings - leaving aside the manner in which they may have been arrived at (voluntary submission, encouragement, negotiation, etc.) - once they were accepted, became part of the conditions under which the investment proposals were approved, in which case compliance could be legally enforced. The Panel therefore found that the word "requirements" as used in Article III:4 could be considered a proper description of existing undertakings.

5.5 The Panel could not subscribe to the Canadian view that the word "requirements" in Article III:4 should be interpreted as "mandatory rules applying across-the-board" because this latter concept was already more aptly covered by the term "regulations" and the authors of this provision must have had something different in mind when adding the word "requirements". The mere fact that the few disputes that have so far been brought before the CONTRACTING PARTIES regarding the application of Article III:4 have only concerned laws and regulations does not in the view of the Panel justify an assimilation of "requirements" with "regulations". The Panel also considered that, in judging whether a measure is contrary to obligations under Article III:4, it is not relevant whether it applies across-the-board or only in isolated cases. Any interpretation which would exclude case-by-case action would, in the view of the Panel, defeat the purposes of Article III:4.

5.6 The Panel carefully examined the Canadian view that the purchase undertakings should be considered as private contractual obligations of particular foreign investors vis-à-vis the Canadian government. The Panel recognized that investors might have an economic advantage in assuming purchase undertakings, taking into account the other conditions under which the investment was permitted. The Panel felt, however, that even if this was so, private contractual obligations entered into by investors should not adversely affect the rights which contracting parties, including contracting parties not involved in the dispute, possess under Article III:4 of the General Agreement and which they can exercise on behalf of their exporters. This applies in particular to the rights deriving from the national treatment principle, which - as stated in Article III:1 - is aimed at preventing the use of internal measures "so as to afford protection to domestic production".

5.7 The Panel then examined the question whether less favourable treatment was accorded to imported products than that accorded to like products of Canadian origin in respect of requirements affecting their purchase. For this purpose the Panel distinguished between undertakings to purchase goods of Canadian origin and undertakings to use Canadian sources or suppliers (irrespective of the origin of the goods), and for both types of undertakings took into account the qualifications "available", "reasonably available", or "competitively available".

5.8 The Panel found that undertakings to purchase goods of Canadian origin without any qualification exclude the possibility of purchasing available imported products so that the latter are clearly treated less favourably than domestic products and that such requirements are therefore not consistent with Article III:4. This finding is not modified in cases where undertakings to purchase goods of Canadian origin are subject to the qualification that such goods be "available". It is obvious that if Canadian goods are not available, the question of less favourable treatment of imported goods does not arise.

5.9 When these undertakings are conditional on goods being "competitively available" (as in the majority of cases) the choice between Canadian or imported products may frequently coincide with normal commercial considerations and the latter will not be adversely affected whenever one or the other offer is more competitive. However, it is the Panel's understanding that the qualification "competitively available" is intended to deal with situations where there are Canadian goods available on competitive terms. The Panel considered that in those cases where the imported and domestic product are offered on equivalent terms, adherence to the undertaking would entail giving preference to the domestic product. Whether or not the foreign investor chooses to buy Canadian goods in given practical situations, is not at issue. The purpose of Article III:4 is not to protect the interests of the foreign investor but to ensure that goods originating in any other contracting party benefit from treatment no less favourable than domestic (Canadian) goods, in respect of the requirements that affect their purchase (in

Canada). On the basis of these considerations, the Panel found that a requirement to purchase goods of Canadian origin, also when subject to "competitive availability", is contrary to Article III:4. The Panel considered that the alternative qualification "reasonably available" which is used in some cases, is a fortiori inconsistent with Article III:4, since the undertaking in these cases implies that preference has to be given to Canadian goods also when these are not available on entirely competitive terms.

5.10 The Panel then turned to the undertakings to buy from Canadian suppliers. The Panel did not consider the situation where domestic products are not available, since such a situation is not covered by Article III:4. The Panel understood the choice under this type of requirement to apply on the one hand to imported goods if bought through a Canadian agent or importer and on the other hand to Canadian goods which can be purchased either from a Canadian "middleman" or directly from the Canadian producer. The Panel recognized that these requirements might in a number of cases have little or no effect on the choice between imported or domestic products. However, the possibility of purchasing imported products directly from the foreign producer would be excluded and as the conditions of purchasing imported products through a Canadian agent or importer would normally be less advantageous, the imported product would therefore have more difficulty in competing with Canadian products (which are not subject to similar requirements affecting their sale) and be treated less favourably. For this reason, the Panel found that the requirements to buy from Canadian suppliers are inconsistent with Article III:4.

5.11 In case undertakings to purchase from Canadian suppliers are subject to a "competitive availability" qualification, as is frequent, the handicap for the imported product is alleviated as it can be obtained directly from the foreign producer if offered under more competitive conditions than via Canadian sources. In those cases in which Canadian sources and a foreign manufacturer offer a product on equivalent terms, adherence to the undertaking would entail giving preference to Canadian sources, which in practice would tend to result in the purchase being made directly from the Canadian producer, thereby excluding the foreign product. The Panel therefore found that requirements to purchase from Canadian suppliers, also when subject to competitive availability, are contrary to Article III:4. As before (paragraph 5.9), the Panel considered that the qualification "reasonably available" is a fortiori inconsistent with Article III:4.

5.12 The Panel considered the Canadian view expressed in paragraph 3.9 above that the word "requirements" in Article III:4 of the General Agreement should be interpreted in the light of Article 12 of the Havana Charter, the general principles of which the contracting parties, in Article XXIX of the General Agreement, agreed to observe to the fullest extent of their executive authority. The Panel noted that the deletion of Article XXIX of the General Agreement was proposed in 1955 and accepted by all but one contracting party<sup>1</sup>, and that - although this Article is technically still in force - it refers to an instrument which itself has never been implemented and the acceptance of which is no longer pending as is assumed in Article XXIX. This leaves considerable doubt as to the manner in which its provisions would have been interpreted if they had entered into force. The Panel further noted that paragraph 1(c) of Article 12 of the Charter was to apply "without prejudice to existing international agreements to which Members are parties", and that paragraph 1(a), (b) and (d) as well as paragraphs 2 and 3 of this Article tended to encourage international investments (including international co-operation in this field). It is therefore doubtful whether paragraph 1(c) which reserved the rights of Members to prescribe "reasonable requirements" should by itself be considered as a "general principle" in the sense of Article XXIX:1 of the General Agreement. The wording of this latter provision suggests that it was not the intention of its drafters that contracting parties should "undertake to observe to the fullest extent of their executive authority" what they would in any case judge to be in their own interest, nor that they should invoke the Charter to detract from their obligations under the General Agreement, but rather that they should observe general principles which reinforced or added to these obligations.

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<sup>1</sup>Protocol Amending Part I and Articles XXIX and XXX of the General Agreement on Tariffs and Trade, annexed to the Final Act adopted at the Ninth Session of the CONTRACTING PARTIES, published 10 March 1955. This protocol did not enter into force (see Status of Legal Instruments, page 2-7.1).

In the light of the foregoing facts and considerations the Panel could not subscribe to the assumption that the drafters of Article III had intended the term "requirements" to exclude requirements connected with the regulation of international investments and did not find anything in the negotiating history, the wording, the objectives and the subsequent application of Article III which would support such an interpretation.

5.13 Article III:5. The Panel then considered the United States contention that purchase undertakings which obliged the investor to purchase in Canada a specified amount or proportion of his requirements were also contrary to Article III:5. The Panel noted that these cases had been characterized by both parties as purchase undertakings (paragraph 2.5) and had also been presented as such by the United States (paragraphs 3.1(a) and 3.12). In this regard the Panel noted that in paragraph 5 of Article III the conditions of purchase are not at issue but rather the existence of internal quantitative regulations relating to the mixture, processing or use of products (irrespective of whether these are purchased or obtained by other means). On the basis of the presentations made, the Panel (which was unable to go into a detailed examination of individual cases where purchase undertakings referred to percentages or specific amounts) therefore did not find sufficient grounds to consider the undertakings in question in the light of Article III:5, but came to the conclusion that they fell under the purchase requirements that had been found inconsistent with Article III:4.

5.14 Article XI. The United States further asked the Panel to find that the purchase undertakings operate as restrictions on the importation of products into Canada and are therefore contrary to Article XI:1. The Panel shares the view of Canada that the General Agreement distinguishes between measures affecting the "importation" of products, which are regulated in Article XI:1, and those affecting "imported products", which are dealt with in Article III. If Article XI:1 were interpreted broadly to cover also internal requirements, Article III would be partly superfluous. Moreover, the exceptions to Article XI:1, in particular those contained in Article XI:2, would also apply to internal requirements restricting imports, which would be contrary to the basic aim of Article III. The Panel did not find, either in the drafting history of the General Agreement or in previous cases examined by the CONTRACTING PARTIES, any evidence justifying such an interpretation of Article XI. For these reasons, the Panel, noting that purchase undertakings do not prevent the importation of goods as such, reached the conclusion that they are not inconsistent with Article XI:1.

5.15 Article XVII:1(c). The United States requested the Panel to find that the purchase undertakings obliging investors to give less favourable treatment to imported products than to domestic products prevent the investors from acting solely in accordance with commercial considerations and that they therefore violate Canada's obligations under Article XVII:1(c).

5.16 The Panel takes the view that, through its reference to sub-paragraph (a), paragraph 1(c) of Article XVII of the General Agreement imposes on contracting parties the obligation to act in their relations with state-trading and other enterprises "in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders". This obligation is defined in sub-paragraph (b), which declares, inter alia, that these principles are understood to require the enterprises to make their purchases and sales solely in accordance with commercial considerations. The fact that sub-paragraph (b) does not establish a separate general obligation to allow enterprises to act in accordance with commercial considerations, but merely defines the obligations set out in the preceding sub-paragraph, is made clear through the introductory words "The provisions of sub-paragraph (a) of the paragraph shall be understood to require ...". For these reasons, the Panel considers that the commercial considerations criterion becomes relevant only after it has been determined that the governmental action at issue falls within the scope of the general principles of non-discriminatory treatment prescribed by the General Agreement. The Panel saw

great force in Canada's argument that only the most-favoured-nation and not the national treatment obligations fall within the scope of the general principles referred to in Article XVII:1(a). However, the Panel did not consider it necessary to decide in this particular case whether the general reference to the principles of non-discriminatory treatment referred to in Article XVII:1 also comprises the national treatment principle since it had already found the purchase undertakings at issue to be inconsistent with Article III:4 which implements the national treatment principle specifically in respect of purchase requirements.

(c) Undertakings to export specified quantities or proportions

5.17 The United States requested the Panel to find that the undertakings which oblige investors to export specified quantities or proportions of their production are inconsistent with Article XVII:1(c) because the export levels of companies subject to such undertakings cannot be assumed to be the result of a decision-making process based on commercial considerations.

5.18 As explained in paragraph 5.16 above, Article XVII:1(b) does not establish a separate obligation to allow enterprises to act in accordance with commercial considerations but merely defines the obligation of the enterprises, set out in sub-paragraph (a) of Article XVII:1, to "act in a manner consistent with the general principles of non-discriminatory treatment" prescribed in the General Agreement. Hence, before applying the commercial considerations criterion to the export undertakings, the Panel first had to determine whether Canada, in accepting investment proposals on the condition that the investor export a certain quantity or proportion of his production, acts inconsistently with any of the general principles of non-discriminatory treatment prescribed in the General Agreement. The Panel found that there is no provision in the General Agreement which forbids requirements to sell goods in foreign markets in preference to the domestic market. In particular, the General Agreement does not impose on contracting parties the obligation to prevent enterprises from dumping. Therefore, when allowing foreign investments on the condition that the investors export a certain amount or proportion of their production, Canada does not, in the view of the Panel, act inconsistently with any of the principles of non-discriminatory treatment prescribed by the General Agreement for governmental measures affecting exports by private traders. Article XVII:1(c) is for these reasons not applicable to the export undertakings at issue.

(e) Article XX(d)

5.19 Canada contended that, in the event that the Panel were to consider the purchase undertakings to be inconsistent with Article III:4, these would fall within the exception provided for in Article XX(d) of the General Agreement because, within the meaning of that provision, the Foreign Investment Review Act constitutes "a law which is not inconsistent with the provisions of the General Agreement" and the purchase undertakings are "measures necessary to secure compliance" with that law.

5.20 Since Article XX(d) is an exception to the General Agreement it is up to Canada, as the party invoking the exception, to demonstrate that the purchase undertakings are necessary to secure compliance with the Foreign Investment Review Act. On the basis of the explanations given by Canada the Panel could not, however, conclude that the purchase undertakings that were found to be inconsistent with Article III:4 are necessary for the effective administration of the Act. The Panel is in particular not convinced that, in order to achieve the aims of the Act, investors submitting applications under the Act had to be bound to purchasing practices having the effect of giving preference to domestic products. It was not clear to the Panel why a detailed review of investment proposals without purchasing requirements would not be sufficient to enable the Canadian government to determine whether the proposed investments were or were likely to be of significant benefit to Canada within the meaning of Section 2 of the Foreign Investment Review Act.

(f) Other undertakings

5.21 To avoid any misunderstanding the Panel wishes to underline that some of the undertakings mentioned in paragraph 2.5 above, such as undertakings to set up a purchasing division in the Canadian subsidiary or to consult with Canadian industry specialists in drawing up tender lists, - although related to the purchase of goods in Canada - have not been the subject of United States contention in the Panel proceedings and were therefore not examined. The Panel also wishes to stress that the considerations relating to the purchase undertakings examined in paragraphs 5.1 to 5.20 remain strictly without prejudice to the status of other undertakings agreed upon in the context of the Foreign Investment Review Act and referred to in paragraph 2.4 but pertaining to employment, investment, research and development and other subjects which clearly fall outside the scope of the General Agreement.

6. Conclusions

6.1 In the light of the considerations set out in paragraphs 5.4 to 5.12, the Panel concluded that the practice of Canada to allow certain investments subject to the Foreign Investment Review Act conditional upon written undertakings by the investors to purchase goods of Canadian origin, or goods from Canadian sources, is inconsistent with Article III:4 of the General Agreement according to which contracting parties shall accord to imported products treatment no less favourable than that accorded to like products of national origin in respect of all internal requirements affecting their purchase. The Panel further concluded that in relation to Article III:5, there were insufficient grounds to consider the purchase undertakings which refer to specific amounts or proportions under its provisions (paragraph 5.13). Noting that purchase undertakings do not prevent the importation of goods as such, the Panel reached the conclusion that they are not inconsistent with Article XI:1 (paragraph 5.14). Further, having reached a decision on purchase requirements in relation to Article III:4, the Panel did not consider it necessary to make a specific finding on the interpretation of Article XVII:1(c) in the context of this case, and therefore did not reach a separate conclusion regarding the consistency of purchase requirements with this provision (paragraphs 5.15 and 5.16). On the basis of the evidence before it, the Panel could not conclude that the purchase undertakings that were found to be inconsistent with Article III:4 are necessary within the meaning of Article XX(d) for the effective administration of the Foreign Investment Review Act (paragraphs 5.19 to 5.20).

6.2 For the reasons set out in paragraphs 5.17 and 5.18, the Panel found that Canada does not act inconsistently with Article XVII:1(c) of the General Agreement when allowing certain investments subject to the Foreign Investment Review Act conditional upon undertakings by investors to export a specified amount or proportion of their production. Finally, the Panel considered that the examination of undertakings to manufacture goods which would be imported otherwise was not covered by its terms of reference (paragraph 5.3).

6.3 The Panel is aware that inconsistency with Article III:4 was not intended by the Foreign Investment Review Act, which does not require the submission of undertakings, but that this practice developed as the administration of the Act evolved, to the point that "they are now routinely submitted in support of nearly all larger investment proposals" (paragraph 2.4 above). This evolution may partly reflect the need for foreign investors to demonstrate, by this and other means, to the Canadian administration that their proposed investment would be of significant benefit to Canada. The Panel sympathizes with the desire of the Canadian authorities to ensure that Canadian goods and suppliers would be given a fair chance to compete with imported products. However, the Panel holds the view that the purchase requirements under examination do not stop short of this objective but tend to tip the balance in favour of Canadian products, thus coming into conflict with Article III:4.

6.4 The Panel recognizes that purchase requirements may reflect plans which the investors would have carried out also in the absence of the undertakings; that undertakings with such provisos as "competitive availability" have an adverse impact on imported products only in those cases in which imported and Canadian goods are offered on equivalent terms; and that the undertakings are enforced flexibly. Many of the undertakings, though technically in violation with the General Agreement, therefore possibly do not nullify or impair benefits accruing to the United States under the General Agreement. However, understanding GATT practice, a breach of a rule is presumed to have an adverse impact on other contracting parties (BISD 26S/216), and the Panel also proceeded on this assumption.

6.5 As to the extent to which purchase requirements reflect plans of the investors, the Panel does not consider it relevant nor does it feel competent to judge how the foreign investors are affected by the purchase requirements, as the national treatment obligations of Article III of the General Agreement do not apply to foreign persons or firms but to imported products and serve to protect the interests of producers and exporters established on the territory of any contracting party. Purchase requirements applied to foreign investors in Canada which are inconsistent with Article III:4 can affect the trade interests of all contracting parties, and impinge upon their rights.

6.6 The Panel carefully considered the effects of the purchase requirements on trade. The Panel concluded that an evaluation of these effects would entail scrutiny and analysis of the implementation of several thousands of often differently worded undertakings as well as speculation on what the purchasing behaviour of foreign investors would have been in their absence. The Panel could not undertake such an evaluation and it is therefore not in a position to judge how frequently the purchase requirements cause investors to act differently than they would have acted in the absence of the undertakings and how frequently they therefore adversely affect the trade interests of other contracting parties. The Panel, however, believes that an evaluation of the trade effects was not directly relevant to its findings because a breach of a GATT rule is presumed to have an adverse impact on other contracting parties (see paragraph 6.4 above).

6.7 Taking into account all the above considerations, the Panel considered what scope might exist for modifications of administrative practices under the Foreign Investment Review Act so as to bring them into conformity with Canada's obligations under the General Agreement. In this connection, the Panel considered the following Canadian submission contained in paragraph 3.6 of particular relevance:

"Since both the investor and the Canadian government had to act in the context of markets in which the investor's competitors were not subject to undertakings, it was highly unlikely that purchase undertakings would either be offered or sought that departed significantly from the purchasing practices the investor would follow in the absence of the undertaking."

On the face of it, this statement and the above-mentioned considerations seem to suggest that there may be scope for adapting the administration of the Foreign Investment Review Act in such a way as to remove the implication that imported products are treated less favourably than domestic products. The Panel notes that in a previous case another Panel had been confronted with a somewhat similar situation and had suggested a solution along these lines.<sup>1</sup> In the case at issue, the Panel considers that the Canadian authorities might resolve the problem by ensuring that any future purchase undertakings will not provide more favourable treatment to Canadian products in relation to imported products. The Panel's findings also apply to existing purchase undertakings. However, the Panel recognizes that an immediate application of its findings to these undertakings might cause difficulties in the administration of the Foreign Investment Review Act. Consequently, the Panel suggests that the CONTRACTING PARTIES recommend that Canada bring the existing purchase undertakings as soon as possible into conformity with its obligations under the General Agreement, and invite Canada to report on the steps taken to that effect before the end of 1985.

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<sup>1</sup>BISD 7S/66-67: "The Panel considered, furthermore, that if the considered view of the Italian Government was that these credit facilities had not influenced the terms of competition on the Italian market, there would not seem to be a serious problem in amending the operation of the Law so as to avoid any discrimination as regards these credit facilities between the domestic and imported tractors and agricultural machinery."