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ARTICLES / ARTICLES

Issues in Canadian Cross-Border Financing

David Nadler and Lisa Mantello***

Introduction

In our increasingly global financing market, Canadian entities frequently seek credit from international lenders. In addition, international lenders often lend to non-Canadian companies with Canadian affiliates that may be borrowers or guarantors under the debtors' credit facilities. This paper discusses Canadian legal issues that international lenders might encounter when dealing with Canadian credit parties. It provides a brief overview of the legislative and regulatory framework applicable to financings involving Canadian loan parties, including the taking of security interests over personal property. The major differences between the Canadian framework and the frameworks in the US and UK (specifically England and Wales)[1] are discussed as they arise. The impact on financings of financial assistance rules, restrictions on corporate benefit and loans to directors, laws against usury, environmental legislation, restrictions on the practices of foreign banks in Canada, the International Financial Reporting Standards ("IFRS"), Basel III, and certain other recent developments are also addressed.

I. Overview of the Legislative Framework

Secured transactions in Canada (with the exception of the province of Québec) are governed by provincial personal property security legislation (the "PPSA"). Reference is made to specific provisions in the Ontario PPSA,[2] which is paradigmatic of similar provisions in each of the other provinces, unless otherwise specified. Personal property includes chattel paper, documents of title, goods, instruments, intangibles, money and investment property, including fixtures, but excluding building materials that have been affixed to real property.[3] The PPSA applies to every transaction that creates a security interest, without regard to form.[4]

In each of the provinces and territories, except Prince Edward Island, in addition to certain specifications under the PPSA, security interests in investment property are governed by a *Securities Transfer Act*[5] or similar legislation (the "STA"). The STA is largely based on Article 8 of the United States *Uniform Commercial Code* ("UCC").[6] Taken together, the PPSA and STA deal with the conflict of laws rules,[7] the rights of secured parties with control of investment property as collateral,[8] the priority rules[9] for investment property and the rights and obligations of securities issuers, intermediaries, secured parties and investors.

The province of Québec is a civil law jurisdiction that is governed by the *Civil Code of Québec* (the "Civil Code").[10] The Civil Code establishes a distinct set of rules that governs secured transactions in that jurisdiction. Any relevant differences among the provinces are identified as they arise below.

The *Bank Act* (Canada)[11] ("Bank Act") is another relevant statutory regime in Canadian financing transactions. The Bank Act regulates all banking activity in Canada, including the activities of foreign banks therein. Section 427 of the Bank Act enables chartered banks operating in Canada to acquire

Questions relatives au financement transfrontalier au Canada

David Nadler et Lisa Mantello

Dans un marché financier de plus en plus mondialisé, les entités canadiennes souscrivent souvent des prêts de prêteurs internationaux. L'article qui suit entend discuter des questions juridiques canadiennes que peuvent rencontrer les prêteurs internationaux lorsqu'ils traitent avec des parties canadiennes. L'article donne une vue d'ensemble du cadre législatif et réglementaire applicable aux opérations de prêt impliquant des parties canadiennes, et examine certaines différences entre le Canada, les États-Unis et le Royaume-Uni (plus précisément : l'Angleterre et le pays de Galles).

Cette vue d'ensemble du cadre législatif canadien décrit les méthodes de création des sûretés sur différents types de biens personnels au Canada. Les types de biens couverts comprennent les biens matériels, les biens immatériels, les biens de placement, la propriété intellectuelle, les comptes de dépôt, la participation dans une société de personnes et les créances d'assurance. L'article couvre également la diligence raisonnable dont les prêteurs font habituellement preuve avant de faire un prêt à une partie canadienne, notamment les types d'enquête qu'ils effectuent en général. Enfin, l'article discute du principe général régissant la priorité de rang des sûretés concurrentes, de la règle de l'antériorité (*"first in time" principle*) et de ses exceptions, notamment concernant les sûretés en garantie du prix d'acquisition, l'exception de trente jours prévue

aux lois canadiennes sur la faillite, et les fiducies implicites.

Outre le cadre législatif et réglementaire applicable aux opérations de financement impliquant des parties canadiennes, l'article aborde d'autres questions qu'un prêteur pourrait vouloir examiner concernant les opérations de financement au Canada. Cela comprend les conversions entre les contrats de sûreté générale canadiens et américains, le regroupement des patrimoines, les règles de l'aide financière, les restrictions touchant les avantages sociaux et les prêts aux administrateurs, les lois contre l'usure, les lois sur l'environnement, les restrictions touchant les activités des banques étrangères au Canada, les exigences en matière de comptabilité, la mise en œuvre des accords de Bâle III, et d'autres développements récents.

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security over the personal property of a borrower.[12] Priority disputes may arise where there are competing interests under the Bank Act and a provincial PPSA. Recent amendments to the Bank Act, discussed in Section IV(B)(iv) below, aim to clarify the priority positions as between these types of interests.

In the US, secured transactions are governed primarily by Articles 8 and 9 of the UCC, as enacted in every state. In the UK, security interests created by companies are governed primarily by the *Companies Act 2006* ("Companies Act").[13]

II. Taking Security in Personal Property

A. Introduction to Attachment and Perfection

To obtain a security interest that is enforceable against third parties, attachment and perfection of the security interest are required.

Attachment occurs when the following requirements for creation of a security interest are satisfied: (i) value is given, (ii) the debtor has rights in the collateral or has the power to transfer rights in the collateral to a secured party, and (iii) the debtor has signed a security agreement that contains a description of the collateral sufficient to enable it to be identified.[14]

Upon attachment, the debtor's rights in the collateral are restricted by the secured party's rights therein.[15] However, the secured party cannot enforce its security interest against third parties until it has perfected the security interest, or 'published' it in Quebec. A PPSA security interest must have attached before it can be perfected.

A secured party has "perfected" its security interest when it has obtained the greatest bundle of rights under the PPSA or STA, as applicable, with respect to the secured collateral. Perfection occurs when a security interest has attached and all steps required for perfection have been taken.[16] The method through which a security interest is perfected depends on the collateral. There are three possible methods: registration, possession, and control. A security interest in any type of collateral may be perfected by registration.[17] Only a security interest in chattel paper, goods, instruments, negotiable documents of title, and money may be perfected by possession.[18] A security interest in investment property is generally perfected by control. Greater detail on the process through which security in each type of collateral is perfected is provided below.

A similar framework of attachment and perfection exists in the US and UK. In both jurisdictions, a security interest must attach to be enforceable against the debtor and be perfected to be enforceable against third parties.[19]

A security interest may also be acquired over future assets. In Canada, these are commonly referred to as "after-acquired property." In Canada, as well as in the US and

UK, a security interest attaches to after-acquired property when the debtor acquires rights in that property. Unlike in Canada, additional steps are required in the US for certain after-acquired property, such as intellectual property.[20] In the UK, security may be obtained over future assets through a floating charge, which is a charge over a shifting pool of assets. A security document that creates a floating charge generally provides that if certain events occur, such as a default by the borrower, the charge crystallizes (effectively becomes fixed) and the borrower loses its right to deal with the relevant assets.[21] While this was previously the case in Canada, such a distinction between fixed and floating charges no longer exists in the common law provinces with respect to a security interest in personal property.

B. Creation and Perfection Requirements by Type of Collateral

As mentioned above, once a security interest has attached it can be perfected by registering a financing statement. Financing statements are forms of notice registered in a computerized provincial or territorial database that can be searched by the general public, including potential lenders and asset purchasers. Requirements for the registration of financing statements vary depending on the type of property at issue.

i. Tangible Personal Property

Secured creditors are often granted a general security interest covering all of the debtor's present and after-acquired personal property, both tangible and intangible. Security over tangible personal property, which primarily includes goods that are inventory or equipment, is created when a debtor grants a security interest in such property to a creditor pursuant to a security agreement. A security interest in tangible personal property must be registered in the jurisdiction in which the collateral is located at the time of attachment of the security interest.

In the US, a security interest in personal property must be registered in the jurisdiction in which the debtor is located at the time of attachment of the security interest, rather than the jurisdiction in which the collateral is located.[22] A debtor is located at its place of business, or if it has more than one place of business, its chief executive office.[23] The issue of jurisdiction of registration of a security interest does not arise in the UK, as it has a central register rather than a number of regional registers.

In the UK, certain charges created by companies must be registered at the Company Charges Register within 21 days of creation.[24] These include non-possessory charges over goods.[25] If the charge is not registered within 21 days, it will be ineffective against other secured creditors and in the event of the debtor's insolvency.[26]

In Québec, security in tangible property is granted by publication of a hypothec (similar to perfection in the common law provinces). The process through which publication is achieved depends on whether the property is moveable or immoveable. Publication of security in moveable property in Quebec is governed by the law of the jurisdiction where the property is situated. The requirements for publication of a hypothec depend on whether it is with or without delivery of the secured property. Where the hypothec is without delivery, it is created by deed. It is not necessary to execute the deed before a Québec notary, unless the hypothec secures the payment of bonds or other titles of indebtedness. In this case, the hypothec can be published by computerized registration at the Register of Personal and Movable Real Rights. Where the hypothec is with delivery of the secured property, it is created by pledge, and there is no written agreement required. In this circumstance, physical delivery of the collateral to the pledgee or a custodian who is mutually agreed upon by the parties is sufficient for enforceability.

Security over immovable property in Québec is also granted by registration of a hypothec. The security is created under a deed, which is executed by the grantor and the secured party before a Québec notary. To be published, the security must be registered against title to the property in the division where the property is situated. As is the practice in the common law provinces, the hypothec is typically registered by the lender. Depending on the category of immovable, the hypothec may require immatriculation; that is, the creation of a specific land file or registration in a particular register. The categories that attract that requirement include forest management (timber) rights, mining rights and claims, networks relating to railway, cable communications, water or gas distribution, power lines, oil or gas pipelines, and sewage conduits.[27]

There are certain types of tangible personal property that fall under federal jurisdiction, such as ships, aircraft, and rolling stock. Security interests in such property can be granted under the PPSA or the Civil Code. However, secured parties must take any additional steps required under the applicable federal legislation to establish a first-ranking lien in such property.

Fungible assets as a class are allowed to be reliably secured under the PPSA if they are personal property. If goods are transformed through manufacturing and are no longer identifiable, any previously perfected security interest in those goods continues in the

transformed end-product. In Québec, a hypothec can charge future or fungible assets. The security interest continues to subsist in any new movable property resulting from a transformation of the collateral.[28] This rule extends to property resulting from the combination of several movables, only some of which are charged.

ii. Intangible Personal Property

Section 7(1) of the PPSA addresses security interests in intangibles, equipment and inventory goods that are normally used in more than one jurisdiction, leased inventory and non-possessory security interests in instruments, negotiable documents of title, or chattel papers. This list captures claims and receivables such as debts or rights under contracts. Security over intangible personal property is created when a debtor grants a security interest in such property to a creditor pursuant to a security agreement.

Intangible property is governed by the laws of the jurisdiction where the debtor is located at the time the security interest attaches. Thus, a security interest in intangible property is perfected by registering a financing statement in that jurisdiction. There are a number of mechanisms by which the debtor's location is determined. The debtor is deemed to be located at its place of business if there is one, at the debtor's chief executive office if there is more than one place of business, or otherwise at the debtor's principal place of residence.[29] Proposed amendments to the Ontario, British Columbia and Saskatchewan PPSAs would alter the way in which the debtor's location is determined.[30] As of the date of writing, these amendments are not in force. In Québec, debtor location is the debtor's domicile or registered office.[31]

In the US, security over intangible assets is acquired in a similar manner. In the UK, charges created by companies over many intangible assets must be registered in the Company Charges Register within 21 days of creation, as is required for charges over tangible assets.[32] These include charges over uncalled share capital of a company, accounts receivable, goodwill and intellectual property.[33] A floating charge over a company's property, including any intangible assets, must also be registered.[34]

iii. Investment Property

The PPSA and STA define investment property as including securities, security entitlements, securities accounts, futures contracts and futures accounts.[35] In most provinces, security over investment property is taken under a securities pledge agreement and/or a control agreement. In Québec, security over investment property is taken under a hypothec. Through these agreements, a debtor must grant a security interest to a creditor in investment property and that interest must attach and then be perfected.

A similar system is in place in the US. Security over investment property may be perfected by possession (certificated securities), by control agreement with the issuer or securities intermediary, or by becoming the holder of a securities entitlement.[36] In the UK, charges over investment property, such as shares and debts other than book debts of a company, cannot be perfected by registration.[37] Where a charge is not registrable, a chargee may choose to take possession or control of the collateral in order to provide public notice of the charge and prevent any other purchaser or encumbrancer from obtaining legal title.[38]

The requirements for perfection of a security interest in investment property in Canada differ depending on whether the securities are certificated or uncertificated. To perfect a security interest in certificated securities, a PPSA financing statement (similar to Form 1 under the UCC) must be registered in the jurisdiction in which the debtor is located and control of the pledged securities must be obtained.[39] Control is obtained through possession of the securities' certificates. Perfection by control is the preferred method because it provides the lender with a higher priority than a security interest perfected by registration alone. Lenders should also take an endorsement or have the securities registered in the lender's name.

Perfection of uncertificated securities is governed by the law of the jurisdiction of the issuer, securities intermediary or futures intermediary, as the case may be.[40] Lenders obtain control over uncertificated securities by registering the securities in the lender's name, or obtaining a control agreement from the issuer of the securities. Where the securities are held by a securities intermediary, the lender would obtain control of such collateral by either arranging for the intermediary to record the lender as the entitlement holder, or by obtaining a control agreement from the securities intermediary or a third party having control for the benefit of the lender.

iv. Other Intangible Property

Under the PPSA, lenders can also take security over deposit accounts, which are treated as receivables owed by the lender to the borrower. Security over deposit accounts is perfected by registration of a PPSA financing statement.[41] Proposed amendments to the PPSA would allow perfection of such security by taking control over the deposit account, as is the case in the US.[42]

In the US, security over deposit accounts is perfected by control. If the secured party is the financial institution obligated to pay the account, perfection of the security is automatic. Otherwise, control may be achieved by a control agreement among the borrower, the secured party and the financial institution regarding the account or by transfer of the account into the name of the secured party.[43] In the UK, charges over bank accounts may be registered under the Companies Act to achieve validity against creditors. [44] Control is necessary to obtain a fixed charge over the accounts, although not to obtain a floating charge.

It should be noted that under Section 12(1) of the STA, an interest in a partnership or limited liability company is not a security except: (i) where the interest is dealt in or traded on a securities exchange or in securities markets, (ii) the terms of the interest expressly provide that the interest is a security for the purposes of the STA, or (iii) where the interest is a mutual fund security within the meaning of Section 11 of the STA.[45]

Although intellectual property rights are regulated by federal legislation, they also constitute personal property under the PPSA. They are classified as intangibles and therefore, the perfection requirements are as stipulated for intangibles above. In addition, it is customary to register security agreements regarding intellectual property with the Canadian Intellectual Property Office. This registration does not perfect the security interest (that is achieved by registering a financing statement under the PPSA) but it does provide notice of the security interest in the intellectual property collateral. In the US, security over certain intellectual property must be registered at the state level, while security over other intellectual property must be registered at a specialized federal register.[46] In the UK, security over certain intellectual property rights must be registered at the Company Charges Register and may also be registered at the UK Patent Office.[47]

The PPSA expressly excludes an interest in or claim under any insurance policy or annuity contract from its scope. As a result, lenders must take additional steps with the insurer to secure any such interest. However, the PPSA provides that a security interest extends to any proceeds received as compensation for the loss or destruction of assets that are secured.[48] Where a debtor has insurance on other secured personal property assets, this concept may remedy the insurance exclusion. This issue does not arise in Québec where insurance policies themselves can be charged under a hypothec.[49]

C. Due Diligence: Conducting Appropriate Searches

Although perfection means that the secured party has achieved the greatest possible bundle of rights under the PPSA with respect to the collateral, this does not mean that the party has priority ahead of all other claims against the collateral. Thus, it is advisable for counsel to the lender in a financing transaction to conduct PPSA searches against the borrower and any guarantors to identify any competing registrations. These searches must be conducted where the borrowers or guarantors are located, organized, carry on business, and lease or own property. The location in which PPSA searches must be conducted varies depending on whether the property is tangible or intangible. Tangible personal property is governed by the law of the jurisdiction where the property is situated at the time of the attachment of a security interest. Intangible personal property and goods that are used in more than one jurisdiction are governed by the laws of the jurisdiction where the debtor is located at the time of the attachment of a security interest.[50] In the US, tangible and intangible property is governed by the jurisdiction where the debtor is located.

In addition to PPSA searches, a number of searches are generally conducted against each borrower and guarantor as a matter of practice in Canada. These include general corporate searches, bankruptcy searches, searches under Section 427 of the Bank Act, litigation searches and other federal searches depending on the nature of the collateral.

Where a lender is seeking security over real estate, land registry office searches are also customary. Security over real property is perfected by the registration of a mortgage, debenture or trust deed against title to the land and, typically, that registration is made by the lender. It is also notable that certain types of real property are subject to particular legislation. For example, federal statutes govern federally regulated facilities like major shipping ports, prisons, and airports. These particularities should be considered by counsel.

III. Priority Considerations

A. The General PPSA Rule

The PPSA has numerous specific priority rules. If none of these apply, in the event of a contest between two or more security interests in the same property, the PPSA establishes that priority is determined by the "first in time" principle. This means that a security interest that has attached and been perfected will enjoy priority over any subsequent claims.

Where there is a contest between a perfected security interest and an unperfected security interest, the perfected security interest will take priority.[51] Where there is a contest between two perfected security interests, priority is determined on the basis of the default rules set out in Section 30 of the PPSA, which codifies the "first in time" principle. The "first in time" principle refers primarily to registration; that is, if the contest is between two or more security interests perfected by registration, priority is given to the first to register, regardless of whether that party was the first to perfect. The "first in time" principle is also applicable in Quebec, with certain exceptions.[52]

In the common law provinces, it is customary for the secured party to register a security interest from a business debtor prior to execution of the security agreement or attachment of the security interest (typically referred to as pre-registering). In Quebec, security may not be registered prior to execution of the security agreement. In the US, a secured party will not often pre-register a security interest, as it must have a written and signed authorization from the debtor to do so.

Priority rules in the US are generally similar to the Canadian rules.[53] However, the priorities in the UK are significantly more complicated. The Companies Act does not address priorities. The primary common law rule is that priority of competing charges is determined by the order of their creation (such as through the execution of a security agreement).[54] This focus on creation differs from the Canadian and American systems, which refer to registration. Registration, however, is relevant in the UK in that an unregistered charge will be subordinate to a charge taken after the 21 day window for registration of the first charge.[55] There are many and extensive exceptions to the first-in-time principle under the UK common law, such as floating charges, assets other than those included as registrable charges under Section 860 of the Companies Act,[56] or assets that can be registered in specialized registers, which often have their own rules regarding priority.[57]

B. Exceptions to the General Rule: When First in Time is not Necessarily First in Line

The "first in time" principle does not necessarily apply to: (i) purchase-money security interests ("PMSIs"), (ii) property that falls under the "thirty day goods exception" in the *Bankruptcy and Insolvency Act*,[58] (iii) certain implied pensions and trusts, and (iv) other particular statutory claims.

i. PMSIs

It is advisable for counsel to the lender to review PPSA search results conducted against the borrower to

identify any competing registrations. In most secured senior debt financings in Ontario, the lender is granted a first ranking lien, subject only to "Permitted Liens". These are generally defined to include liens that are an exception to the "first in time" rule. The super-priority statutorily granted to PMSIs is one such example.

A similar priority is available to a PMSI in the US and UK, provided that certain conditions are met.[59]

In order to qualify as a PMSI in Canada, the security interest must be: (a) a security interest taken or reserved in collateral, other than investment property, to secure payment of all or part of its price, (typically referred to as an unpaid vendor's claim); (b) a security interest taken in collateral, other than investment property, by a person who gives value for the purpose of enabling the debtor to acquire rights in or to the collateral, to the extent that the value is applied to acquire the rights (typically referred to as a financer's claim); or (c) the interest of a lessor of goods under a lease for a term of more than one year (typically referred to as a lessor's claim).[60]

Secondly, the secured party must comply with the requirements set out in Section 33 of the PPSA. These requirements differ depending on whether the collateral to be secured is inventory or non-inventory. Super-priority for a PMSI in inventory and its proceeds will apply if the following conditions are met:

i. The PMSI was perfected at the time the debtor or third party, at the request of the debtor (such as a transport company hired by the debtor), takes possession of the collateral; and

ii. Before the debtor receives possession of the inventory, the third party with an interest in the inventory or accounts of the debtor has received a notice in writing from the secured party that the secured party has, or is expected to take, a PMSI in such inventory or accounts.[61]

If these requirements are met, super-priority will also extend to the proceeds of the inventory.[62]

Super-priority for a PMSI in non-inventory will apply:

i. Where the collateral is tangible, if the PMSI was perfected before or within fifteen days after the debtor, or the third party at the request of the debtor, obtained possession of the collateral; or

ii. Where the collateral is intangible, if the PMSI was perfected before or within fifteen days after attachment.[63]

There is no need to give notice to other creditors for the PMSI priority to take effect.

ii. The "Thirty Day Goods Exception"

The BIA contains what is known as the "thirty day goods exception," which displaces the default priority rules in Section 30 of the PPSA.[64] Under this exception, if goods have been supplied to the debtor, the unsecured supplier may repossess the goods in certain circumstances. The first circumstance is if, within thirty days of delivery, the supplier presents a written demand for repossession to the debtor. The second is if the debtor is either bankrupt or a receiver has been appointed in relation to the debtor. If the thirty day goods exception applies, the unsecured supplier has priority over a prior general security interest in the same goods, even if the supplier has not met the requirements for a PMSI or does not have a perfected security interest. A similar exception exists under the Civil Code in Quebec.[65]

iii. Implied Trusts/Pensions

Another exception to the "first in time" principle arises where the debtor's accounts or inventory and its proceeds are impressed with a statutory deemed trust, such as a trust granted under the Ontario *Employment Standards Act 2000*[66] or Ontario *Pension Benefits Act* [67] ("PBA"). A secured party's PPSA interest in these circumstances will be subordinated to the interests of beneficiaries of the deemed trust, regardless of whether the security interest has been perfected. However, the statutory deemed trust does not take priority over interests in other types of collateral, nor does it take priority over a PMSI in inventory and its proceeds.

In *Indalex Limited (Re)*[68] ("Indalex"), the Ontario Court of Appeal held that a statutory deemed trust created under the PBA in the context of a restructuring proceeding under the *Companies' Creditors Arrangement Act*[69] ("CCAA") may have priority over claims secured by a court-ordered super-priority charge. The Court also held that the deemed trust may apply to the entire wind-up deficiency of a defined benefit pension plan, rather than only to the contributions outstanding at the date of the wind up.[70] The Supreme Court of Canada heard an appeal of Indalex on June 5, 2012.[71] As of the date of writing, judgment has not been rendered.

Recent cases have limited the scope of the decision in Indalex. The decision in *Re Timminco Ltd.*[72] suggests that a claim secured by a court-ordered super-priority charge in CCAA proceedings may have priority over a deemed trust under provincial legislation where the court order addresses the issue of paramountcy of the federal CCAA over the provincial

legislation.[73] In *White Birch Paper Holding Company (Arrangement relative à)*,[74] the Quebec Superior Court held that the decision in Indalex does not apply in Quebec.

In the US, a lien under the *Employee Retirement Income Security Act of 1974*[75] ("ERISA") for an employer's failure to pay pension contributions generally has priority over a previously perfected security interest with respect to assets acquired by the debtor after the filing of the notice of lien.[76] Missed contributions can also lead to excise taxes of up to 100% of the contribution, which can result in a federal tax lien. Federal tax liens have the same priority as liens under ERISA. The priority of state tax liens varies by state.[77]

iv. Other Claims

Rules similar to those relating to statutory deemed trusts under employment and pension legislation apply to deemed trusts in favour of the Crown for unremitted source deductions under the federal *Income Tax Act*,[78] *Excise Tax Act*,[79] *Canada Pension Plan*,[80] and *Employment Insurance Act*.[81] In these circumstances, a secured party's PPSA interest will be subordinated to the interests of beneficiaries of the deemed trust, regardless of whether the latter's security interest has been perfected. Goods on lease or conditional sale, not owned by the tax debtor, are exempted by case law from these Crown rights.

Certain additional statutory claims may affect priority where a borrower or guarantor has declared bankruptcy. For example, the Canadian federal government could have a super-priority claim and charge against the debtor's current assets under the *Wage Earner Protection Program Act*.[82] The claim can be up to a maximum of $2,000 (CDN) per employee for any unpaid wages (including vacation pay) earned up to six months before the date of bankruptcy.[83] Other examples include compensation due to the Crown for the costs of environmental damage, and the expenses of the bankruptcy trustee and any other court-ordered charges that may be granted over the debtor's property. Further, a lien provided by statute or a rule of law may have priority over the interest of a secured party.[84] For example, a lien arising from the provision of materials or services with respect to goods has priority over a perfected security interest in those goods, unless the statute that created the lien provides otherwise.[85]

As mentioned in Section II, amendments to the Bank Act have clarified the order of priority where multiple secured parties have a security interest in the same collateral. The amendments provide that a security interest under the Bank Act has priority over a security interest that was unperfected at the time the bank acquired its security.[86] A general definition of "unperfected" was added to the Bank Act, which refers broadly to the law under which a security interest is created.[87] However, a prior unperfected security interest would still take priority where the bank has "knowledge" of such unperfected security interest.[88]

In the US, the claim of a statutory or common law lien holder in possession of the collateral after completing work on it generally has priority over the claim of a secured creditor.[89] The same may be true of a warehouseman's lien, although this is less clear.[90] A secured party may be able to protect against such a claim through a waiver agreement in which the warehouseman waives all liens.

IV. A Note on Guarantees and Negative Pledges

Guarantees are commonly used in commercial lending in Canada. Usually, a guarantor provides a standalone guarantee in favour of a secured creditor, supporting obligations that the borrower owes to the creditor. In Québec, suretyships are used in commercial lending. These are typically in writing, but are not subject to formalities.

In the US, an upstream or cross stream guaranty may be considered a fraudulent conveyance under federal bankruptcy law or similar state law, and thus be void.[91] Broadly, this may occur where the guarantor was insolvent or nearing insolvency at the time of the guarantee and received less than a reasonably equivalent value for providing the guarantee.[92]

Lenders providing financing to a US borrower may seek to obtain a guarantee from any subsidiaries or affiliates the borrower has in Canada. However, such a guaranty may trigger a taxable deemed dividend to the US borrower of the value of the benefit associated with the guarantee.[93] As a result, these guarantees are not often obtained.

Negative pledges are also frequently used in the Canadian commercial lending market. They do not create a security interest, but negative pledges can be important where the debt is unsecured. For example, a negative pledge may prohibit a borrower from granting a security interest in its assets to another lender.

V. Risk Areas for Lenders

The following describes a number of potential risks in connection with Canadian financing transactions. For the most part, these risks are minimal. For example, the financial assistance rules described below have almost entirely been eliminated from federal and provincial legislation. However, in select circumstances, they may pose issues for the unwary.

A. Conversions Between Canadian and US Security Agreements

An international lender may require that each US affiliate of a Canadian borrower grant a security interest in its assets. To maintain contractual uniformity among cross-border obligors, the Canadian General Security Agreement used for the borrower may be converted into a US security agreement. Although these two agreements are generally similar, particular granting language must be used in the US security agreement to achieve the intended security. The PPSA and Article 9 of the UCC both provide that a security interest will not attach unless the relevant security agreement includes a description of the collateral sufficient to identify it. Article 9 of the UCC also provides that generic collateral descriptions such as "all the debtor's property" do not meet the identification requirement for the purposes of a security agreement. The PPSA does not include this requirement. As a result, this generic granting language is often used in Canadian security agreements, followed by a list of specific categories of collateral to be secured. Given this difference in legislation, better practice in a US security agreement would be to reverse the order of the granting language by including such a list first and a catch-all phrase, such as "any other of the debtor's property," after the list.[94]

B. Substantive Consolidation

Special purpose vehicles ("SPVs") are a common mechanism used by lenders to protect against the risk of substantive consolidation in bankruptcy; that is, where a bankruptcy court treats a group of affiliated companies as one, merging their assets and liabilities for the purposes of the bankruptcy proceeding. SPVs are also used by borrowers in order to limit recourse. Lenders will typically take security in both the SPV's assets and ownership interests. This facilitates realizing on the security, limits claims against the SPV and, as intended, protects from the risk of substantive consolidation.

C. Financial Assistance Rules

Financial assistance refers to the provision by a corporation of loans, guarantees, or similar assistance to its directors, officers, employees and shareholders. Corporate legislation historically has restricted financial assistance where there were reasonable grounds to believe that the corporation was or may become insolvent. These restrictions have been eliminated from federal and most provincial corporate statutes, except in New Brunswick, Prince Edward Island, Newfoundland, Northwest Territories, Yukon and Nunavut.[95] These jurisdictions excepted, Canadian companies can provide financial assistance to affiliated entities or third parties, subject to disclosure obligations. It should be noted that several provincial corporate statutes prohibit a company from providing financial assistance for the acquisition of its own shares.

As in Canada, financial assistance is not restricted by any specific rules in the US.[96] In the UK, financial assistance by a public company for the acquisition of its own shares or those of its holding company is prohibited.[97] However, it is permitted for a private holding company.[98]

D. Corporate Benefit

While there is no corporate benefit requirement in Canadian corporate statutes, transactions with no benefit to a Canadian corporation may breach directors' fiduciary duties[99] or attract the oppression remedy which may be sought by minority shareholders or creditors.[100] Similar rules exist in the US and UK. In general, though, guarantees supporting the debt of related companies are enforceable, provided that the financing is beneficial to the corporate group as a whole.

E. Loans to Directors

Loans by companies to their own directors are not specifically restricted. However, directors owe a fiduciary duty to the corporation and thus cannot profit from material agreements with the corporation unless certain requirements are met. The director must declare his or her interest in the transaction to the corporation and the corporation must consent.[101] Further, the director cannot attend any meeting at which the agreement is discussed and must abstain from voting regarding the agreement.[102] Where the director fulfills these requirements, he may proceed with the agreement and need not account to the corporation for any benefit derived from it. A loan provided by the corporation to a director on terms that would not be available to that director in the market (for example, below-market interest rates) may trigger these requirements.

F. Usury

It is a crime to either enter into an agreement or an arrangement to receive interest at a criminal rate, or to receive payment or partial payment of interest at a criminal rate.[103] For the purposes of that offence, the current criminal rate is greater than sixty percent per annum, calculated over the period during which the loan is outstanding, regardless of the stated term of the loan. Interest includes charges of any kind and in any form that are paid or payable in connection with the advance of credit, calculated on an actuarial method. For example, interest includes facility fees, structuring fees, work fees, commitment fees, bonuses and other, miscellaneous charges that must be paid to obtain the credit.

Lenders typically insert provisions

into loan agreements that invalidate any interest in excess of the criminal rate along with a mechanism designed to convert any excess into repayments of principal. However, lenders must be wary to avoid a situation in which the term of the loan is shortened and the actual rate is inadvertently pushed above the sixty percent per annum ceiling. If a court finds that a lender has charged a usurious interest rate, the court may read down the interest rate provisions in the loan agreement or void the agreement entirely.

G. Environmental Laws

Generally, there is no liability for lenders under Canadian environmental laws for making a loan or holding or enforcing security or a guarantee. However, liability can arise if the enforcement of the loan requires or permits the lender to take possession or control. In that scenario, the question becomes whether the lender has the ability to appoint directors and approve environmental programs or policy. Lenders' counsel should keep in mind that even if the lender is not in actual possession, and did not participate in any activity polluting the land, the risk of liability may exist. Each situation must be evaluated on the circumstances. Nevertheless, lenders tend to be more concerned with the impact environmental issues have on a borrower's ability to service the loan rather than their own potential liability for environmental violations.

H. International Lenders

There are no general restrictions on the making of loans by international lenders, or the granting of security or guarantees in favour of international lenders. The same is true in the US and UK. However, the Bank Act prohibits foreign banks from engaging in or carrying on "any business that a bank is permitted to engage in or carry on under the Bank Act, or any other business in Canada."[104] This includes the provision of "any financial service."[105] "Foreign banks" include, among others, entities that are incorporated or formed by or under the laws of a country other than Canada that engage in the business of lending money and accepting deposit liabilities transferable by cheque or other instrument.[106] To clarify, these restrictions only apply where the foreign bank engages in such activities within Canada. In general, foreign entities are free to lend to Canadian entities. In addition, the realisation on collateral by a foreign lender may trigger foreign ownership and other restrictions.

Where there is a foreign choice of law clause in a loan agreement, Canadian courts will generally recognize such a clause as the parties' intention, provided that a number of conditions are met. Firstly, the application of the law must not be contrary to public policy. Secondly, Canadian procedural law and certain overriding provincial and federal laws will be applied regardless of the choice of law clause, including bankruptcy and insolvency statutes, federal criminal legislation, employment legislation, and consumer protection legislation. In addition, local law will generally apply to collateral-related matters.

VI. Other Considerations in a Canadian Financing

In addition to being acquainted with the general rules and procedures of cross-border financing in Canada, there are additional systemic considerations of which lenders should be aware. The potential impact of some recent systemic changes, such as the transition from using Generally Accepted Accounting Principles ("GAAP") to using IFRS and the Canadian implementation of Basel III in the transactional process, are discussed below.

A. Accounting for the Transition to IFRS

Effective 2011, Canada has switched from using Canadian GAAP to IFRS for financial institutions and public companies. Counsel should be aware of the need to carefully consider the impact of legacy deals on Canadian transactions, and ensure that financial covenants and definitions are revised to appropriately reflect the business requirements of the participants. Note, in particular, that there is a fairly significant difference between the continued US GAAP presentation and IFRS presentation.

B. Basel III

Basel III is a global regulatory standard that imposes more stringent requirements on banks with regard to capital, risk coverage, leverage ratios, risk management and supervision, disclosure, and liquidity. When Basel III becomes effective in Canada, the capital cost to a bank of acquiring and holding, and arranging and syndicating loans to corporate borrowers will increase. Canada plans to implement Basel III gradually and incrementally, beginning in January 2013. As a result, the effect on deposit-taking institutions' margins of profit on credit agreements will not be fully known until the regulations are fully implemented, or at least until final quantitative ratios are determined.

VII. Conclusion

Lenders providing financing in Canada have a number of issues to consider before executing these transactions. In addition to understanding the legal framework applicable to a Canadian financing, it is prudent to be aware of additional issues that a lender may encounter, such as financial assistance rules, corporate benefit concerns, restrictions on corporate loans to directors, usury issues,

environmental legislation, restrictions on foreign banks, IFRS, and Basel III implications.

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The authors gratefully acknowledge the research assistance of Heather Gallagher, Student-at-Law, Goodmans LLP.

ENDNOTES

[1] All references to the UK are specific to England and Wales. Scotland and Ireland each have distinct legal systems, which are beyond the scope of this paper.

[2] *Personal Property Security Act*, RSO 1990, c P. 10 [*PPSA*].

[3] *Ibid*, s 1(1) ("personal property").

[4] *Ibid*, s 2(a).

[5] See e.g. *Securities Transfer Act 2006*, SO 2006, c 8 [*STA*].

[6] *Uniform Commercial Code* § 8 (2011) [*UCC*].

[7] *PPSA*, *supra* note 2, s 7.1.

[8] *Ibid*, s 17.1.

[9] *Ibid*, s 30.1.

[10] *CCQ*.

[11] SC 1991, c 46.

[12] *Ibid*, s 427.

[13] (UK), c 46. A security interest created by a person who is not a company is governed by the *Bills of Sale Act* (UK), c 35.

[14] *PPSA*, *supra* note 2, s 11(2).

[15] Richard H McLaren, *Secured Transactions in Personal Property in Canada*, loose-leaf, vol 1A, 3d ed, (Toronto: Carswell, 2012).

[16] *PPSA*, *supra* note 2, s 19.

[17] *Ibid*, s 23.

[18] *Ibid*, s 22(1).

[19] See generally Royston M Goode, *Goode on Legal Problems of Credit and Security*, 4th ed (London, UK: Sweet and Maxwell, 2007); Barkley Clark & Barbara Clark, *The Law of Secured Transactions Under the Uniform Commercial Code*, vol 1, 3d ed (New York: A.S. Pratt, 2012).

[20] Practical Law Company, *Cross-Border Finance: Secured Lending Handbook 2007-8* (London, UK: Practical Law Company Ltd., 2007) at 224.

[21] *Ibid* at 208.

[22] UCC § 9-301(1).

[23] UCC § 9-307.

[24] *Companies Act*, *supra* note 13, ss 860, 870; Practical Law Company, *supra* note 20 at 209 (The charges listed in s 860 of the *Companies Act* must be registered to achieve validity against creditors. These include a charge on land or any interest in land (other than a charge for any rent or other periodical sum issuing out of land); a charge created or evidenced by an instrument which, if executed by an individual, would require registration as a bill of sale; a charge for the purposes of securing any issue of debentures; a charge on uncalled share capital of the company; a charge on calls made but not paid; a charge on book debts of the company; a floating charge on the company's property or undertaking; a charge on a ship or aircraft; or any share in a ship; a charge on goodwill or on any intellectual property; and others).

[25] Philip R Wood, *Comparative Law of Security Interests and Title Finance*, 2d ed (London, UK: Sweet and Maxwell, 2007) at 153.

[26] *Companies Act*, *supra* note 13, s 874; Goode, *supra* note 19 at 78.

[27] CCQ, art 3031.

[28] *Ibid*, art 2673.

[29] *PPSA*, *supra* note 2, s 7(3).

[30] *Ministry of Government Services Consumer Protection and Service Modernization Act, 2006*, c 34, Sched E, s 3(2); *Finance Statutes Amendment Act, 2010*, SBC 2012, c 4, s 43; *The Personal Property Security Amendment Act, 2012*, SS 2010, c 26, s 5 (Under these amendments, where the debtor is a partnership (other than a limited partnership), then consideration must be given to the partnership agreement. If the agreement stipulates the law that is to govern the agreement, then the debtor is said to be located in that jurisdiction. Where the debtor is a limited liability partnership, registration requirements must be met prior to carrying on business in a province other than the province in which the limited liability partnership is initially formed. Where the debtor is a corporation, a limited partnership, or an organization and is incorporated, continued, or amalgamated in a Canadian province or territory that requires disclosure through a public record, then the location of the debtor is said to be the jurisdiction where this occurred. Lastly, for federally incorporated debtors, the applicable jurisdiction is the location of the head office as set out in the constating documents of the corporation. For this category, the *Canada Business Corporations Act*, RSC 1985, c C-44, s 19 [*CBCA*] requires corporations to at all times maintain a registered office in the province specified in its articles).

[31] CCQ, art 3083.

[32] *Companies Act*, *supra* note 13, ss 860, 870; Practical Law Company, *supra* note 20 at 209.

[33] *Companies Act*, *ibid*, s 860.

[34] *Ibid*.

[35] *PPSA*, *supra* note 2, s 1(1).

[36] Clark & Clark, *supra* note 19 at 1.02[5][q].

[37] *Companies Act*, *supra* note 15, s 860; Goode, *supra* note 21 at 82-83, 109 (A book debt is a debt arising in the course of a company's business that would ordinarily be entered into the company's books,

whether it is actually entered or not); *Financial Collateral Arrangements (No. 2) Regulations 2003*, SI 2003/3226, Reg 3 [*Collateral Arrangement Regulations*].

[38] Goode, *ibid* at 255 (Note that a charge may not be registrable as a result of the application of the *Financial Collateral Arrangements*, *ibid*).

[39] *STA*, *supra* note 5, s 7.1(2).

[40] *Ibid*, s 7.1(2).

[41] *PPSA*, *supra* note 2, s 23.

[42] Ontario Ministry of Finance, *Stronger Action for Ontario: 2012 Ontario Budget* (Toronto: Queens Printer for Ontario, 2012), Chapter I; The Ontario Bar Association, Personal Property Security Law Subcommittee, "Perfecting Security Interests in Cash Collateral" (Ontario Bar Association, February 2012).

[43] Clark & Clark, *supra* note 19 at 1.02[5][h].

[44] Wood, *supra* note 25 at 153.

[45] *STA*, *supra* note 5 ("'mutual fund security' means a share, unit or similar equity interest issued by an open-end mutual fund, but does not include an insurance policy, endowment policy or annuity contract issued by an insurance company" at s 11).

[46] Practical Law Company, *supra* note 20 at 221.

[47] *Ibid* at 209.

[48] *PPSA*, *supra* note 2, s 1(1) ("proceeds").

[49] CCQ, arts 2687-8.

[50] *PPSA*, *supra* note 2, s 7(1).

[51] *Ibid*, s 20.

[52] CCQ, art 2945.

[53] Practical Law Company, *supra* note 20 at 222.

[54] *Registration of Security Interests: Company Charges and Property Other Than Land: A Consultation Paper* (London, UK: The Law Commission, 2002) at 33.

[55] *Ibid*.

[56] See note 24, above, for a list of charges that are registrable under s 860 of the *Companies Act*.

[57] Goode, *supra* note 19 at 174.

[58] RSC 1985, c B-3, s 81.1 [*BIA*].

[59] UCC § 9-324; Goode, *supra* note 21 at 213-214.

[60] *PPSA*, *supra* note 2, s 1(1) ("purchase-money security interest").

[61] *Ibid*, s 33(1).

[62] *Ibid*, s 33(1).

[63] *Ibid*, s 33(2).

[64] *BIA*, *supra* note 58, s 81.1.

[65] CCQ, art 1741.

[66] SO 2000, c 41.

[67] RSO 1990, c P.8 [*PBA*].

[68] 2011 ONCA 265 [*Indalex*].

[69] RSC 1985, c C-36.

[70] *Indalex*, *supra* note 68.

[71] Supreme Court of Canada, News Release, "Supreme Court of Canada – Appeal Heard" (June 5, 2012), online: <http://scc.lexum.org> (The news release indicates that the appeal will be cited as *Sun Indalex Finance, LLC et al v United Steelworkers et al* (Ont.) (Civil) (By Leave) (34308)).

[72] 2012 ONSC 948.

[73] In *Re Timminco Ltd.*, *ibid* the Ontario Superior Court of Justice (Commercial List) invoked the doctrine of paramountcy of the federal CCAA over provincial legislation to grant a super-priority charge in a CCAA proceeding. The Ontario Court of Appeal did not grant leave to appeal and affirmed that the trial court's order was the correct use of the doctrine of paramountcy. (*Timminco Limited and Becancour Silicon Inc, Re*, (20 July 2012), Ontario M41062 & M41085 (Ont CA)).

[74] 2010 QCCS 4915.

[75] 29 USCS § 1002.

[76] Clark & Clark, *supra* note 19 at 5.02.

[77] *Ibid* at 5.09.

[78] RSC 1985, c 1.

[79] RSC 1985, c E-15.

[80] RSC 1985, c C-8.

[81] SC 1996, c 23.

[82] SC 2005, c 47, s 2(1) ("eligible wages").

[83] David Nadler, David Wiseman and Brendan O'Neill, "A Q&A Guide to finance in Canada," *PLC Multi-Jurisdictional Guide to Finance* (2011), online: < http://www.practicallaw.com>.

[84] McLaren, *supra* note 15 at 7.08[2].

[85] *PPSA*, *supra* note 2, s 31; *Repair and Storage Liens Act*, RSO 1990, c R. 25.

[86] *Financial System Review Act*, SC 2012, c 5, s 38 [*FSRA*] (The amendments discussed here received Royal Assent on March 29, 2012 and were proclaimed to come into force on May 24, 2012).

[87] *Ibid*, s 36.

[88] *Ibid*, s 37 (This exception may prove to be problematic, as "knowledge" is an undefined and ambiguous term).

[89] Clark & Clark, *supra* note 19 at 3.07.

[90] UCC § 7-209.

[91] An upstream guarantee is a guarantee provided by a subsidiary for debts of its parent company. A cross stream guarantee is one provided among affiliate companies.

[92] *Internal Revenue Code*, 11 USC § 548(a)(1).

[93] Internal Revenue Service, *Internal Revenue Manual* § 4.10.7.2.1, s 956, online: < http://www.irs.gov/irm/>.

[94] Joseph McKernan & Victoria Saxon, "Convert security agreements with care", *The Lawyers Weekly* (August 17, 2012).

[95] In these jurisdictions, there are some restrictions, disclosure requirements or shareholder approval requirements in relation to financial assistance provided by corporations to affiliated or closely related entities.

[96] Practical Law Company, *supra* note 20 at 224.

[97] *Companies Act*, *supra* note 13, s 678.

[98] *Ibid*, s 679.

[99] *CBCA*, *supra* note 30, s 122(1)(a).

[100] *Ibid*, s 241.

[101] *Ibid*, s 120(1).

[102] *Ibid*, s 120(1).

[103] *Criminal Code*, RSC 1985, c C-46, s 347 (While the crime is aimed at loan sharking, it is used to defeat payments by debtors on the basis that illegal provisions are unenforceable).

[104] *Bank Act*, *supra* note 11, s 409.

[105] *Ibid*, s 409(2).

[106] *Ibid*, s 2 ("foreign bank").

CASE COMMENTARY / ANALYSE DE CAS

World Fuel Services Corporation v. The Ship "Nordems"

*Rui Fernandes**

Introduction

The intrinsic ties that bind private international law and maritime law were reaffirmed in *World Fuel Services Corporation v. The Ship "Nordems"*. This case factually spans four continents, and in February 2011 reached our Federal Court of Appeal.[1]

The case centres around the efforts of the appellant bunker supplier to recover costs for the supply of fuel to the ship Nordems from the respondent ship and ship-owners subsequent to the bankruptcy of the sub-time charterer who engaged the fuel expenditure. The ship flew the Cypriot flag and was managed out of Germany. The bankrupt charterer was, on the other hand, a South Korean corporation and the bunkers were ordered in South Africa where they were supplied by an American corporation pursuant to a contract concluded between it and the charterer. The contract was subject to American law. As the contract provided credit to the purchasing charterer, the contract was deemed to be made in the United States, and payments were due at an American bank. The Nordems did not, however, at any pertinent time sail into American waters. The ship would later sail to, and be arrested in Canadian waters pursuant to a claim by the appellant for a maritime lien over the ship for past due payments for the necessaries; that is,the fuel supplied to the ship. As one can appreciate, the context would be a meritorious factum for a complex law school conflicts problem.

Analysis of the *Nordems*

Before the Federal Court, on the successful first instance application by the ship-owner for summary dismissal of the claim, only two laws were pled. The appellant had relied on American law, claiming its application principally on the basis of the choice of law clause contained in the contract of sale of fuel to the charterer. The defendants, on the other hand, pled Canadian law. This divergence of strategies flows from what is the first key point of law addressed by the Court of Appeal. As put summarily by Nadon J.A. in his opinion, followed unanimously by the bench, there are "very important differences between Canadian maritime law and American maritime law with regard to the rights of suppliers of necessaries." [2]

American law, in two key respects, provides for significantly greater security in favour of a supplier of necessaries. First, under American law, a maritime lien is created in favour of the supplier, whereas under Canadian law, for an action *in rem* to succeed, it is necessary that a valid claim also be available against the ship-owner.[3] Second, the assertion of a personal claim against the ship-owner by a supplier of necessaries is easier under American maritime law than under Canadian maritime law. U.S. law allows the supplier of necessaries to presume that the charterer has the authority to bind the ship for the provision of necessaries, which presumption may be overcome at law only by actual knowledge of the supplier that the ship-owner withheld such authority from the charterer to subject the ship to a lien. Canadian law, on the other hand, creates a presumption that Nadon J.A. reiterates is "weaker" than its American counterpart. In order for the presumption not to be rebutted, Canadian jurisprudence has consistently required, that there be conduct on the part of the ship-owner which induces the supplier to trust that the charterer is invested with the right to bind the ship.

At the trial level, the Federal Court was required to decide the proper law governing the relationship. The defendant German owners denied there was a contractual relationship with the supplier. Both sides agreed however, to allow the Canadian court to decide the issues.

World Fuel Services Corp. c. Le navire « Nordems »

Rui Fernandes

L'affaire World Fuel Services Corp. c. Le navire « Nordems » portait sur les efforts d'un fournisseur de combustible de soute pour recouvrer les coûts liés à la fourniture de combustible au navire « Nordems ». La Cour d'appel fédérale était appelée à appliquer des principes relatifs au conflit des lois dans une affaire comportant une situation factuelle complexe dans laquelle les parties étaient domiciliées dans différents pays, et à appliquer le droit canadien et le droit américain à un navire battant pavillon chypriote saisi au Canada. La Cour devait s'attaquer aux questions juridiques relatives au lien contractuel et à la présomption de responsabilité; elle a finalement conclu que le propriétaire du navire n'était pas partie au contrat d'approvisionnement en combustible et qu'aucun privilège maritime ne grevait le navire.

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Justice Harrington made two findings that drove his analysis of the legal issues in the case. He summarized these as follows:

> Parkroad [the charterer] had no actual authority from the owners or managers of the Nordems to contract for the supply of bunkers on their behalf, or on the credit of the ship. They were expressly prohibited from so doing. However, World Fuel Services Corporation had no actual knowledge of that fact. The importance of these findings is that, briefly put, the maritime law of the United States, the law selected by World Fuel Services Corporation and Parkroad to govern their contract, is such that a necessaries man is presumed to have contracted on the credit of the ship. That presumption can only be rebutted by establishing that the necessaries man had actual knowledge that the contracting party did not have authority to bind the ship. If that presumption is not rebutted, American law creates a maritime lien on the ship. On the other hand, under Canadian maritime law, apart from a few exceptions which are not relevant here, a necessaries man does not enjoy a maritime lien. Under sections 22 and 43 of the *Federal Courts Act*, he has a statutory right *in rem* against the ship, but only if her owners are personally liable. As in American law, there is a presumption that the necessaries were ordered on the credit of the ship. However it is not necessary to establish actual knowledge of lack of authority on the part of the necessaries man to rebut that presumption. [4]

Justice Harrington then went on to highlight some of the distinctions between a maritime lien and a statutory right *in rem* and to explain why Canadian choice of law rules make Canada a popular forum for American necessaries men who extend credit to time charterers:

> There are a number of important distinctions between a maritime lien and a statutory right *in rem*. Only one is relevant in this case, that being that a maritime lien may exist even though the owners of the ship are not personally liable. A maritime lien arises at the moment of the transaction, be it for instance a collision, while a statutory right *in rem* only comes into existence when proceedings are instituted, or perhaps only when the action *in rem* is served on the ship (this issue was extensively reviewed in the light of English statutes by Mr. Justice Brandon in the "Monica S", [1968] P. 741, [1967] 3 All E.R. 740, [1967] 2 Lloyd's Rep. 113). The maritime lien travels with the ship into the hands of third-party purchasers for value. However a potential action *in rem* is defeated by a legitimate change of ownership, although the original owners, of course, if personally liable in the first place, remain liable. [5]

The Federal Court also highlighted the fact that Canadian choice of law rules dictate that if a transaction is governed by another system of law, such as American, and that law has been proven to differ from Canadian law, Canada will give effect to it. Canada is an attractive forum for necessaries men who enjoy a maritime lien under the proper law of their transaction in that in ranking priorities Canadian law gives the necessaries men the status of a maritime lien, a status which a Canadian necessaries man does not enjoy. Justice Harrington points out that this is not the situation in England, where priorities are considered to be a matter of procedure governed by the *lex fori*, rather than a matter of substance.[6]

Canadian law was amended in 2009 to give necessaries men carrying on business in Canada a maritime lien against a foreign ship. The services must have been provided at the request of the owner or a person acting on his behalf.[7]

Justice Harrington then went on to look at the evidence in this case and to come to some conclusions on this summary judgment application. The evidence consisted of some affidavit evidence including from two American attorneys regarding American law.

The Federal Court found that the relevant charterparty contained the prohibition against a lien for supplies or necessaries. Clause 7 provided that,"[t]he Charterers undertake … they will not procure any supplies or necessaries or services, including any port expenses and bunkers, on the credit of the owners…."[8]

Justice Harrington first needed to decide if the owners of the Nordems were bound by the contract purportedly made on their behalf by Parkroad. "If so, that is the end of the matter. If not, then the issue becomes whether the presumption that the necessaries were supplied on the credit of the ship has been successfully rebutted."[9] The court found that:

> According to its contract with Parkroad, World Fuel Services relied on commercial registries, such as *Lloyd's Register of Shipping*, to identify the owners of ships. I directed during the hearing that the relevant entries from the Register at the

> time be produced. The owners are stated to be Partenreederei m.s. Nordems. The contract clearly demonstrated World Fuel Services' own experience that the person ordering bunkers may not have actual authority to bind the ship. Had it followed the general provisions of its contract, which was not to extend credit, it would either have been paid or would not have delivered the bunkers at all. *In my opinion it was on notice and should have verified with the owners whether or not Parkroad had authority.* [10] [Emphasis added]

Justice Harrington concluded that under domestic Canadian maritime law the owners of the Nordems, much less her managers, were not personally liable and so the action would be dismissed *in rem* and *in personam*.

The Federal Court then had to determine if American law applied and whether American law would grant World Fuel Services a maritime lien. The Court considered the factors that connect the case to the United States:

> The plaintiff's best case is that it is an American corporation and that because credit was extended the contract was deemed to have been made in the United States. Payment was to be made to a bank in the United States. The contract with Parkroad was governed by American law, with non-exclusive American jurisdiction. On the other hand, the bunkers were ordered in South Korea and delivered in South Africa to a Cypriot flag ship, owned and managed out of Germany. At no relevant time did the Nordems ply American waters, and the ship was arrested in Canada. [11]

After reviewing the case law on how factors are weighed the Federal Court concluded that the non-American factors outweigh the American ones, stating:

> These include the flag of the ship (Cyprus), the domicile of her owners (Germany), the place where the offer to purchase bunkers was accepted (South Korea), the place where the bunkers were delivered (South Africa), and the place where the ship was arrested (Canada). If it is necessary to choose among these laws, the proper law is that of South Africa. There are only two points of contact between the ship owner and the plaintiff. The first is South Africa where the bunkers were supplied. If a maritime lien exists, it existed from that moment. Had credit not been extended, the plaintiff would have been in position to arrest the ship then and there. Since the law of South Africa has not been alleged and proven to differ from Canadian law, the arrest would be set aside as there is no personal liability on the part of the owners and as the presumption that the bunkers were delivered on the credit of the ship has been rebutted. The bunker receipt signed by the master does not even refer to World Fuel Services. The receipt is on the letterhead of Caltex Oil (SA) (Pty) (Ltd), with a Cape Town post office address and Cape Town telephone number. That receipt gives no indication whatsoever that the plaintiff was Caltex's unnamed principal. The second point of contact was Canada, the place of arrest. [12]

The Federal Court ultimately held that the shipowners were not party to the World Fuel Services contract and were not bound by its terms. Parkroad had no actual or ostensible authority to contract on their behalf or on the credit of the ship. The presumption that the bunkers were supplied on the credit of the ship was successfully rebutted. United States law was not the proper law.

The Federal Court of Appeal rejected the attempts of the appellant to claim that the first instance judge had erred with respect to the substance of Canadian law. Nadon J.A. resolutely denied that the first judge had failed to apply the presumption under Canadian law, and dismissed the appellant's efforts to rearticulate the presumption regarding the creation of a lien under Canadian law in a manner that would align with U.S. law. Finally, appellant's premise that the first judge had erred in finding that the presumption in Canadian law had been rebutted was concisely rejected given that Nadon J.A. was "unable to detect from the evidence any conduct of behaviour on the part of the shipowners which could have led the appellant into thinking that [the charterer] was somehow authorized by them to purchase bunkers on their behalf."[13]

As a result, the Federal Court of Appeal confirmed that American and Canadian law were substantively different, and thus that the resolution of the conflicts of law question would be primordial to deciding the case.[14]

The creation of a presumption of liability of a ship-owner for expenses incurred by a charterer not serving as his agent, is an assault on the foundational common law concept of privity of contract. As such, the Court did not seek to determine the law of the contract, which the parties had clearly stipulated as American law, but rather the court sought to identify the law of

the transaction of supply of the bunkers, which would be "the law which had the closest and most substantial connection thereto."[15]

Conclusion

This result of the decision is to be approved, given that it would be inequitable for a charterer and a supplier to determine the liabilities of the ship and ship-owner through their election of the choice of law in their contract which would be most generous in incurring the liability of the ship and ship-owner. The ship and ship-owner would, through the operation of a choice of law clause and the primacy accorded to such clauses in conflicts analysis, *de facto* become the insurer and guarantor of the liabilities of the charterer, even where, as in this case, the charterer was acting in violation of explicit contractual conditions in its agreement with the ship-owner to refrain from engaging the vessel as security.

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ENDNOTES

[1] 2011 FCA 73 [*Nordems Court of Appeal*].
[2] *Ibid* at para 3.
[3] The transactions in this case took place in 2008, before section 139 of the *Marine Liability Act* was amended to grant a statutory maritime lien against foreign vessels in favour of ship suppliers carrying on business in Canada. The principles discussed in the Nordems are still relevant to the shipping community and their legal advisers because these principles still apply to ship suppliers not carrying on business in Canada who seek to enforce their claims through Federal Court in *rem* proceedings in Canada. The Court of Appeal decision includes important affirmations of the Canadian test for liability of a vessel in *rem* and the application of conflicts of law principles.
[4] 2010 FC 332 at para 9 [*Nordems Federal Court*].
[5] *Ibid* at para 11.
[6] *Ibid* at paras 73-74.
[7] See *An Act to Amend the Marine Liability act and the Federal Courts Act and to make consequential amendments to other Acts*, SC 2009, c 21, s 139 [*MLA*].
[8] *Nordems Federal Court*, *supra* note 4 at para 21.
[9] *Ibid* at para 41.
[10] *Ibid at* paras 49-50 [emphasis added].
[11] *Ibid* at para 53.
[12] *Ibid* at para 66.
[13] *Nordems Federal Court of Appeal*, *supra* note 1 at para 62.
[14] What underlies this differing presumptions in Canadian and U.S. law is the fundamental rule of Canadian Maritime Law known generally to practitioners as the rule in the "Jensen Star" but referred to in the Court of Appeal reasons as "Mount Royal." US Admiralty law (having parted company from England in 1776) views the existence of a claim in *rem* and the existence of a maritime lien as practically coterminous. If a maritime lien exists, the ship is liable per se and the claimant need not demonstrate contractual privity with the shipowner. By contrast, Canadian maritime law has evolved differently with a restricted number of "pure" maritime liens and a broader category of statutory rights of arrest. Before the enactment of *MLA* section 139, and continuing with respect to claims by ship suppliers not carrying on business in Canada, and claims by Canadian ship suppliers against Canadian registered vessels, a claim of an unpaid ship supplier cannot be asserted in *rem* against the vessel unless the unpaid ship supplier can demonstrate one of two things: i) the supplier is able to demonstrate it was in contractual privity with the shipowner or that the shipowner somehow acquiesced in, authorized or ratified the transaction so as to give the unpaid supplier a right in *rem* against the ship itself (the rule in the "Jensen Star"); or ii) the supplier can prove that the foreign law governing the supply contract confers a direct maritime lien (the rule in the "Ioannis Daskelelis".)
[15] The decision is important authority that the claimant has to demonstrate that the foreign law which confers a maritime lien, should, by the application of conflicts of law principles, apply.

PRACTICE NOTES / LA PRATIQUE EN BREF

Mitigating Our Clients' Corruption Exposure: Risk Assessment is the First Step

*John W. Boscariol**

Recent enforcement activities in Canada under its *Corruption of Foreign Public Officials Act* ("CFPOA"),[1] including the conviction of Niko Resources Ltd. ("Niko") in June of last year and ongoing high-profile Royal Canadian Mounted Police ("RCMP") investigations of other Canadian companies, has caught the attention of boards and executives across the country.[2] Additional prosecutions or settlements are expected in the near future, as it is understood that the RCMP has over 30 foreign corruption investigations ongoing at this time.

This note highlights the importance for in-house and outside counsel to ensure clients conduct a thorough risk assessment before designing and implementing anti-corruption compliance processes and procedures.

Anti-Corruption Risk Abroad

Canadian companies operating abroad can face particularly high anti-corruption risk exposure depending on the countries in which they operate and their interactions with foreign government officials, whether directly or through agents, consultants or other third parties.

Canadian companies are now beginning to understand the risks and costs of non-compliance with the CFPOA and other anti-bribery regimes that may apply to them, including the US *Foreign Corrupt Practices Act* and the U.K. *Bribery Act 2010* (*"Bribery Act")*.[3] They are beginning to understand the very substantial impact of compliance failure on their directors, executives and employees, share price, the inherent value of their company, as well as their attractiveness to others as a business partner or acquisition target. Many are now looking to take the next step: the implementation of processes and procedures to ensure effective compliance is achieved.

A quick search of the Internet can easily locate many examples of anti-corruption compliance programs and employee and executive training modules. These plans may cover all the right bases, namely implementing written processes and procedures and appropriate internal accounting controls, appointing responsible compliance officers, demonstrating strong senior management support, periodic training and certification, internal auditing, internal reporting and voluntary disclosure, disciplinary procedures for non-compliance, agent and third party due diligence, and contract review.

It is, however, critical that companies ensure they have first conducted a thorough risk assessment before developing, adopting and implementing these compliance mechanisms. Without undertaking an effective risk assessment exercise and then properly tailoring its compliance measures to the company's specific circumstances, the compliance program will be of little assistance, and in some cases can be harmful to the company.

Undertaking Risk Assessment

The internal controls and policies specified in the Probation Order agreed to by Niko and approved by the Court handling their guilty plea are particularly instructive as a list of CFPOA compliance measures expected to be implemented by Canadian companies.

Réduire les risques de corruption pour les clients : l'évaluation des risques constitue la première étape

John W. Boscariol

Les récentes activités liées à l'application de la Loi sur la corruption d'agents publics étrangers (LCAPE) au Canada, notamment la condamnation de la société Niko Resources Ltd. en juin de l'année dernière, et les enquêtes très médiatisées en cours que mène la Gendarmerie royale du Canada (GRC) sur d'autres sociétés canadiennes, ont retenu l'attention des conseils d'administration et des dirigeants d'entreprises dans tout le pays. On s'attend, dans les jours à venir, à ce qu'il y ait d'autres poursuites ou des règlements extrajudiciaires, puisque la GRC aurait ouvert actuellement plus de 30 enquêtes sur des affaires de corruption à l'étranger.

La présente note interpelle particulièrement les juristes internes et externes sur l'importance d'effectuer une évaluation approfondie des risques avant de concevoir et de mettre en œuvre des procédés et procédures de lutte contre la corruption.

John W. Boscariol a obtenu un baccalauréat en commerce (médaille d'or) de l'Université de Toronto en 1980. Il possède un baccalauréat en droit de la Faculté de droit de l'Université de Toronto et a été admis au Barreau de l'Ontario en 1995. En 1998, il a reçu une maîtrise en droit (en commerce international et droit de la concurrence) de la Faculté de droit Osgoode Hall. Ancien président de la Section du droit international de l'Association du Barreau de l'Ontario, il dirige le groupe du droit du commerce et de l'investissement international du cabinet McCarthy Tétrault s.r.l. Il s'est spécialisé dans les questions de conformité et d'application des lois et des politiques liées à la lutte contre la corruption, aux sanctions économiques, aux contrôles des exportations et aux autres lois régissant le commerce transfrontalier

The importance of conducting a risk assessment was highlighted in the Probation Order as follows:

> The company will develop these compliance standards and procedures, including internal controls, ethics and compliance programs, on the basis of a risk assessment addressing the individual circumstances of the company, in particular foreign bribery risks facing the company, including, but not limited to, its geographical organization, interactions with various types and levels of government officials, industrial sectors of operation, involvement in joint venture agreements, importance of licenses and permits in the company's operations, degree of governmental oversight and inspection, and volume and importance of goods and personnel clearing through customs and immigration.[4]

This exercise is a significant one. In providing guidance on its *Bribery Act*, the UK government lists risk assessment as one of six fundamental principles for preventing bribery. It identifies both external and internal risks to be considered.[5] External risks are categorized into five groups: country risk, sectoral risk, transaction risk, business opportunity risk and business partnership risk, while common internal factors include deficiencies in employee training and skills, a culture that rewards excessive risk taking, a lack of clarity in the company's policies, a lack of clear financial controls and a lack of a clear anti-bribery message from senior management.

Some Questions to Consider

Although the length of this note does not permit an exhaustive listing, some key questions and considerations to be addressed with clients include:

- **Where we do stand now?**

  What current controls, due diligence and training programs do we have in place? Are they being taken seriously? Do our employees follow these procedures? What is the level of engagement of our senior management and executives? What is our history of compliance in this area?

- **Where are our operations located?**

  How are those countries ranked on indices, such as Transparency International's *Corruption Perceptions Index*? What is the level of political stability and democracy in these locations? Are we vulnerable to risk of regime change? In addition to the CFPOA, how do other potentially aggressive anti-bribery regimes, such as those of the United States, the United Kingdom or the host country apply to our activities?

- **Where and how do we interact with government officials?**

  What are our government "touchpoints" through all stages of our business operations? What permits and licenses do we require? Do we also deal with government-owned or -controlled entities? How and with whom are our concession or royalty agreements negotiated? Do we need to import goods, equipment and heavy machinery for our operations and how do we deal with customs authorities in that process?

- **Which positions within the company are most exposed?**

  Which executives or employees have responsibilities for dealing with government officials or authorizing related expenditures? How are they compensated? What financial incentives may exist for individuals within the company to engage in bribery of government officials?

- **How do we use third parties in our business operations?**

  What kind of agents and consultants do we retain to assist us in developing and doing business in third countries? Do they interact with government officials on our behalf? How about lawyers, customs brokers and joint venture partners? How do we screen, approve, retain, pay and then monitor these third parties?

With this and other information flowing from their initial risk assessments in hand, companies should be well-positioned to develop anti-corruption compliance processes and procedures on a targeted and cost-effective basis.

John W. Boscariol received his B. Com (Gold Medalist) from the University of Toronto in 1990. He received his LLB from the Faculty of Law at the University of Toronto and was called to the Ontario Bar in 1995. In 1998, he received his LLM (International Trade and Competition Law from the Osgoode Hall Law School). He is the past Chair of the Ontario Bar Association International Law Section and leads McCarthy Tétrault LLP's International Trade & Investment Law Group. He specializes in compliance and enforcement matters related to anti-corruption laws and policies, economic sanctions and export controls and other laws governing the cross-border trade in goods, services and technology and foreign investment. (E-mail: jboscariol@mccarthy.ca)

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ENDNOTES

[1] SC 1998, c 34.

[2] For more analyses on the Niko plea and its impact on Canadian anti-corruption enforcement and compliance, see John Boscariol, "A Deeper Dive into Canada's First Significant Foreign Bribery Case: Niko Resources", *The Globetrotter* 16:1 (December 2011), online: <http://www.oba.org/En/International_en/int_main/news_en.aspx>.

[3] *Foreign Corrupt Practices Act*, 15 USC § 78dd-1; *Bribery Act 2010* (UK), c 23.

[4] *Her Majesty the Queen v Niko Resources Ltd* (24 June 2011), Calgary E-File No CCQ11NIKORESOURCES (Alta QB).

[5] UK, Ministry of Justice, *The Bribery Act 2010 Guidance* (2011), online: <http://www.justice.gov.uk/guidance/bribery.htm>.

TREATIES / TRAITÉS

Canada's Tangled Trade Web: Agreements, Negotiations, Sanctions and Export/Import Controls

*Eduarda M. Matos**

Canada's many trade and trade-related agreements, negotiations, economic sanctions and export/import controls represent an evolving tangled web sometimes difficult to decipher or monitor. From free trade agreements ("FTAs") that have been in force for many years such as NAFTA and the Canada-Israel FTA, to trade negotiations that have just begun like the Trans-Pacific Partnership talks; from foreign investment promotion and protection agreements ("FIPAs") with countries such as Argentina, Russia and Venezuela, to memorandums of understanding ("MOUs") with India and the United Arab Emirates; from trade and investment cooperation arrangements ("TICAs") with South Africa and MERCOSUR, to trade and economic cooperation arrangements ("TECAs") with Iceland and Australia; from frameworks for economic cooperation and trade with the Palestinian Liberation Organization on behalf of the Palestinian Authority, to bilateral agreements with key trading partners such as the United States; from the imposition of trade or economic sanctions against foreign states and non-state actors, to the control of the flow of certain goods to and from certain countries through export/import controls, all of these examples reflect the complexity of Canada's trading relationships and the importance trade plays in the Canadian economy. They also reflect what the current government describes as its pursuit of the most ambitious pro-trade plan in Canadian history, one that focuses on protecting current exports, forging new trade and investment ties with key partners and opening new markets. The following chart, which contains information obtained from Foreign Affairs and International Trade Canada (www.international.gc.ca) and Export Development Canada, (www.edc.ca), provides a comprehensive quick reference on Canada's current trading relationships and pursuits.

L'enchevêtrement des relations commerciales du Canada : accords, négociations, sanctions et contrôles à l'exportation et à l'importation

*Eduarda M. Matos**

Les nombreux engagements commerciaux du Canada sous forme d'accords, de négociations, de sanctions économiques ou de contrôles à l'exportation et à l'importation sont tellement enchevêtrés qu'ils sont devenus difficiles à démêler ou vérifier. Des accords de libre-échange (« ALE ») qui sont en vigueur depuis plusieurs années, tels l'Accord de libre-échange nord-américain (« ALENA ») et l'Accord de libre-échange Canada-Israël, aux négociations qui viennent de s'ouvrir comme les négociations sur le Partenariat transpacifique; des Accords sur la promotion et la protection de l'investissement étranger (« APIE ») avec des pays comme l'Argentine, la Russie et le Venezuela, aux Protocoles d'entente (« PE ») avec l'Inde et les Émirats arabes unis; des Ententes de coopération en matière de commerce et d'investissement (« ECCI ») avec l'Afrique du Sud et le Marché commun du Sud (« MERCOSUR »), aux Arrangements de coopération commerciale et économique (« ACCE ») avec l'Islande et l'Australie; de l'Accord-cadre Canado-Palestinien de coopération économique et commerciale entre le gouvernement du Canada et l'Organisation de libération de la Palestine, agissant au nom de l'Autorité palestinienne, aux accords bilatéraux avec les principaux partenaires commerciaux comme les États-Unis; de l'imposition des sanctions commerciales ou économiques à l'égard d'États étrangers et d'acteurs non étatiques, au contrôle des flux de certaines marchandises destinées à certains pays ou provenant de certains pays par l'entremise des contrôles à l'exportation et à l'importation, tous ces exemples reflètent la complexité et l'importance du rôle que joue le commerce dans l'économie du Canada. Ceci reflète également ce que l'actuel gouvernement décrit comme étant le plus ambitieux programme commercial de l'histoire du pays, un programme axé sur la protection des exportations existantes, le développement de nouveaux liens de commerce et d'investissement avec des partenaires clés et l'ouverture de nouveaux marchés. Le tableau suivant, qui contient des renseignements obtenus d'Affaires étrangères et Commerce international Canada (www.international.gc.ca) et d'Exportation et développement Canada (www.edc.ca), présente une référence brève, mais détaillée, des relations commerciales du Canada et des développements en cours.

FREE TRADE AGREEMENTS ("FTAs")

FTAs in Force	
Canada – Chile	Brought into force on July 5, 1997, the Canada-Chile FTA ("CCFTA") is a comprehensive agreement that covers trade in goods and services, as well as the bilateral investment relationship between the two countries. The CCFTA has been very beneficial to both Canada and Chile with trade between the two countries having more than tripled since its implementation in 1997. Efforts have been under way to modernize and broaden the CCFTA, the highlights of which were the introduction of a new government procurement chapter in 2008 and the signing of a Note of Interpretation on Indirect Expropriation in 2010. In 2012, the two countries signed an agreement to amend the CCFTA by adding a financial services chapter and updating the chapters on government procurement, dispute settlement and custom procedures. Key Industries: construction & infrastructure, environmental infrastructure & waste water, mining & metals, power. Canadian exports to Chile (2011): $818,777,273 Canadian imports from Chile (2011): $1,910,734,928
Canada – Colombia	Brought into force on August 15, 2011. The Canada-Colombia FTA came into force along with a Labour Cooperation Agreement and an Agreement on the Environment. The two countries enjoy good commercial and investment relations, and the presence of Canadian companies in Colombia continues to grow, especially in the mining, oil exploration and printing sectors. Key Industries: construction & infrastructure, environmental infrastructure & waste water, mining & metals, oil & gas, power, telecom. Canadian exports to Colombia (2011): $760,888,169 Canadian imports from Colombia (2011): $799,773,636
Canada – Costa Rica	Brought into force on November 1, 2002. The Canada-Costa Rica FTA ("CCRFTA") came into force along with a Labour Cooperation Agreement and an Agreement on the Environment. The CCRFTA focuses mainly on trade in goods and does not include substantive provisions in areas such as cross-border trade in services, financial services, investment and government procurement. Negotiations to modernize the CCRFTA began in August of 2011 and are ongoing. Comments and input from Canadians are being welcomed as part of the government's consultation process for this trade initiative. Key Industries: Construction & infrastructure, food & beverage. Canadian exports to Costa Rica (2011): $160,755,858 Canadian imports from Costa Rica (2011): $475,761,469
Canada – European Free Trade Association ("EFTA") (Iceland, Liechtenstein, Norway & Switzerland)	Brought into force on July 1, 2009. The Canada-EFTA FTA emphasizes tariff elimination and does not include substantial obligations in areas such as services, investment, or intellectual property. Two meetings of the CEFTA Joint Committee were held recently to discuss the implementation and operation of the Canada-EFTA FTA, as well as its possible expansion into additional areas. Another meeting is planned for Autumn 2012 to discuss possible next steps. Iceland's Key Industries: Machinery – packaging, industrial & analytical instruments, oil & gas, clothing & textiles.

	Norway's Key Industries: Oil & gas, ICT, cleantech, construction & infrastructure Switzerland's Key Industries: Machinery – packaging, industrial & analytical instruments, plastics & chemicals, transportation services, mining & metals, agriculture. Canadian exports to Iceland (2011): $52,461,800 Canadian imports from Iceland (2011): $42,015,350 Canadian exports to Norway (2011): $2,791,783,524 Canadian imports from Norway (2011): $4,344,131,842 Canadian exports to Switzerland (2011): $1,141,382,200 Canadian imports from Switzerland (2011): $3,163,257,143
Canada – Israel	Brought into force on January 1, 1997. The Canada-Israel FTA ("CIFTA") eliminated tariffs on many items including all industrial products and some agricultural and fisheries products. The CIFTA does not include substantive provisions in areas such as services, investment or government procurement. Key Industries: Natural resources, mining & metals, agriculture, consumer goods. Canadian exports to Israel (2011): $399,907,760 Canadian imports from Israel (2011): $982,370,509
Canada – Jordan	Brought into force on October 1, 2012. The Canada-Jordan FTA came into force along with a Labour Cooperation Agreement and an Agreement on the Environment. This FTA will eliminate tariffs on the majority of Canadian exports to Jordan, directly benefiting key Canadian sectors such as forestry, manufacturing, and agriculture and agri-food. Key Industries: Agriculture, mining & metals, power, light manufacturing, oil & gas. Canadian exports to Jordan (2011): $70,145,780 Canadian imports from Jordan (2011): $18,728,359
Canada – Peru	Brought into force on August 1, 2009. The Canada-Peru FTA came into force along with a Labour Cooperation Agreement and an Agreement on the Environment. This FTA eliminated tariffs on certain goods, it promotes two-way investment between Canada and Peru and it has expanded access for Canadian companies into this Latin American country. Key Industries: Construction & infrastructure, environmental infrastructure & waste water, mining & metals, oil & gas, power. Canadian exports to Peru (2011): $516,425,420 Canadian imports from Peru (2011): $4,402,672,597
North American Free Trade Agreement (Canada, U.S.A., Mexico)	Brought into force on January 1, 1994. The North American Free Trade Agreement ("NAFTA") created the world's largest free trade area when it came into force in January of 1994. United States' Key Industries: Agriculture, capital goods, consumer goods, machinery – packaging, industrial & analytical instruments. Mexico's Key Industries: Aerospace, automotive, agriculture, mining & metals, oil & gas, plastics & chemicals, power, telecom. Canadian exports to the United States (2011): $329,799,505,820 Canadian imports from the United States (2011): $220,895,498,794 Canadian exports to Mexico (2011): $5,476,487,629 Canadian imports from Mexico (2011): $24,572,828,961

FTAs – Negotiations Concluded	
Canada – Honduras	Negotiations concluded on August 12, 2011. The Canada-Honduras FTA and parallel agreements on labour and environmental cooperation are currently undergoing a legal review after which they can be formally signed. This FTA will benefit Canadian businesses in many sectors of the Canadian economy, including agriculture, professional services, value added food processing and manufacturing. Key Industries: Agriculture, construction & infrastructure, forestry (lumber, pulp, paper). Canadian exports to Honduras (2011): $49,185,206 Canadian imports from Honduras (2011): $186,059,148
Canada – Panama	Signed on May 14, 2010. Negotiations towards a Canada-Panama FTA began in October of 2008, and after several rounds of talks, the two countries announced the conclusion of those negotiations in August of 2009. The Canada-Panama FTA covers areas such as market access for goods, cross-border trade in services, telecommunications, investment, financial services and government procurement. Key Industries: Construction & infrastructure, food & beverage, mining & metals. Canadian exports to Panama (2011): $111,222,796 Canadian imports from Panama (2011): $124,125,000

FTAS – Ongoing Negotiations	
Canada – Andean Community Countries (Bolivia, Colombia, Ecuador and Peru)	In August of 2002, Canada and the Andean countries of Bolivia, Colombia, Ecuador and Peru, agreed to begin exploratory discussions towards a free trade agreement. However, because not all of the four countries were in a position to move forward with these negotiations at the same time, Canada began negotiating FTAs with Colombia and Peru first. The Canada-Peru FTA came into force on August 1, 2009, along with a Labour Agreement and an Agreement on the Environment. The Canada-Colombia FTA came into force on August 15, 2011. In terms of Ecuador and Bolivia, the Canadian government has agreed to continue discussions with the former while it continues to expand commercial relations with the latter. Bolivia's Key Industries: Environmental infrastructure & waste water, oil & gas, mining & metals. Colombia's Key Industries: construction & infrastructure, environmental infrastructure & waste water, mining & metals, oil & gas, power, telecom. Ecuador's Key Industries: Construction & infrastructure, mining & metals, oil & gas. Peru's Key Industries: Construction & infrastructure, environmental infrastructure & waste water, mining & metals, oil & gas, power. Canadian exports to Bolivia (2011): $16,435,452 Canadian imports from Bolivia (2011): $237,794,899 Canadian exports to Colombia (2011): $760,888,169 Canadian imports from Colombia (2011): $799,773,636 Canadian exports to Ecuador (2011): $281,316,351 Canadian imports from Ecuador (2011): $224,630,389 Canadian exports to Peru (2011): $516,425,420 Canadian imports from Peru (2011): $4,402,672,597

Canada – Caribbean Community ("CARICOM")	CARICOM is a regional grouping of 15 Caribbean countries: Antigua & Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Kitts & Nevis, St. Lucia, St. Vincent & the Grenadines, Suriname, Trinidad & Tobago. Anguilla, Bermuda, British Virgin Islands, Cayman Islands, Turks and Caicos Islands are Associate Members. Negotiations towards a trade agreement between Canada and the CARICOM member countries began in July of 2007. Four rounds of negotiations have been held to date, dealing with a number of issues such as market access, services, investment and development cooperation. A FTA between Canada and CARICOM member countries would benefit many sectors of the Canadian economy including industrial goods, agriculture and fish and seafood. Canadian exports to Barbados (2011): $49,556,575 Canadian imports from Barbados (2011): $6,919,737 Canadian exports to Dominica (2011): $4,037,937 Canadian imports from Dominica (2011): $288,853 Canadian exports to Grenada (2011): $4,750,442 Canadian imports from Grenada (2011): $1,718,032 Canadian exports to Haiti (2011): $37,728,858 Canadian imports from Haiti (2011): $25,743,928 Canadian exports to Montserrat (2011): $325,005 Canadian imports from Montserrat (2011): $290,786 Canadian exports to St. Lucia (2011): $9,430,402 Canadian imports from St. Lucia (2011): $272,278 Canadian exports to Anguilla (2011): $2,422,089 Canadian imports from Anguilla (2011): $271,087 Canadian exports to the B.V.I. (2011): $48,346,362 Canadian imports from the B.V.I. (2011): $820,635
Canada – Central America Four ("CA4") (Honduras, Guatemala, El Salvador and Nicaragua)	Canada agreed to enter into free trade negotiations with the Central American Four countries ("CA4") at the Canada-Central America Summit of September 28, 2000. Formal negotiations were launched in November of 2001 and after 10 rounds the talks reached an impasse in 2004, primarily over market access issues. Negotiations resumed eventually and officials from Canada and the CA4 countries met in 2006, were in contact throughout 2007, and met again on three separate occasions in 2008. More meetings took place in 2009 and 2010, at which point Canada concluded that among the CA4 countries, Honduras offered the best opportunity to conclude a free trade agreement in the short-term. The two countries decided therefore to concentrate on bilateral negotiations, successfully negotiating an FTA along with parallel agreements on labour and environmental cooperation, by August of 2011. Honduras' Key Industries: Agriculture, construction & infrastructure, forestry (lumber, pulp, paper). Guatemala's Key Industries: Agriculture, construction & infrastructure, forestry (lumber, pulp, paper). El Salvador's Key Industries: Agriculture, construction & infrastructure, forestry (lumber, pulp, paper). Canadian exports to Honduras (2011): $49,185,206 Canadian imports from Honduras (2011): $186,059,148

	Canadian exports to Guatemala (2011): $109,636,340 Canadian imports from Guatemala (2011): $403,981,259 Canadian exports to El Salvador (2011): $36,205,693 Canadian imports from El Salvador (2011): $129,441,454 Canadian exports to Nicaragua (2011): $37,313,185 Canadian imports from Nicaragua (2011): $333,663,991
Canada – Costa Rica (Negotiations to modernize the "CCRFTA")	The Canada-Costa Rica FTA ("CCRFTA") was brought into force on November 1, 2002. In August of 2010, it was announced that Canada and Costa Rica had agreed to begin negotiations toward modernizing the CCRFTA. Exploratory discussions and public consultations have been taking place since then and the Government of Canada is currently welcoming comments and input of Canadians in this regard. Key Industries: Construction & infrastructure, food & beverage. Canadian exports to Costa Rica (2011): $160,755,858 Canadian imports from Costa Rica (2011): $475,761,469
Canada – Dominican Republic	Free Trade negotiations between Canada and the Dominican Republic were launched in June of 2007 and ended without success in December of 2009. However, officials continue to exchange information with the goal of identifying a mutually acceptable basis upon which to re-launch negotiations. Key Industries: Construction & infrastructure, food & beverage, power. Canadian exports to the Dominican Republic: $148,768,143 Canadian imports from the Dominican Republic: $148,512,831
Canada – European Union: Comprehensive Economic and Trade Agreement ("CETA")	Negotiations towards a Comprehensive Economic and Trade Agreement ("CETA") between Canada and the EU were launched in May of 2009. Thus far, nine rounds of negotiations have been completed and the goal of both parties is to reach a successful conclusion in 2012. Significant progress has been made in areas such as goods, services, investment and government procurement, but key issues remain to be explored and negotiated. Canada and the EU have a long history of economic cooperation. Composed of 27 Member States with a total population of over 500 million, the EU is the world's largest single common market and as an integrated block, it represents Canada's second largest trading partner in goods and services. The government of Canada has made the CETA negotiations a priority in its international trade agenda. Key Industries: Information and communications technology (software, wireless), life sciences (biopharmaceuticals, medical devices, services), renewable energy (bioenergy, wind), aerospace and defence (avionics, aerostructures), agriculture, food, and beverages (shrimp and seafood, health and wellness). Canadian exports to the E.U. (2011): $40,073,232,126 Canadian imports from the E.U. (2011): $52,053,640,442
Canada – India	Free trade negotiations between Canada and India were launched in November of 2010. Five rounds of negotiations toward a Comprehensive Economic Partnership Agreement ("CEPA") have been held to date, with the last one having taken place in New Delhi from July 24 to 26, 2012. These negotiations are a key priority for the government of Canada whose goal is to conclude the CEPA in 2013. Key Industries: Automotive, clean technology, forestry (lumber, pulp, paper), mining &

	metals, telecommunications, transportation services. Canadian exports to India (2011): $2,628,585,061 Canadian imports from India (2011): $2,533,472,103
Canada – Japan	Negotiations towards a comprehensive and high-level economic partnership agreement ("EPA") between Canada and Japan were launched in March of 2012, following the release that same month of a Joint Study examining the feasibility for a free trade agreement between the two countries. The Joint Study also outlined a number of issues which could be negotiated, including trade in goods, services, investment and trade facilitation. Key Industries: Agriculture, natural resources, oil & gas, telecom. Canadian exports to Japan (2011): $10,670,582,514 Canadian imports from Japan (2011): $13,057,675,788
Canada – Korea	Free trade negotiations between Canada and Korea were launched in July of 2005. Since then, the two countries have held thirteen rounds of negotiations covering a wide range of issues, including in trade in goods, rules of origin, customs procedures, trade facilitation, non-tariff measures, cross-border trade in services, financial services, temporary entry, investment, government procurement, competition, intellectual property, e-commerce, dispute settlement and institutional provisions. Negotiations are now well advanced, but resolving the remaining sensitive issues will be challenging. Key Industries: Oil & gas, mining & metals, power, construction & infrastructure, environmental infrastructure & waste water, telecom, agriculture. Canadian exports to Korea (2011): $5,098,434,553 Canadian imports from Korea (2011): $6,604,750,944
Canada – Morocco	Free trade negotiations between Canada and Morocco were launched in January of 2011. Three rounds of negotiations have taken place thus far with good progress made in areas such as custom procedures, sanitary and phytosanitary measures and government procurement. An FTA with Morocco would be Canada's first with an African country and a potentially important step to deepen Canada's commercial presence in the region. Key Industries: Construction & infrastructure, mining & metals, telecom, agriculture, transportation services, aerospace. Canadian exports to Morocco (2011): $299,794,541 Canadian imports from Morocco (2011): $119,110,335
Canada – Singapore	Free trade negotiations between Canada and Singapore were launched in October of 2001. Six rounds of negotiations ensued until December of 2003 when talks were suspended due to an impasse over certain provisions of the FTA. The parties agreed to resume talks and two rounds of negotiations followed in 2007, but an FTA has not yet materialized. Negotiations have covered a wide range of topics such as trade in goods, trade in services, financial services, investment, government procurement, dispute settlement and competition policy, but more work remains to be done on issues such as market access for services and investment. Key Industries: Aerospace, agriculture, biotechnology, clean technology, environmental infrastructure & waste water, healthcare, information & communication technologies, telecom. Canadian exports to Singapore (2011): $804,358,079 Canadian imports from Singapore (2011): $1,555,287,241

Canada – Trans-Pacific Partnership Negotiations	The Trans-Pacific Partnership Negotiations ("TPP") currently comprise Australia, Brunei Darussalam, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam representing a market of more than 658 million people and a combined GDP of $20.5 trillion. Canada joined the TTP in October of 2012. Fourteen TPP negotiating rounds have taken place thus far, and the next round is scheduled to take place in December of 2012 in Auckland, New Zealand. Negotiators will continue to act on the direction provided in the *TPP Leaders' Statement* with a view to making progress on key elements of the agreement's outline announced by TTP leaders in November of 2011: o *Comprehensive market access: to eliminate tariffs and other barriers to goods and services trade and investment, so as to create new opportunities for our workers and businesses and immediate benefits for our consumers.* o *Fully regional agreement: to facilitate the development of production and supply chains among TPP members, supporting our goal of creating jobs, raising living standards, improving welfare and promoting sustainable growth in our countries.* o *Cross-cutting trade issues: to build on work being done in APEC and other fora by incorporating in TPP four new, cross-cutting issues. These are:* - *Regulatory coherence. Commitments will promote trade between the countries by making trade among them more seamless and efficient.* - *Competitiveness and Business Facilitation. Commitments will enhance the domestic and regional competitiveness of each TPP country's economy and promote economic integration and jobs in the region, including through the development of regional production and supply chains.* - *Small- and Medium-Sized Enterprises. Commitments will address concerns small- and medium-sized enterprises have raised about the difficulty in understanding and using trade agreements, encouraging small- and medium-sized enterprises to trade internationally.* - *Development. Comprehensive and robust market liberalization, improvements in trade and investment enhancing disciplines, and other commitments, including a mechanism to help all TPP countries to effectively implement the Agreement and fully realize its benefits, will serve to strengthen institutions important for economic development and governance and thereby contribute significantly to advancing TPP countries' respective economic development priorities.* o *New trade challenges: to promote trade and investment in innovative products and services, including related to the digital economy and green technologies, and to ensure a competitive business environment across the TPP region.* o *Living agreement: to enable the updating of the agreement as appropriate to address trade issues that emerge in the future as well as new issues that arise with the expansion of the agreement to include new countries.*
Canada – Ukraine	Negotiations on a bilateral free trade agreement between Canada and the Ukraine were launched in mid-May of 2010. Five rounds of negotiations have been held since then, but more work remains to be done. Key Industries: Agriculture, ICT, mining & metals, oil & gas, transportation services. Canadian exports to Ukraine (2011): $150,190,919 Canadian imports from Ukraine (2011): $136,348,202

Free Trade Area of the Americas ("FTAA")	The Free Trade Area of the Americas ("FTAA"), a collaboration among thirty four democratic governments in the Americas, including Canada, was first conceived in principle in December of 1994 at the inaugural Summit of the Americas held in Miami. Formal free trade negotiations among the thirty four member countries of the FTAA were launched in April of 1998 and continued until February of 2004. Such negotiations were carried out by nine different groups with mandates to negotiate in specific substantive areas: market access; investment; services; government procurement; dispute settlement; agriculture; intellectual property rights; subsidies, anti-dumping and countervailing duties; and competition policy. Annual meetings of the FTAA trade ministers were held to review progress and make decisions, including on detailed guidance to negotiators. At the eighth annual meeting of the FTAA trade ministers in November of 2003, agreement was reached on a more flexible negotiating framework for the final phase of the FTAA negotiations. Negotiators attempted to implement the new framework, but consensus could not be reached and as a result, formal negotiations have been suspended since February 2004.

FTAs – Exploratory Discussions	
Canada – Israel (Negotiations for the modernization of)	Brought into force on January 1, 1997, the Canada-Israel FTA ("CIFTA") eliminated tariffs on many items including all industrial products and some agricultural and fisheries products. The CIFTA does not include substantive provisions in areas such as services, investment or government procurement. On October 10, 2010, it was announced that Canada and Israel were to undertake steps toward modernizing the existing CIFTA. Key Industries: Natural resources, mining & metals, agriculture, consumer goods. Canadian exports to Israel (2011): $399,907,760 Canadian imports from Israel (2011): $982,370,509
Canada – MERCOSUR Exploratory Trade Discussions	MERCOSUR, also known as the Southern Cone Common Market, is a customs union established in 1991 by Argentina, Brazil, Paraguay and Uruguay. On June 24, 2011, the Canadian government announced that Canada and MERCOSUR were entering into exploratory discussions to enhance their trade relationship. Three exploratory meetings have taken place thus far, the last of which took place in May of 2012 in Ottawa. Argentina's Key Industries: Telecom. Brazil's Key Industries: Mining & metals, oil & gas, Telecom, transportation services. Paraguay's Key Industries: Agriculture, forestry (lumber, pulp, paper), telecom. Uruguay's Key Industries: Construction & infrastructure, environmental infrastructure & waste water, forestry (lumber, pulp, paper), telecom. Canadian exports to Argentina (2011): $495,296,016 Canadian imports from Argentina (2011): $2,358,757,983 Canadian exports to Brazil (2011): $2,840,773,482 Canadian imports from Brazil (2011): $3,880,041,627 Canadian exports to Paraguay (2011): $13,737,378 Canadian imports from Paraguay (2011): $6,299,802 Canadian exports to Uruguay (2011): $115,793,725 Canadian imports from Uruguay (2011): $40,924,895

Canada – Thailand Free Trade Agreement Exploratory Discussions	On March 23, 2012, it was announced that Canada and Thailand will pursue exploratory discussions toward a bilateral free trade agreement. Canada and Thailand enjoy a close economic relationship based on 50 years of cooperation. Thailand is Canada's largest merchandise trading partner in the Association of South East Asian Nations ("ASEAN"). Thailand's Key Industries: Agriculture, construction & infrastructure, light manufacturing, mining & metals, power, telecom. Canadian exports to Thailand (2011): $839,166,173 Canadian imports from Thailand (2011): $2,674,510,935
Canada – Turkey Free Trade Agreement Exploratory Discussions	In October of 2009, Turkey expressed its interest in pursuing an FTA with Canada. An informal meeting of officials from both countries took place in February of 2010 followed by public consultations on this initiative in August of 2010. Formal exploratory talks took place in October of 2010 in Ankara, but the parties came to the conclusion that there was not sufficient common ground to pursue ambitious and comprehensive free trade negotiations at the time. Turkey's Key Industries: Construction & infrastructure, forestry (lumber, pulp, paper), mining & metals, oil & gas, services – non-industrial, transportation services, telecom. Canadian exports to Turkey (2011): $1,271,493,189 Canadian imports from Turkey (2011): $1,122,316,998

FOREIGN INVESTMENT PROMOTION AND PROTECTION AGREEMENTS ("FIPAs")

A Foreign Investment Promotion and Protection Agreement ("FIPA") is a bilateral agreement designed to protect and promote foreign investment through legally-binding rights and obligations. FIPAs set out the respective rights and obligations of the countries that are signatories to the treaty with respect to the treatment of foreign investment. Canada began negotiating FIPAs in 1989 to secure investment liberalisation and protection commitments on the basis of a model agreement developed under the auspices of the Organization for Economic Cooperation and Development ("OECD").

FIPAs				
In Force		**Negotiations Concluded**		**Ongoing Negotiations**
Canada – Argentina	April 29, 1993	Canada – Bahrain	Feb. 2010	Canada – Bénin
Canada – Armenia	March 29, 1999	Canada – China	Feb. 2012	Canada – Burkina Faso
Canada – Barbados	Jan. 17, 1997	Canada – India	Sep. 2011	Canada – Cameroon
Canada – Costa Rica	Sept. 29, 1999	Canada – Kuwait	Sep. 2011	Canada – Côte d'Ivoire
Canada – Croatia	Jan. 30, 2001	Canada – Madagascar	Aug. 2008	Canada – Ghana
Canada – Czech Republic	Jan. 22, 2012	Canada – Mali	Oct. 2011	Canada – Indonesia
Canada – Ecuador	June 6, 1997			Canada – Kazakhstan
Canada – Egypt	Nov. 3, 1997			Canada – Mongolia
Canada – Hungary	Nov. 21, 1993			Canada – Pakistan
Canada – Jordan	Dec. 14, 2009			Canada – Tanzania
Canada – Latvia	Nov. 24, 2011			Canada – Tunisia
Canada – Lebanon	June 19, 1999			Canada – Vietnam
Canada – Panama	Feb. 13, 1998			Canada – Zambia
Canada – Peru	June 20, 2007			

Canada – Philippines	Nov. 13, 1996			
Canada – Poland	Nov. 22, 1990			
Canada – Romania	Nov. 23, 1991			
Canada – Russia	June 27, 1991			
Canada – Slovak Republic	March 14, 2012			
Canada – Thailand	Sept. 24, 1998			
Canada – Trinidad & Tobago	July 8, 1996			
Canada – Ukraine	July 24, 1995			
Canada – Uruguay	June 2, 1999			
Canada – Venezuela	Jan. 28, 1998			

OTHER TYPES OF AGREEMENTS AND INITIATIVES

Memorandums of Understanding ("MOUs")	
Memorandum of Understanding between the Government of Canada and the Government of the Republic of India on the Establishment of a Joint Study Group to Examine the Feasibility of a Comprehensive Economic Partnership Agreement ("CEPA")	This MOU between Canada and India was signed in November of 2009. It committed the two countries to establishing a Joint Study Group to examine the feasibility of the CEPA, and it set out the objectives of such agreement: i. Broaden and deepen cooperation in all economic fields; ii. Encourage trade and investment flows, bilaterally and regionally; iii. Contribute to trade and investment facilitation through minimizing tariff and non-tariff barriers, reducing any administrative costs; iv. Improve business climate in the two countries; v. Enhance transparency of regulation and promote cooperation among relevant institutions. Key Industries: Automotive, clean technology, forestry (lumber, pulp, paper), mining & metals, telecommunications, transportation services. Canadian exports to India (2011): $2,628,585,061 Canadian imports from India (2011): $2,533,472,103
Memorandum of Understanding between the Ministry of Economy of United Arab Emirates and the Department of Foreign Affairs and International Trade of Canada on Economic Cooperation, Trade and Investment	This MOU between Canada and the United Arab Emirates was signed in March of 2009 and it had the following objectives: a. To enhance economic relations in the fields of trade, industry, services and investment; b. To strengthen cooperation with a view to liberalizing trade and investment between the Participants in accordance with their respective laws and international obligations; c. To facilitate the increased involvement of the private sector in trade and commercial cooperation; d. To promote a favourable environment and complementary activities to encourage private sector investment between the Participants. This MOU also established a Joint-Economic Committee which will meet once every two years to discuss issues related to economic cooperation, trade and investment between the two countries.

Central America Memorandum of Understanding on Trade and Investment ("MOUTI")	The MOUTI was signed by Canada and the Central American countries of Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua in March of 1998. It has the following objectives: a. To enhance economic relations in the fields of trade and investment. b. To strengthen their cooperation with a view to liberalizing trade and investment between the Parties, in accordance with the principles of the World Trade Organization and the process to establish the Free Trade Area of the Americas. c. To maintain the operation of free market economies and highlight the importance of private sector initiatives as sources of prosperity, in order to promote economic development. d. To strengthen and diversify cooperative actions between the Parties, as defined in Article II of this Memorandum of Understanding. e. To promote a favourable environment and complementary activities to encourage private sector investment between the Parties. f. To agree on formal mechanisms for the promotion and protection of investment. This MOU also established a Council on Trade and Investment at the ministerial level comprised of the Ministers of Economy or Foreign Trade of Central America and the Minister for International Trade of Canada, and an Executive Committee comprised of the Deputy Ministers of Economy or Foreign Trade of Central America and the Deputy Minister for International Trade of Canada.

Trade and Investment Cooperation Arrangements ("TICAs")		**Trade and Economic Cooperation Arrangements ("TECAs")**	
Canada – Andean Community	May 31, 1999	Canada – Iceland	March 24, 1998
Canada – South Africa	Sept. 24, 1998	Canada – Norway	Dec. 3, 1997
Canada – Southern Cone Common Market ("MERCOSUR")	June 16, 1998	Canada – Switzerland	Dec. 9, 1997
		Canada – Australia	Nov. 15, 1995

Frameworks for Economic Cooperation and Trade	
Canadian – Palestinian Framework for Economic Cooperation and Trade	On February 27, 1999, Canada concluded the Joint Canadian-Palestinian Framework on Economic Cooperation and Trade with the Palestinian Liberation Organization ("PLO") on behalf of the Palestinian Authority ("PA").

Bilateral Canada – U.S.A. Agreements	
Canada – U.S. Agreement on Government Procurement	On February 12, 2010, Canada and the United States signed an agreement that will allow Canadian companies to participate in U.S. infrastructure projects financed under the American Recovery and Reinvestment Act.
Canada – U.S. Softwood Lumber Agreement	Sept. 12, 2006
Amendments to the Canada – U.S. Softwood Lumber Agreement	Oct. 12, 2006

Ongoing Negotiations	
Bilateral Air Negotiations between Canada and Foreign Countries	Air transportation has experienced significant growth in Canada and around the world over the past several decades, leading to an increase in the global flow of people and goods. The negotiation of air transport agreements between Canada and foreign countries is the responsibility of the Chief Air Negotiator at Foreign Affairs and International Trade Canada, in collaboration with Transport Canada. Canada currently has bilateral air agreements with more than 75 countries. Since December of 2006 alone, Canada signed or updated air agreements with the following countries: • Colombia, Honduras, Nicaragua, Curacao and Saint Maarten (April 2012). • China (February 2011) • Japan (October 2011) • Mexico, Costa Rica, Brazil (August 2011) • Qatar (February 2011) • Algeria (January 2011) • Egypt, Jamaica, Trinidad and Tobago (December 2010) • Switzerland (October 2010) • El Salvador (April 2010) • Tunisia, Ethiopia (March 2010) • Morocco, Cuba (February 2010) • European Union (December 2009) • South Africa (August 2009) • New Zealand, Republic of Korea (July 2009) • Turkey (March 2009) • Dominican Republic (September 2008) • Panama (June 2008) • Philippines (May 2008) • Barbados (February 2008) • Mexico (December 2007) • Singapore (November 2007) • Iceland, Jordan (July 2007) • Kuwait (May 2007) • Ireland (April 2007) • United States of America (March 2007) • Croatia and Serbia (December 2006)
Canada – European Union Trade and Investment Enhancement Agreement (“TIEA”)	Leaders from Canada and the European Union agreed at a summit in Ottawa in March of 2004, to a framework for a new Canada-EU Trade and Investment Enhancement Agreement (“TIEA”) and reiterated their commitment to reaching a successful conclusion to the World Trade Organization’s (“WTO”) Doha Development Agenda. The TIEA is an ambitious and forward-looking initiative that responds to current issues, tries to anticipate future challenges and creates opportunities to broaden and deepen the trade, investment and overall relationship between Canada and the EU. This agreement is intended to move beyond traditional market access issues and into areas such as trade and investment facilitation, competition, mutual recognition of professional qualifications, financial services, e-commerce, temporary entry, small- and medium-sized enterprises, sustainable development, civil society consultation, and science and technology. Formal TIEA negotiations were launched in Brussels in May of 2005, and three rounds of talks have taken place thus far, the last of which took place in February of 2006.

Ongoing Initiatives	
Canada – China Economic Complementarities Study	On August 15, 2012, the release of the Canada-China Economic Complementarities Study was announced by representatives of both countries. The Study highlights the strong momentum and expansion in Canada-China trade and economic relations, and identifies a number of important complementarities and prospects for growth. Key Industries: Aerospace, agriculture, mining & metals, oil & gas, telecommunications, transportation services. Canadian exports to China (2011): $16,809,661,570 Canadian imports from China (2011): $48,152,674,921

TRADE SANCTIONS & EXPORT/IMPORT CONTROLS

Trade Sanctions

Trade or economic sanctions against foreign states and non-state actors are an important tool used by the international community to enforce international norms and laws. Sanctions can encompass a wide variety of measures, including limitations on official and diplomatic contacts or travel, the imposition of legal measures to restrict or prohibit trade or other economic activity, or the seizure or freezing of property situated in the country imposing sanctions. Although there have been instances where Canada unilaterally imposed sanctions against certain countries, most often it does so in support of United Nations initiatives by adopting those UN initiatives into Canadian domestic law.

Export/Import Controls

Export and import controls are also an important tool used by the Canadian government to, among other things, regulate trade in military goods and prevent the proliferation of weapons of mass destruction, prevent the supply of military goods to countries that threaten Canada's security, protect vulnerable Canadian industries, obtain negotiated benefits from international agreements, implement trade restrictions in support of Canada's supply management programs, and implement UN Security Council trade sanctions.

The *Export and Import Permits Act* ("EIPA") was first enacted in 1947, and it delegates to the Minister of Foreign Affairs wide discretionary powers to control the flow of goods contained in specified lists provided for under the Act. The EIPA provides for the establishment of lists known as: the *Import Control List* ("ICL"), the *Export Control List* ("ECL"), and the *Area Control List* ("ACL"):

The ICL generally lists goods some of which are only controlled for certain countries of origin. All goods contained in this list require an import permit (agricultural products, firearms, textiles and clothing and steel).

The ECL is a list of goods only, all of which also require an export permit (military and strategic goods and technology, softwood lumber, firearms, sugar and sugar containing products, peanut butter, logs and U.S.-origin goods and technology).

- The ACL is a list of countries for which export permits are required to export any and all goods (currently Belarus and the Democratic People's Republic of Korea or North Korea).

Terrorism	Terrorism has become an increasingly dangerous force in today's world and the international community has adopted several measures to undermine it, including trying to prevent terrorist organizations from using the global financial system to further their activities. Canada has established a process for the listing of terrorist entities in order to apply specified measures, such as the freezing of assets, to those who are listed. This process has taken the form of three distinct terrorist listing mechanisms: the *United Nations Al-Qaida and Taliban Regulations*, the *Regulations Implementing the United Nations Resolutions on the Suppression of Terrorism*, and the *Criminal Code*.

	1) *Al-Qaida and Taliban Regulations* The *United Nations Al-Qaida and Taliban Regulations* (SOR/99-444) (the "*Al-Qaida and Taliban Regulations*") were introduced in 1999 and freeze the assets of the Taliban, Osama bin Laden and his associates, and the members of the Al-Qaida organization, and prevent the supply, sale, and transfer of arms and technical assistance to them. **2) *Suppression of Terrorism Regulations*** The *Regulations Implementing the United Nations Resolutions on the Suppression of Terrorism* (SOR/2001-360), as amended (the "*Suppression of Terrorism Regulations*") were made in 2001 and create a Canadian list of terrorist individuals and entities, in the Schedule to the regulations. The assets of those covered by the *Suppression of Terrorism Regulations* are frozen, and it is illegal to raise funds on their behalf. The Schedule to the *Suppression of Terrorism Regulations* currently lists among others: Khalid Shaikh Mohammed, Real IRA, Al Aqsa Islamic Bank, Continuity Irish Republican Army, New People's Army/Communist Party of the Philippines, Palestinian Relief and Development Fund (Interpal) and Al-Aqsa Foundation. **3) Criminal Code** The *Criminal Code* also contains a process to list and apply appropriate criminal measures to listed entities which currently include among others: Al Qaida , Al Shabaab, Al-Aqsa Martyrs' Brigade ("AAMB"), Autodefensas Unidas de Colombia ("AUC"), Euskadi Ta Askatasuna ("ETA"), Fuerzas Armadas Revolucionarias de Colombia ("FARC"), Hamas (Harakat Al-Muqawama Al-Islamiya) ("Islamic Resistance Movement"), International Sikh Youth Federation ("ISYF"), Kurdistan Workers Party ("PKK"), Liberation Tigers of Tamil Eelam ("LTTE"), Palestine Liberation Front ("PLF"), Popular Front for the Liberation of Palestine - General Command ("PFLP-GC"), Popular Front for the Liberation of Palestine ("PFLP"), Sendero Luminoso ("SL"), Tehrik-e-Taliban Pakistan ("TTP"), Vanguards of Conquest ("VOC") and World Tamil Movement ("WTM").
Burma / Myanmar	Sanctions against Burma or Myanmar were imposed in December of 2007 through the *Special Economic Measures (Burma) Regulations*, or the *Burma Regulations*. These Regulations imposed a number of prohibitions on import, export, investment, the docking and landing of ships and airplanes, and the provision or acquisition of financial services. These sanctions were imposed in response to human rights violations in Burma, but there have been a number of positive developments since 2010, most notably the release of pro-democracy opposition leader and Nobel Laureate Aung San Suu Kyi. In April of 2012, Canada announced substantial changes to its sanctions against Burma. Prohibitions on imports, exports and investment have for the most part been removed, but a few prohibitions remain: trade in arms and related material is still forbidden, along with technical and financial assistance related to military activities. An asset freeze and prohibition on transactions also remain in place against designated individuals and entities.
Belarus	In December of 2006, the Canadian government issued a notice advising exporters that Belarus had been added to the *Area Control List* ("ACL"). This was in response to the deteriorating human rights situation in Belarus following the March 19, 2006 presidential election. The notice also stated that all applications for permits to export items to Belarus will be reviewed on a case-by-case basis. Permits for humanitarian goods, including food, clothing, medicines, medical supplies, information material, casual gifts and personal effects belonging to persons leaving Canada for Belarus, will generally be approved. Permits for other items will generally be denied.
Cote d'Ivoire	In November of 2004, the United Nations Security Council imposed sanctions against Côte d'Ivoire in response to the resumption of hostilities there and the repeated violations of a ceasefire

	agreement signed on May 3, 2003. These sanctions have been renewed several times since 2004, most recently in March of 2011. Subject to certain exceptions, the measures imposed against Côte d'Ivoire include a prohibition on the export of arms and related material to any person in Côte d'Ivoire, a prohibition on the provision to any person in Côte d'Ivoire of technical assistance related to military activities, an assets freeze against persons designated by the Committee of the Security Council and a travel ban against persons designated by the same Committee.
Democratic Republic of Congo	In July of 2003, the United Nations Security Council imposed sanctions against the Democratic Republic of the Congo ("DRC") in response to continuing hostilities in the eastern part of the country which were threatening the peace process. These sanctions have been modified and strengthened since 2003 and include, subject to certain exceptions, a prohibition on the export of arms and related materiel to any person in the territory of the DRC, a prohibition on the provision, to any person in the DRC, of technical assistance related to military activities, an assets freeze against persons designated by the relevant UN sanctions committee, and a travel ban against persons designated by the same committee.
Eritrea	In January of 1992, the United Nations Security Council ordered an immediate and complete embargo on all deliveries of weapons and military equipment to Somalia. This was in response to the rapid deterioration of the situation and the heavy loss of human life and widespread material damage resulting from the conflict in that country. More sanctions were introduced from 2001 to 2008, and again in 2009 as Eritrea continued to play a destabilizing role in Somalia. The measures imposed by the United Nations Security Council in 2009 included a prohibition on the sale, supply or transfer of arms and related material to Eritrea and to persons designated by the relevant UN sanctions committee, a prohibition on the provision to Eritrea and to persons designated by the same committee of technical, training, financial or other assistance related to military activities or to the supply, sale, transfer, manufacture, maintenance or use of arms and related material of all types, an assets freeze and travel ban against certain persons.
Guinea-Bissau	In May of 2012 and in response to a military coup which occurred the previous month in Guinea-Bissau, the United Nations Security Council imposed certain measures against this small African country.
Iran	In July of 2010, Canada imposed sanctions against Iran under the *Special Economic Measures Act* ("SEMA"). These sanctions were in response to Iran's continued violation of its international obligations by ignoring successive UN Security Council resolutions to cooperate fully with the International Atomic Energy Agency ("IAEA") and suspend its enrichment-related activities. In October of 2011, Canada imposed further sanctions against Iran, this time in response to reports of an Iranian-coordinated plot to assassinate the Saudi ambassador to the United States. In November of 2011 and in response to the IAEA's assessment of Iran's nuclear program, Canada imposed further sanctions against Iran under the SEMA, prohibiting financial transactions with Iran, expanding and amending the list of prohibited goods, and adding new individuals and entities to the list of designated persons found in Schedule 1 of the SEMA regulations. In January of 2012, Canada imposed further sanctions against Iran under the SEMA, and on September 7, 2012, Foreign Affairs Minister John Baird announced the closure of the Canadian embassy in Iran and the expulsion of Iranian diplomats from Canada.
Iraq	In August of 1990, the United Nations Security Council imposed comprehensive sanctions against the regime of Saddam Hussein in response to Iraq's invasion of Kuwait. Most sanctions against Iraq were lifted in May of 2003, with the exception of an embargo against weapons and a prohibition on dealing in stolen Iraqi cultural property.

Lebanon	In August of 2006, the United Nations Security Council imposed sanctions against Lebanon, in response to the continued escalation of hostilities in Lebanon and Israel stemming from Hizbollah's attack of July 12, 2006, on Israel.
Libya	In February of 2011, the United Nations Security Council imposed sanctions against Libya in response to the situation in the Libyan Arab Jamahiriya involving violence and the use of force against civilians. With the eventual fall of the Qadahfi regime and the need to help stabilize Libya, Canada announced in September of 2011 that it had lifted its unilateral sanctions in order to support the Libyan people and the new governing authorities.
Liberia	In March of 2001, the United Nations Security Council imposed sanctions against Liberia in response to former President Taylor's support for the Revolutionary United Front in Sierra Leone. Additional sanctions were imposed in May of 2003 and subsequently replaced and revised to reflect changing circumstances in Liberia.
North Korea	In August of 2011, Canada imposed sanctions against North Korea under the *Special Economic Measures Act* ("SEMA"). These sanctions were in addition to existing sanctions passed under the *United Nations Act* and provide for among other things, a ban on all exports, a ban on all imports to Canada from North Korea, a ban on all new investment in North Korea, a ban on the provision of financial services to North Korea and to persons in North Korea, and a ban on the docking and landing in, and transiting of, Canada by North Korean ships and aircraft.
Sierra Leone	In October of 1997, the United Nations Security Council imposed sanctions against Sierra Leone in response to the violence and loss of life and deteriorating humanitarian conditions there following the military coup of May 25, 1997. The sanctions regime was subsequently modified and eventually terminated in September of 2010.
Somalia	In January of 1992, the United Nations Security Council imposed a complete embargo on all deliveries of weapons and military equipment to Somalia in response to the rapid deterioration of the situation in Somalia and the heavy loss of human life and widespread material damage resulting from the conflict in the country. Additional sanctions were imposed in November of 2008 in response to the acts of violence in Somalia and the increase in acts of piracy and armed robbery at sea against vessels off the coast of Somalia. On June 8, 2012, Canada imposed further sanctions against Somalia.
Sudan	In July of 2004, the United Nations Security Council imposed sanctions against Sudan in response to the humanitarian crisis and widespread human rights violations resulting from the conflict in Darfur region.
Syria	In May of 2011, Prime Minister Harper announced that targeted sanctions would be imposed against members of the current Syrian regime under the *Special Economic Measures Act*. However, as the situation in Syria continued to deteriorate, Canada expanded its targeted sanctions: • On August 13, 2011, Canada began taking measures to freeze the assets of additional individuals and entities associated with the Syrian government. • On October 4, 2011, Canada expanded its targeted sanctions by prohibiting imports of petroleum products from Syria and new investments in the Syrian oil industry. • On December 23, 2011, Canada expanded its targeted sanctions by prohibiting all imports from Syria, except for food for human consumption, as well as all new investment in Syria and the export to Syria of telecommunications monitoring equipment. • On January 25, 2012, Canada expanded its targeted sanctions by imposing an assets freeze and dealings prohibition on additional individuals and entities associated with the Assad regime.

	• On March 5, 2012, Canada expanded its targeted sanctions by broadening the prohibition on financial services. • On March 30, 2012, Canada expanded its targeted sanctions by imposing an assets freeze and dealings prohibition on additional individuals and entities associated with the Assad regime. • On May 18, 2012, Canada expanded its targeted sanctions by prohibiting the export, sale, supply or shipping of luxury goods to Syria. • On July 6, 2012, Canada expanded its targeted sanctions by prohibiting the export, sale, supply or shipping to Syria of a number of goods that can be used for internal repression as well as in the production of chemical and biological weapons. • On August 31, 2012, Canada imposed further sanctions against Syria under the SEMA.
Tunisia & Egypt	In March of 2011, the Governor in Council made, pursuant to the *Freezing Assets of Corrupt Foreign Officials Act*, the *Freezing Assets of Corrupt Foreign Officials (Tunisia and Egypt) Regulations*. These Regulations gave effect to written requests from Tunisia and Egypt to freeze assets of their former leaders and senior officials or their associates and family members suspected of having misappropriated state funds, or obtained property inappropriately as a result of their office or family, business or personal connections.
Zimbabwe	In September of 2008, the *Special Economic Measures (Zimbabwe) Regulations* (SOR/2008-248) came into force in order to respond to the gravity of the situation in Zimbabwe.

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LEGAL DEVELOPMENTS / DÉVELOPPEMENTS JURIDIQUES

This section is intended to provide only summaries or highlights of selected recent legal developments from around the world. The articles do not constitute specific legal advice on the part of the authors, their law firms, or the Canadian International Lawyer journal. Readers are advised to retain competent local counsel in order to verify the applicability of the relevant legislation for their particular situations.

Cette section présent uniquement des résumés ou des points saillants de faits récents de nature juridique recueillis de par le monde. L'information publiée sous cette rubrique ne doit pas avoir valeur d'avis juridique ou être réputée remplacer les conseils détaillés portant sur une affaire individuelle. Les lecteurs sont invités à obtenir les services d'un conseiller juridique local compétent afin de vérifier si la législation pertinente trouve application.

CANADA

Opening Salvo: Testing Territorial Jurisdiction Under the CFPOA in *R v. Karigar*

Following the creation of its International Anti-corruption unit in 2008, the RCMP has been vigorously investigating Canadians who may be in breach of the *Corruption of Foreign Public Offices Act ("CFPOA" or "Act")*. Of the 34 reported investigations currently underway (most of which have not been made public), Karigar is the first case since 2008 where an individual has been charged (*R.v. Karigar*, 2012 ONSC 2730, *"Karigar")*.

The RCMP charged Nazir Karigar, a Canadian citizen and a former official of a Canadian company, with one count of bribery under section 3 of the CFPOA. He is accused of bribing an Indian government official in connection with a contract for the supply of a security system. The case has yet to be adjudicated on the facts. However, Karigar brought a motion to quash the indictment for want of territorial jurisdiction to try the offence. The motion was dismissed, but the defence raised some interesting points.

Canada was the only OECD country to specifically exclude itself from the requirement to include nationality for jurisdiction in the *Convention on Combating Bribery of Foreign Public Officials in International Business Transactions ("Convention")*. It has been Canada's position that its territorial basis for jurisdiction is effective to combat foreign bribery.

The Canadian test for territorial jurisdiction comes out of the case of *R. v. Libman (R. v. Libman, 1985, CanLII 51 SCC, "Libman")*. In *Libman*, the defendant used a "boiler-room" telemarketing operation in Canada to convince U.S. residents to invest in a worthless Central American mining company. Libman was charged with both fraud and conspiracy to commit fraud. The Court held that for territorial jurisdiction under Canadian criminal law, there must be a "real and substantial link" between the offence and Canada. The Court established a two-stage test to determine whether the crime was committed in Canada: (1) It must take into account all relevant facts that take place in Canada that may legitimately give this country an interest in prosecuting the offence; and (2) it must then consider whether there is anything in those facts that offends international comity. This means that a portion of the illegal activities will have to have been committed in Canada or have a real impact on Canadians.

Anti-corruption practitioners have noted that the lack of nationality jurisdiction is a weakness in the *CFPOA*, and in 2009, the Canadian government introduced Bill C-31 which would have rectified this by amendment. The amendment would have, in certain circumstances, deemed acts or omissions committed outside Canada that constituted offences under the *CFPOA*, to have been committed in Canada. Unfortunately, for reasons unrelated to the *CFPOA*, the Bill died. Practitioners expect that the amendment will be introduced again, before *Libman* is found to be insufficient to find Canadian jurisdiction in a prosecution under the Act.

Karigar's motion to dismiss was based on three points. The first was the *Libman* principles should be restricted to *Criminal Code* offences and was not applicable to the *CFPOA*. On this point, the Court found no support for the proposition, and noted that *Libman* has been applied broadly to many criminal and regulatory offences such as those under the *Competition Act*.

Secondly, Karigar argued that Canada has never fulfilled its obligation under Article 4 of the *Convention* to enact measures to establish its jurisdiction over bribery of a foreign public official. This novel approach submitted that Canada was obliged, when it enacted the *CFPOA* in 1998, to include provisions establishing territorial jurisdiction sufficient to ground the offence charged.

Article 4(1) provides that: "*Each Party shall take such measures as may be necessary to establish its jurisdiction over the bribery of a foreign public official when the offence is committed in whole or in part in its territory."*

The defence argued that the failed attempt in Bill C-31 to introduce nationality jurisdiction in 2009 was Canada's attempt to satisfy the jurisdictional requirement under Article 4. In rejecting this argument, the Court noted that it had, itself, no jurisdiction with respect to the enforcement obligations provided for in an international convention. However, it further noted that the operative phrase in Article 4 is "as may be required", and since the *CFPOA* contains no express jurisdiction clause, the jurisdiction is left to the applicable common law principles, currently being *Libman*.

Finally, the defence argued that *Libman* could not be satisfied on the facts of the *Karigar* case because there was no real and substantial link between Canada and the activities constituting the offence, and that the case, if allowed to proceed, would contravene the requirements of international comity. Unfortunately, such an argument requires the evidentiary record. As the prosecution and the defence were unable to agree on an agreed statement of facts, the Court held that this argument will have to await the close of the Crown's case at trial.

[Contributed by James Klotz, Miller Thomson LLP. E-mail: jmklotz@millerthomson.com]

WTO's Appellate Body Rules that U.S. Country of Origin Labelling Laws Discriminate Against Canadian Cattle and Hogs

The World Trade Organization's ("WTO") Appellate Body recently issued a report on an appeal of the Panel decision in the *US – COOL* case (WT/DS384/AB/R; WT/DS386/AB/R). Canada, together with Mexico, challenged aspects of several US measures that oblige retailers in the US to provide customers with origin information on a range of commodities on the grounds that they were inconsistent with the US's WTO obligations. The decision in *US – COOL* marked the last of three recent rulings from the Appellate Body that chartered new ground in interpreting obligations under the Agreement on Technical Barriers to Trade ("TBT Agreement") and offers insight into WTO disciplines on WTO Members' use of technical regulations generally and country-of-origin-labelling in particular.

Facts

Canada did not challenge WTO Members' general right to enact country of origin labelling ("COOL"). Rather, the focus of the challenge was on elements of the COOL measure that imposed requirements on the labelling of beef and pork in the US that, in Canada's view, necessitated the segregation of imported Canadian cattle and hogs from their US counterparts, which adversely affected the competitive position of Canadian livestock in the US market vis-à-vis US livestock.

Before a WTO panel, Canada and Mexico successfully argued that the COOL measure violated Articles 2.1 and 2.2 of the TBT Agreement because it: (i) accords less favourable treatment to imported livestock than that accorded to domestic livestock; and (ii) does not fulfil the objective of providing consumer information on origin with respect to meat products. On March 23, 2012, the US appealed these findings. Canada and Mexico each filed cross-appeals on certain elements of the legal reasoning employed by the Panel on March 28. The appeals were heard on May 2 and 3 by the Appellate Body in Geneva.

Law

Under WTO law, a "technical regulation" is a measure that: (i) applies to a product; (ii) lays down one or more characteristics of the product; and (iii) imposes mandatory compliance with those product characteristics. The COOL measure was found to be a technical regulation and therefore subject to the requirements of the TBT Agreement.

Article 2.1 of TBT requires that in respect of technical regulations, WTO Members accord the same treatment to products of a WTO Member as that which is accorded to like domestic products – a so-called "national treatment obligation". Article 2.2 of TBT prohibits the use of technical regulations that are more trade-restrictive than necessary to fulfil a legitimate objective. Article III:4 of the General Agreement on Tariffs and Trade ("GATT") is similar to but broader in scope than TBT Article 2.1's national treatment obligation; it requires WTO Members to treat products imported from a WTO Member in the same manner as it treats like domestic products in respect of all laws, regulations and requirements affecting those products' internal sale.

Among other things, the COOL measure mandates that certain retailers affix labels to beef and pork products that convey country of origin information. Upstream producers in these products' supply chains are required to provide information that enables retailers to accurately affix these labels.

The following table outlines the COOL measure's labelling scheme:

Label A – Product of the US	Meat from animals born, raised and slaughtered in the US (Category A)
Label B – Product of the US, Country X,	Meat animals born in Country X and raised and slaughtered in the US (Category B).
Label C – Product of Country X, US	Meat from animals imported into the US for immediate slaughter (Category C).
Label D – Product of Country X	Foreign meat imported into the US (Category D).

Under the COOL measure, only meat products derived from Category A animals are entitled to bear Label A. Labels B and C can be used for: (i) meat products derived exclusively from Category B and C animals; or (ii) meat products resulting from Category B or C animals that are 'commingled' either with category A animals or with each other on a single production day.

The obligation to provide country of origin labelling on meat products is limited to entities with annual agricultural commodity sales of more than $230,000 (US). Food service establishments (such as restaurants and cafeterias) are exempted from the COOL measure's requirements.

Decision

TBT Article 2.1

The Appellate Body found that the conditions of competition in the US market were altered by the COOL measure to the detriment of Canadian livestock. This was due to the incentives the measure created for US producers to segregate livestock according to origin and to process exclusively US-origin livestock. In so finding, the Appellate Body rejected the US argument that only a measure that imposed a legal choice on market actors to distinguish between imported and domestic products to the detriment of the former could ground violations of national treatment obligations.

After applying its recently articulated step of Article 2.1 of the TBT analysis that inquires into whether a detrimental impact on imports stems from a legitimate regulatory distinction, the Appellate Body found the distinctions that the COOL measure made between products were not legitimate, reflected discrimination, and that this discrimination was arbitrary and unjustifiable. The requirement on livestock and meat producers to possess and transmit information on each and every animal and piece of meat was regarded by the Appellate Body as incommensurate with the information provided to consumers under the COOL measure because: (i) labels B and C were confusing and potentially inaccurate; and (ii) the COOL measure's exemptions exclude a large portion of the meat that is consumed in the US from the COOL measure's scope.

TBT Article 2.2

The Appellate Body did not disturb the Panel's finding that the COOL measure is trade-restrictive and conducted its analysis on the basis of an understanding that the Panel had considered the measure's objective to be the provision of consumer information. After observing that the provision of consumer information bears some relation to objectives that governments are entitled to pursue through trade-restrictive measures under other provisions of the WTO Agreements, the Appellate Body upheld the Panel's finding that the objective pursued by the US through the COOL measure was legitimate.

The Panel's decision that the COOL measure was inconsistent with TBT Article 2.2 because it did not fulfil its objective was overturned by the Appellate Body. The Panel had determined that, as a result of its "complex categories of labels" that conveyed "inaccurate and confusing" information to consumers, the COOL measure did not fulfil its objective. Nevertheless, the Appellate Body found that the COOL measure contributes "at least to some degree" to providing consumers with information on origin.

The Appellate Body explained that, in assessing a measure's compliance with TBT Article 2.2, the degree of the measure's contribution to the achievement of its objective must be considered together with its trade-restrictiveness and the gravity of the consequences that would arise from the non-fulfilment of its objective.

Noting that the Panel Report indicated that the COOL measure had a considerable degree of trade-restrictiveness and that the consequences that would arise from non-fulfilment of the measure's objective would not be particularly grave, the Appellate Body examined the alternative measures proposed by Canada to determine if the COOL measure is more trade-restrictive than necessary to fulfil its objective. However, the absence of factual findings in the Panel Report with respect to these alternatives, as well as a lack of sufficient undisputed facts on the record, led

the Appellate Body to conclude that it was unable to complete the analysis under TBT Article 2.2.

Comment

The COOL ruling avoided addressing a dissonance between the GATT and the TBT Agreement that appears to have arisen in recent Appellate Body jurisprudence. In *US – Clove Cigarettes* (WT/DS406/AB/R), the Appellate Body clearly established that TBT measures are also subject to the disciplines of the GATT – including its national treatment obligation in Article III:4.

A measure that violates GATT Article III:4 because it alters the conditions of competition to the detriment of imported products vis-à-vis similar domestic products will be inconsistent with the GATT unless it is justified by one of the GATT's enumerated exceptions.

In *US – Clove Cigarettes*, the Appellate Body explained that a measure that fails the conditions of competition analysis under TBT Article 2.1 can be justified if the negative effect on imports "stems exclusively from a legitimate regulatory distinction" ("LRD"). The parameters of the LRD are unknown, but if they are any broader than the exceptions in the GATT, a measure could be deemed consistent with the TBT Agreement on the grounds that its negative trade effects result from an LRD, but be inconsistent with the GATT because the Article III:4 violation cannot be justified by any of the GATT's exceptions. This would be an anomalous result because the TBT Agreement, which does not contain an explicit exception to the national treatment obligation, would be more deferential to WTO Members' regulatory autonomy than the GATT, which contains numerous exceptions to its national treatment obligation.

[*Contributed by Ian Medcalf, counsel, Department of Justice Canada. E-mail: medcalfi@gmail.com. Any opinions expressed in this article are those of the author alone, and they do not represent the policies or views of the Government of Canada.]*

IRAN

See UNITED STATES

IRAQ / KURDISTAN

An Overview of the NGO Law in Iraq and the Kurdistan Region

Under the New NGO Law ("Law No. 12 of 2010") which is to govern Iraqi operations, the previous CPA Order 45 ("Order") has been overruled. Under Law No. 12 of 2010, an International Non-Governmental Organization ("INGO") must register to carry on the conceived activities in Iraq. The authority for registering and regulating Non-Governmental Organizations ("NGOs") has changed a number of times since CPA Order 45 was issued and is today governed by the NGO Law of 2012. Initially, registration and regulatory authority rested with the Ministry of Planning. Authority was then transferred to a newly created Minister of State for Civil Society Affairs, which executed the function until recently when it was again moved to the General Secretariat of the Cabinet of Ministers. The requirements for registration have not changed significantly since the Order was issued, although there have been differing interpretations of the requirements and a general desire by the regulatory authority to seek more information than was, perhaps, contemplated by the original Order.

Under the Order, a Non-Governmental Organization is defined as an organization or foundation that is organized to undertake one or more of the following as its principal activities: humanitarian assistance and relief projects; human rights advocacy and awareness; community rehabilitation and resettlement; charitable works; educational, health, and cultural activities; conservation; environmental protection; economic reconstruction and development; promotion of democratic practices; development of civil society; promotion of gender equality; or any other non-profit activity that serves the public interest. (Section 1(1)). According to the Order, an INGO, or Foreign NGO as that term is used in the Order, is an NGO that is established with its registered office or headquarters outside Iraq. According to the most recent registration form for NGOs provided by the NGO Office, INGOs must designate their activities from among the following options:

A. Agriculture;
B. Art/Culture;
C. Democracy;
D. Economic development;
E. Education;
F. Environment;
G. The disabled;
H. Human rights;
I. Humanitarian assistance;
J. Media;
K. Children and orphans;
L. Public health/medicine;
M. General services/infrastructure;
N. Shelter/housing;
O. Women's issues; and
P. Youth and sport.

INGOs must not be for-profit, and must not have any government connection. Once registered, an INGO will be subject to regulation and supervision by the NGO Office. The INGO will be exempt from corporate taxes and social security.

In the Kurdistan Region, the Kurdistan Regional Government has issued Regulations No. 1 regarding the registration and regulation of INGOs in the Kurdistan Region. The Regulations are substantially similar to the requirements for the registration of INGOs under the Order and the instructions of the NGO Office. The activities that an INGO or an NGO may pursue are as follows:

A. Humanitarian support;
B. Relief projects;
C. Housing and community reconstruction;
D. Charity;
E. Education;
F. Health;
G. Cultural activities/protection/advocacy;
H. Environmental protection;
I. Reconstruction;
J. Economic development;
K. Democratic process development;
L. Civil Society development;
M. Female equality;
N. Other non-profit activities considered to be useful or to serve a public good.

The agency responsible for registration and regulation of INGOs in Kurdistan is the Kurdistan Ministry of Humanitarian Aid and Cooperation ("MHAC"). An INGO registered with the NGO Office must pursue a separate registration with the MHAC before conducting any activities in the Kurdistan Region (presently Erbil, Dohuk, and Suleimaniyah), and must submit separate reports on its activities to the MHAC.

Non-Governmental Organization

In addition to the INGO process outlined above, Iraq has a separate and analogous process for domestic NGO, which does not have an international affiliation. An Iraqi NGO is defined in the Order as an NGO that is established with its registered office or headquarters inside Iraq (Section 1(2)).

The same conditions as set out above would apply for registration of an NGO, and the same rules regarding prudential and non-prudential requirements would exist. All NGOs and INGOs must commit to, and observe the following:

1. Formally notify the NGO Office when entering into any joint project or other contractual arrangements with a foreign organization or organizations or any international agency before beginning work with them;
2. Not to work, at all, with any foreign organization not registered with the NGO Office;
3. Inform the NGO Office of any administrative changes in the organization within 30 days thereof;
4. Formally notify the NGO Office in the event of a change in the by-laws of the organization within 30 days thereof;
5. Formally notify the NGO Office of any proposed branch openings in Iraq before any such opening;
6. Not to open any international branch of the organization (for domestic NGOs);
7. Submit to the NGO Office detailed and supported reports regarding the activities of the organization on a quarterly basis;
8. Not to be supported (financially or morally) by any political agency or entity;
9. To remain non-political, non-governmental, and non-profit, and not to discriminate on the basis of ethnicity, religion, or nationality.

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ITALY

Infringer Ordered to Buy Back Infringing Products from Store

By means of a ruling issued on June 27, 2012 in the summary proceedings specifically provided in Italy in Intellectual Property ("IP") matters, the IP Specialized Division of the Court of Turin ordered the infringers of three design registrations owned by Blufin s.p.a., the owner of the famous *haute couture* trademarks Blumarine and Blugirl, to buy back the counterfeiting products from the shops, even at their market price, and to withdraw the relevant advertising material. This is the first time in Italy that the order of withdrawal is given this extension, which is consistent with the provision of Directive n. 2004/48/EC on the judicial defense of IP rights (the so-called Enforcement Directive).

Actually in Italy not only does Article 124 Italian Industrial

Property Code ("IIPC") provide for an "order to withdraw the (infringing) products from the market issued against the owners of said products or those who, at any rate, have them at their disposal" as a corrective measure to be issued at the end of the proceedings on the merits, but furthermore Article 131 IIPC provides for such an order to be issued on a "provisional" basis, too, in the PI/seizure proceedings. Both these rules were introduced in Italy by Legislative Decree 16 March 2006, no. 140, implementing EC Directive 2004/42.

However both Article 124 and Article 131 IIPC provide for the order to withdraw the products from the market to be issued only "against the owners of said products or those who, at any rate, have them at their disposal."

According to the Italian scholars and case law, these rules oblige the infringer to take action to recover and remove from the channels of commerce also infringing goods distributed "for sale on account", i.e. by way of a contract of sale or return, or such like. See in particular Court of Milan, January 16, 2009, which upheld as a final ruling an order to definitively withdraw from the market the infringing product (a calendar) issued in preliminary proceedings also against an intermediary who was not held guilty of infringement.

Instead it was disputed whether the order may apply also to products that have been definitively sold to independent resellers. The order now issued clearly construe the rule in its wider sense, which is consistent with the underlying rationale of these measures, i.e. that of removing all the consequences of the infringing activity and preventing the same from bringing further effects on the market. This way the Italian jurisdiction took another important step forward in defense of IP rights.

The order issued by the Court of Turin is particularly important also for its grounds regarding the protection of design patents, especially if we consider that in the field of fashion – where the products protected by the design patents at issue belong – it is not yet widely used to protect the appearance of clothes, if not against identical imitations.

In fact, protection has been granted on the basis of three patent designs covering three unique floral designs for items of clothing against low-cost non-identical imitations manufactured by a company based in Naples, which carried out a particularly harmful infringing activity, supported by a pervasive and intense advertising campaign all over the Italian peninsula, through many large billboards and advertisements appearing in dozens of the most widely spread women's magazines, thus creating serious damages to Blufin's image.

The Judge of the Court of Turin, Dr. Ratti, fully recognized the innovative nature of the Blufin clothing designs, which, as she wrote, "differ significantly also for the purpose of 'general impression of the whole' by the many previous designs found by the infringer, among which it was not possible to find any clothes capable of challenging the creativity and the originality of its designs" -- activity called by the Court "copying effect."

Even if the copy products were not identical, the Court held them infringing, since they traced almost all the dominant elements which give individual character to the Blufin's floral design on items of clothing, which led the Judge to exclude also the infringer's argument about an alleged, but unlikely, "creative coincidence." Therefore also in this respect the decision is fully consistent with the indications coming from the EU Directive and Regulation on design protection and the construction thereof commonly accepted at the European level.

[By Cesare Galli, IP Law Galli (Milan). Reprinted with the kind permission of the author, IP Law Galli and the International Law Office. E-mail: galli.mi@iplawgalli.it. This article is the original of one that was later revised and published on www.internationallawoffice.com – the Official Online Media Partner to the IBA, an International Online Media Partner to the ACC and the European Online Media Partner to ECLA. Register for a free subscription at www.internationallawoffice.com/subscriptions]

JERSEY

Jersey Joint Venture Vehicles

Whilst the Mergers & Acquisitions ("M&A") pipeline remains relatively strong, getting deals to completion is challenging due to the tightening of available credit and uncertainty with asset valuations. In this climate, Public Limited Companies ("PLCs"), other large corporates and Private Equity ("PE") houses are looking at alternative and more creative structures to gain access to deals that might not be available via traditional M&A. The use of a Jersey Joint Venture ("JV") vehicle is one such alternative structure which can be used in a try-before-you-buy sense and as a precursor to traditional M&A activity in the future.

Structural Neutrality

Rather than using the home jurisdiction of one of the parties, or the jurisdiction where the JVs business is to be located,

seeking a neutral venue to provide a level playing field for all parties is becoming more important and this is where going offshore provides a feasible solution.

The primary motivation for choosing an offshore jurisdiction is often to take advantage of favourable tax regimes that do not levy a corporation tax on profits of the JV vehicle. The impact of this is that a tax neutral position can be maintained for all participants.

Benefits of Using a Jersey JV vehicle

There are both commercial and structural benefits to using a Jersey JV vehicle which include:

- Jersey company law being based on English company law but with greater flexibility (for example, in relation to capital extraction etc);
- An extremely favourable corporate tax regime;
- No stamp duty on the transfer of shares in Jersey companies;
- Jersey's close proximity to and same time zone as London makes closing transactions simpler;
- Fast-track formation of companies (same day if required);
- Being any easy way for two or more parties to pursue a partnership or strategic alliance;
- Allowing investors to gain a better understanding of the assets or regions involved (before one of the parties decides to go at it alone);
- Getting exposure to new and emerging markets especially where, for example, restrictive foreign ownership regulations apply; and
- Going some way toward addressing the issue of valuation gap between traditional M&A players where markets are either (or both) unpredictable or volatile and uncertain because of external factors such as – the European economy, for example.

Corporate Flexibility

One of the key advantages of using a Jersey holding company is the flexibility of Jersey company law in relation to returns to investors - whether by means of dividend, redemption of share capital or share buy-back. In particular, monies payable on the redemption of redeemable shares or on the buy back of shares by a Jersey company, may be funded from any source - including capital. A Jersey company may also make a distribution from a wide range of sources, not merely from distributable profits.

A Jersey holding company also facilitates a tax efficient exit through stamp duty savings and is also suitable for an initial public offering ("IPO").

Tax Regime

A zero rate of income tax applies to virtually all Jersey companies.

However, if required, it is possible to ensure that a Jersey company is tax resident in another jurisdiction provided that:

- It is centrally managed and controlled in another jurisdiction outside Jersey;
- It is tax resident in that other jurisdiction; and
- The highest rate of corporation tax in that other jurisdiction is 20% or above.

No stamp duty is payable on the transfer of shares in a Jersey company and there is no corporation or capital gains tax in Jersey. Jersey levies no annual taxes or charges by reference to a company's authorised or issued share capital. Although Jersey has recently introduced a goods and services tax at a rate of 3%, companies beneficially owned outside Jersey which do not supply goods or services in Jersey will generally qualify for "international service entity" status - effectively bringing them outside the scope of the goods and services tax regime provided that a fee of £100 is paid each year.

Returns to Investors

It is possible to structure returns to investors by way of capital returns by means of redemption or buy back or cash distributions (or a combination of these methods). Jersey company law is very flexible on the sources of funding for redemption of share capital and in relation to requirements for distributions.

Redemption and Buy Back of Shares

Monies payable on the redemption of redeemable shares or on the buy back of shares by a Jersey company may be funded from any source - including capital.

The directors responsible for authorising the redemption or buy back payment will be required to make a statement that they have formed the opinion that:

- Immediately following the date on which the payment is to be made, the company will be able to discharge its liabilities as they fall due; and
- Having regard to -
  - The prospects of the company and to the intentions of the directors with respect to the management of the company's business, and

- The amount and character of the financial resources that will, in their view, be available to the company,

The company will be able to –

- Continue to carry on business, and
- Discharge its liabilities as they fall due

for a period of 12 months after the date of such payment (or, if sooner, a solvent winding up of the company).

Therefore, provided that the solvency statement can be made, there is considerable flexibility in funding the redemption or share buy back.

Distributions

A Jersey company may make a distribution from a wide range of sources, not merely from distributable profits. Therefore, distributions may be made from capital without a need to obtain Court approval for a reduction of capital (as was previously the case).

A distribution may be debited from any account of the company (including the share premium account and the stated capital account) other than the capital redemption reserve or the nominal capital account. The fact that distributions may be made from the stated capital account of a no par value company but not the nominal share capital of a par value company may lead to an increased use of no par value companies in the future.

A distribution may only be made if the directors authorising the distribution make a solvency statement in the form referred to above.

Financial Assistance

Jersey company law historically prohibited a company giving financial assistance in respect of the acquisition of its own shares. This prohibition has now been removed and the amendments make clear that any previous common law prohibition on financial assistance is not renewed by virtue of the removal of the statutory prohibition.

Debt Listing

An acquisition often involves the issue of loan notes in connection with the acquisition financing. The Channel Islands Stock Exchange ("CISX") was designated by the UK Inland Revenue as a recognised stock exchange under Section 841 of the UK Income and Corporation Taxes Act 1988 in 2002. This designation means that qualified debt securities listed on the CISX are eligible for the "Quoted Eurobond Exemption" which allows an issuer within the UK tax net to make payments of interest on the listed securities gross without deduction for tax.

Ogier Corporate Finance Limited ("OCFL") is a full listing member of the CISX and is able to act as sponsor for listing purposes, having extensive expertise in this area.

OCFL sponsored over 100 listings in 2011 and in 2008 listed debt securities issued by Best Buy Distributions Limited which was the 3000th listing on the CISX.

Further details of the services provided by OCFL are available on request.

Exit by IPO

Jersey incorporated companies are increasingly being used for listing on the Alternative Investment Market of the London Stock Exchange and also on the main board of the London Stock Exchange. A separate briefing on the advantages of using a Jersey company for a listing is available on request.

Other Jurisdictions

Ogier also advises on BVI, Cayman and Guernsey law and is, therefore, able to advise on more complex cross-border transactions involving those jurisdictions.

Relevant Examples of Jersey JV Vehicles:

- Hutchison Ports Holdings Limited, a subsidiary of Hutchison Whampoa in relation to the establishment of a Jersey holding structure and joint venture vehicle for a major UK port.
- Thomas Cook Group plc and The Co-operative Group on the Jersey-incorporated joint venture company to be used for the proposed merger of the high street travel and foreign exchange businesses of each of these UK household names.
- PetroChina and British chemicals group INEOS formed INEOS Investments (Jersey) Limited, a Jersey joint venture company, in relation to the refining operations in Grangemouth (Scotland) and Lavéra (France). PetroChina paid US$ 1.015 billion cash for the shares in the joint ventures.
- Lanxess and INEOS together established INEOS ABS (Jersey) Limited, Jersey, to which the Lanxess' Lustran Polymers was transferred.
- A number of Jersey joint venture/co-investment style vehicles used for acquisition and related purposes include:
  - Heineken and Carlsberg, on the recommended cash offer (GBP 7.8bn, EUR 10.5bn, USD 15.5bn) by

Sunrise Acquisitions Limited for UK brewer Scottish & Newcastle; and

- JPMorgan Asset Management and Australia's Colonial First State on the successful by Northwest Electricity Networks (Jersey) Limited bid for United Utilities Electricity.

- Segro and Moorfield Real Estate Fund II established a Jersey joint venture vehicle to acquire the UK Logistics Fund for £314.7 million from Hermes Real Estate, Legal & General and LaSalle Investment.

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RUSSIA

Supreme *Arbitrazh* Court Rejects Alternative (Asymmetrical) Arbitral Clauses

Introduction

The Supreme *Arbitrazh* Court has issued Resolution 1831/12 in a case regarding the claim of ZAO Russkaya Telephonnaya Companiya ("RTC") against OOO Sony Ericsson Mobile Communications Rus.

The resolution reached a conclusion on the invalidity of alternative (asymmetrical) arbitral clauses – that is, agreements under which one party is entitled to refer a dispute to arbitration or to a state court, while the other party has no such alternative. Such clauses have become common in share sale and purchase agreements, immovable property leases and aircraft finance leases.

The resolution will have a significant impact on practice, despite the fact that it does not completely resolve the issue of the validity of arbitration selection as a means of dispute resolution in alternative arbitral clauses.

Facts

The agreement between RTC and Sony Ericsson contained an alternative arbitral clause entitling Sony Ericsson to submit its claim to either the International Chamber of Commerce ("ICC") or the courts. RTC was entitled to submit its claim only to the ICC.

Despite this provision, RTC made a claim before the courts. Sony Ericsson requested the court, pursuant to Article 148 of the *Arbitrazh* Procedure Code, to decline to consider RTC's claim due to an arbitral clause agreed by the parties.

The court declined to consider RTC's claim. The courts at appellate and cassational instances upheld the conclusions of the first instance court.

Decision

The Supreme *Arbitrazh* Court ruled that the case should be sent back for reconsideration. It stated that an alternative arbitral clause entitles only one party to select the means of dispute resolution, thus creating a more favourable position for such party, upsetting the balance of the parties' interests and violating the principle of equal rights.

In justification of its position, the court referred to the general principles of law (equal rights) and to decisions of the European Court of Human Rights under the European Convention for the Protection of Human Rights and Fundamental Freedoms 1950.

Therefore, the court concluded that:

> An agreement on dispute resolution may not entitle only one of the parties (seller) of a contract to refer [a dispute] to a competent state court and deprive the other party (buyer) of such right. If such agreement is concluded, it is invalid as it violates the balance of the parties' rights. Therefore, a party whose right has been infringed by such agreement on dispute resolution may also refer to a competent state court, exercising the guaranteed right to relief in court on equal terms to those applicable to its counterparty.

Comment

The resolution will have a significant impact on practice. It was issued in the context of the negative attitude of the Supreme *Arbitrazh* Court to foreign arbitration tribunals, and is intended to shift disputes involving Russian and foreign entities from arbitration tribunals to Russian courts. Anton Ivanov, chairman of the Supreme *Arbitrazh* Court, has repeatedly declared this intention in the past.

The resolution results in the following conclusions:

- An alternative arbitral clause is invalid insofar as the right to refer to the court is granted to only one party. The party which has not been granted such a right is entitled to refer a dispute to a Russian court.
- The validity of an arbitral clause selecting the arbitration venue (e.g. ICC) is less clear. On the one hand, the resolution did not analyse the validity of the

agreement to select the ICC. Nevertheless, if the court had deemed the selection of the ICC to be valid, it would have had to uphold the conclusions of the lower courts (which it did not).

- The resolution raises questions as to the enforceability of foreign arbitration award when there is an asymetrical arbitral clause. If a foreign arbitral award is passed pursuant to such arbitral clause, the court may deem the arbitral clause invalid and may refuse to recognise and enforce that award.
- There is a risk that Russian courts may initiate proceedings in disputes under contracts including alternative arbitral clauses, thus depriving arbitral clauses of protection.

It is worth revising all agreements which include such alternative arbitral clauses, particularly if proceedings have already been commenced in foreign arbitration tribunals.

[By Yaroslav Moshennikov and Veronika Guseva, DLA Piper (Moscow). Reprinted with the kind permission of the authors, DLA Piper and the International Law Office. E-mail: yaroslav.moshennikov@dlapiper.com, veronika.guseva@dlapiper.com. This article was originally edited by, and first published on, www.internationallawoffice.com – the Official Online Media Partner to the IBA, an International Online Media Partner to the ACC and the European Online Media Partner to ECLA. Register for a free subscription at www.internationallawoffice.com/subscriptions]

SPAIN

Court Rules on Action to Set Aside Arbitral Award

Foreword

On June 22, 2011, the Barcelona Court of Appeals issued a ruling in a case concerning the action to set aside an arbitral award issued by the Barcelona Court of Arbitration. The arguments of the annulment action were based on the Spanish *Insolvency Act* and the Spanish *Civil Procedure Law*.

Facts

On July 19, 2007, a construction works agreement was signed by the company Marina Badalona, S.A. ("Marina") and the Temporary Joint Venture ("TJV") formed by Tiferca, S.A. ("Tiferca") and Tableros y Puentes, S.A. ("Tapusa"). (The TJV is similar to a conventional joint venture, and is known in Spain as a *unión temporal de empresas*" ("UTE")).

According to Marina, the TJV did not fulfil its construction obligations on time and Marina therefore initiated arbitration proceedings, requesting the termination of the contract, despite its already having been partially fulfilled. Marina decided to only sue Tapusa, given that it was jointly and severally liable for all the obligations of the contract, and Tiferca was involved in insolvency proceedings at the time. Former Article 52 of the *Insolvency Act*, (which has recently been amended, stated that arbitration agreements with a debtor who has been declared insolvent shall be without value or effect during insolvency proceedings.

However, Tiferca requested to participate in the arbitration proceedings as an interested party, in accordance with Article 13 of the Spanish *Civil Procedure Law*. After taking this into consideration, Tapusa challenged the arbitral proceeding, arguing that Tiferca's participation was incompatible with former Article 52 of the *Insolvency Act*. Meanwhile, Marina confirmed their interest in only suing Tapusa. The arbitrator finally upheld Marina's position that Tiferca should not participate in the proceedings as an interested party, and pointed out that the fact that one of the TJV former members was involved in insolvency proceedings would not affect the TJV`s arbitration agreement, as long as this member, Tiferca, was not party to the arbitration proceedings.

The award of July 6, 2010, declared the termination of the contract and partially accepted Tapusa's counterclaim regarding certain amounts owed to the TJV. Nevertheless, Marina decided to request the annulment of the award and argued that it might not have legal effects, as it did not refer to all the interested parties involved. Although the award recognises that a certain amount of money is owed to the TJV because the contract was partially fulfilled, in the end it was declared that Marina was not obliged to pay the TJV, as they were never party to the procedure.

Marina's reasons for the challenge are that the effects of the award did not extend to the TJV or its other former member (Tiferca), as a result of the joint and several liability of these types of unions. However, the ruling declares that Marina had already recognised this application through its actions, by initiating the arbitration proceedings.

The Amendment of Article 52 of the *Insolvency Act*

As we have seen, former Article 52 of the *Insolvency Act* stated that arbitration agreements entered into by a debtor declared insolvent should be without value or effect during insolvency proceedings.

It would appear that Marina only sued Tapusa in order to

avoid the application of the aforementioned article (*i.e.* the arbitration agreement would have had no value or effect).

However, Article 52 of the *Insolvency Act* was amended by Law 11/2011 (amending the Arbitration Law). Since June 10, 2011, Article 52 of the *Insolvency Act* states that the initiation of the insolvency proceedings does not in itself affect any mediation or arbitration agreements endorsed by the insolvent party. (However, if the court understands that such agreements or arrangements could undermine the insolvency procedure, it may order their annulment.) Therefore, companies involved in insolvency proceedings can be a party to arbitration proceedings.

Consequently, if Marina had initiated the Arbitration Proceedings after the amendment of the *Insolvency Act*, they would probably not have excluded Tiferca from the proceedings (logically, if more companies are sued, there is a higher likelihood of recovering the amounts owed).

The Joint and Several Liability of the Members of a TJV

As we have seen, both Tapusa and Tiferca were part of a TJV. According to Article 8.e.8 of the Spanish Temporary Joint Ventures Law (Law 18/1982, of May 26, 1982) all members of a TJV are jointly and severally liable *vis-à-vis* third parties.

It appears that Marina only sued Tapusa in order to avoid the application of Article 52. If they had also sued Tiferca, the arbitration agreement would have been without effect and the Judge of the insolvency proceedings would be competent to hear the claim.

Moreover, the arbitrators considered that the claim was properly addressed against Tapusa, but they also decided that, without Tiferca, Tapusa was not entitled to claim the amount that Marina should have to pay to the TJV. Only the TJV could claim for the amount owed.

As a result, despite the fact that the arbitral award declared that a certain amount of money was due to the TJV, it did not order Marina to pay it.

The Barcelona Court of Appeals Applied the Estoppel Appropriately

As we have seen, once the arbitral award partially accepted Tapusa's counterclaim, Marina filed for the annulment of the arbitral award before the Barcelona Court of Appeals.

The Barcelona Court of Appeals considered that Marina could not ask for the annulment of the arbitral award by arguing that the arbitral proceeding should have included Tiferca, given that throughout the arbitral proceedings, Marina challenged Tiferca's joinder.

The Barcelona Court of Appeals considered that Marina could not contradict their own acts. We consider this understanding of the estoppel doctrine in a procedural sense to be correct.

Conclusions

Although the arbitrators deemed it necessary for Marina to pay a certain amount of money to the TJV, Marina was not ordered to pay it because the TJV had not claimed it. Nevertheless, in light of the circumstances, the ruling of the Barcelona Court of Appeals and the arbitral award were both reasonable.

However, if the amendment of Article 52 of the *Insolvency Act* had been in force, Marina would probably not have excluded Tiferca from the proceedings. All parties could have been joined in one single arbitration, with the result that a single decision would have definitively settled the dispute. We believe that such an amendment to Article 52 of the *Insolvency Act* is a good decision by the Spanish legislator.

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UNITED KINGDOM

Three Months to Go: Are You Ready for Jackson?

In November 2008, Lord Justice Jackson was appointed to lead a wide-ranging review into the costs of civil litigation. Four years on, and some of the recommendations from the Jackson review have already been implemented. However, the majority of the changes will come into force in April 2013. It is no exaggeration to say that this will be the most significant shake-up of the civil justice system since the implementation of the Woolf reforms in 1999. With three months to go, we outline the key changes, and what they mean for lawyers and their clients.

How Will the Changes be Made?

The changes in law required by the Jackson review are contained in the *Legal Aid, Sentencing and Punishment of Offenders Act 2012* ("LASPO"), which was given Royal Assent in May 2012.

The changes to the Civil Procedures Rules required by the Jackson review are largely complete. They are expected to be released in January 2013, prior to implementation in April 2013.

What Key Changes are Already Implemented?

- **Costs management pilots.**

  The Jackson review recommended active costs management by the courts, which would involve the parties preparing costs budgets (more detailed than the current costs estimates). The judge would review these budgets and give an indication of the extent to which they were approved. Cost assessment at the end of the case would then be carried out by reference to the initial budget. Pilot schemes are currently underway for all cases in the Technology and Construction Court and Mercantile Court, and for defamation cases in the Royal Courts of Justice and the Manchester District Registry. These will continue until the end of March 2013.

- **"Hot tubbing" pilot.**

  Hot tubbing is the practice, developed in the Australian courts and used in some international arbitration, of experts giving evidence concurrently. The experts are sworn in and the court effectively chairs a discussion between them, with questions from counsel as and when allowed by the judge. This is thought to offer potential time and cost savings over the current system of sequential evidence. The Jackson review recommended its use in all cases where the parties agree to it. A pilot has been in place in the Manchester Technology and Construction Court and Mercantile Court since June 2010, albeit with relatively low take-up.

- **Docketing pilot.**

  The Jackson review recommended expanding the availability of docketing - the process by which one judge controls a case from beginning to end - as a means to encourage judges to take a more hands-on approach to case management. Docketing has been piloted at the Leeds County Court and Registry (although it is already available to a variable extent in other courts). The results, unsurprisingly, were positive, with an evaluation concluding that docketing "brought advantages using existing resources and without major reorganisation". However, widespread availability of docketing is unlikely until some time beyond April 2013.

- **Enabling provisions of LASPO.**

  Some sections of LASPO have already been brought into force, which will enable appropriate changes to be made to the CPR in time for the full roll-out of the Jackson reforms in April 2013.

What Key Changes Will be Implemented in April 2013?

- **Success fees in conditional fee agreements ("CFAs") no longer recoverable.**

  A success fee is a fee, calculated by reference to the lawyer's standard fees, which the client agrees to pay to a lawyer in the event of success. For example, a lawyer may charge an uplift of 100% on his fees if he wins, and charge nothing if he loses ("no win, no fee"). The Jackson review identified a number of disadvantages to this type of deal including unfairness to defendants. In accordance with the recommendations of the review, success fees will no longer be recoverable from losing defendants. This means that the claimant will have to pay its lawyer's success fee out of its damages, which in turn is likely to reduce the use of CFAs. As this change may reduce access to justice for impecunious claimants, particularly in personal injury cases, the Jackson review proposed various measures to mitigate these concerns, such as a modest increase in the level of damages awarded in personal injury cases. However the most significant measure is the introduction of alternative funding schemes such as DBAs (see below).

- **After the event ("ATE") insurance premiums no longer recoverable.**

  ATE insurance allows a party to insure against the risk of losing the case and having to pay the other side's costs. Premiums may be deferred and contingent, i.e. the party only has to pay the premium if it wins, at which point it is recoverable from the other side. ATE policies are often used hand-in-hand with CFAs to enable a claimant to litigate at zero or negligible cost or risk. Again, the Jackson review concludes that this is unfair to defendants. As such, parties who succeed at trial will no longer be able to recover their ATE premium from the losing party. This is likely to reduce the use of ATE policies.

- **Introduction of contingency fees.**

  A contingency fee is an agreed fee payable to a lawyer on success, calculated as a percentage of the sum

recovered. Contingency fees are currently prohibited in most forms of court proceedings in the UK as they are thought to carry a risk that the lawyer, whose interests are tied up the outcome of the case, may fail to give impartial advice to the client. However the Jackson review recommends the introduction of contingency fees based on the Ontario model (sometimes referred to as "Damages Based Agreements" or "DBAs") which are designed to mitigate this risk, alongside certain other procedural safeguards to be introduced. Essentially this allows for contingency fees, but with the proviso that recovery from the losing party is limited to the lawyer's normal costs. This means that a claimant would have to pay any contingency fee to the lawyer out of its damages. From a claimant's perspective, similar arrangements are already on offer through third party litigation funders, who will typically require a fixed percentage of any recovery in return for funding legal costs. The new development will mean that lawyers will be able to offer these arrangements themselves, rather than referring clients to third party funders.

- **Part 36 "plus".**

  The Jackson review recommended the introduction of an additional sanction (10% of the value of the claim) to be paid by defendants who refuse a reasonable Part 36 offer from the claimant and then fail to beat it at trial. Section 55 of LASPO is now in force, enabling appropriate rules to be made. An amendment will therefore be made to CPR 36.14(3) to implement this recommendation. Many litigation lawyers, and clients with regular litigation, will have experience of cases where the parties' opposing offers stalled within 10% of each other. This change should encourage settlement of such cases.

- **Disclosure "menu" for large claims.**

  The Jackson review concluded that the default requirement of standard disclosure should be dropped in favour of a menu of disclosure options which may be more or less onerous than standard disclosure so that a choice can be made depending on the requirements of the case. As such, a new CPR 31.5A is to be introduced which will provide a number of disclosure options from which the court and the parties can choose. This is a long overdue change which will bring court procedure more into line with the practice in arbitrations, where parties often agree speedier, cheaper mechanisms for disclosure.

- **Costs management.**

  Following the pilot projects outlined above, a standard costs management procedure will be introduced into the CPR. This will apply to all multi-track cases commenced on or after April 1, 2013 in a county court, the Chancery Division, or the Queen's Bench Division (except the Admiralty and Commercial Courts). Additionally, the courts will have the power to order a case either in or out of the system. This will be a major procedural change and all litigation practitioners will need to be familiar with the new rules prior to their implementation. The extent to which the new regime will benefit litigants by reducing costs will largely depend upon how it is implemented in practice by the judiciary.

- **Hot tubbing.**

  If the results of the hot tubbing pilot are positive there is expected to be an amendment to CPR 35 to provide for use of that system in appropriate cases. However, it is not certain at this stage that this will be introduced in April 2013.

Conclusions

The centrepiece of the Jackson reforms lies in the abolition of recovery of CFA success fees and ATE premiums, and the introduction of DBAs. Under a CFA, a lawyer's maximum uplift is limited to 100% of fees. Under a DBA, the lawyer may be paid a percentage of damages and payment is unlimited (albeit in personal injury cases, fees will be capped at 25% of damages). A law firm, or counsel, will only need to have one success in a claim worth hundreds of millions, or billions, to make profits which are out of all comparison to existing business. This may have major consequences for the legal profession.

Furthermore, the economics of funding cases will change. Cases are unlikely to be funded under DBAs where the potential damages, and therefore the pot available to pay the lawyer, are low. At the moment these cases are likely to be perfectly viable under CFAs, as the legal costs and success fee can be recovered from the other side, leaving damages largely intact. Once recoverability of success fees is abolished, this no longer works. Hence, an impecunious claimant may be unable to bring such claims in future.

The other key Jackson changes to Part 36, disclosure, costs management and so on, will require time to bed in before their impact can be fully assessed. However, as with Woolf, it may be that the changes establish a culture which then generates a momentum of its own.

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UNITED STATES

Foreign Subsidiaries of US Corporations Now Fully Subject to Iranian Sanctions

On October 9, 2012, the President issued a new Executive Order, EO 13628, "Authorizing the Implementation of Certain Sanctions Set Forth in the *Iran Threat Reduction and Syria Human Rights Act of 2012* and Additional Sanctions with Respect to Iran." This EO was issued to implement certain provisions of the *Iran Threat Reduction and Syria Human Rights Act of 2012* (Public Law 112-158) ("ITRSHRA"), including those extending certain prohibitions on dealings with Iran to non-US companies owned or controlled by US persons. Simultaneously, OFAC issued three new Frequently Asked Questions to clarify certain aspects of the new rules.

ITRSHRA was enacted on August 10, 2012. Among other things, the statute prohibits any non-US entity owned or controlled by a US person from knowingly engaging in any transaction with the Government of Iran ("GOI") or with a person subject to the GOI's jurisdiction, if US law prohibits US persons from engaging in the same transaction. Under the EO, "knowingly" with respect to conduct, a circumstance, or a result, means that "a person has actual knowledge, or should have known, of the conduct, the circumstance, or the result." ITRSHRA required the President to prohibit such transactions within 60 days of its enactment, and that prohibition has now been implemented through this EO.

Prior to the enactment of the ITRSHRA, independent foreign subsidiaries of US persons were generally permitted to conduct transactions involving Iran so long as no US persons or US-origin goods or services were involved in the transaction. Because European, Asian and Middle Eastern companies have generally been permitted to do business with Iranian companies in the past, various complex business arrangements exist and need to be addressed in time for companies to comply with the February 6, 2013 deadline.

The EO specifies that if a transaction involving Iran is exempt from the existing prohibitions, or is authorized by a general license if engaged in by a US person, it would not be prohibited for a foreign subsidiary to engage in the transaction provided that it satisfies all the conditions and requirements of the exemption or general license. It also appears that foreign subsidiaries will be able to apply for licenses under the *Trade Sanctions Reform Act* ("TSRA") for the export of agricultural commodities, medicines, and medical devices to Iran. Presumably, other licenses that can be obtained by US persons under favourable licensing policies of OFAC will also be available to foreign subsidiaries. On the other hand, if a US company has already received a specific license to conduct a transaction, and the foreign subsidiary is not referenced in the license, then it may be necessary to amend the license or request a second license in order to complete the transaction with the involvement of the foreign subsidiary.

The EO contains several definitions which help to clarify the new restrictions, but not all important terms are defined and the definitions do not answer critical questions. For instance, there is not a complete definition for the term "entity owned or controlled by a United States person." Under Section 218(a)(2) of the ITRSHRA, foreign subsidiaries with greater than 50% ownership by a US parent (or majority board control) are clearly intended to be covered, but the status of other affiliated entities which may be controlled, but not owned, by a US person, is less certain. These entities are covered if a US company "otherwise control[s] the actions, policies, or personnel decisions of the entity." For example, if a UK parent has a subsidiary in the United States which controls many of the activities of an affiliate in Europe or Asia, the EO does not specify the degree of control necessary to subject the affiliate to the prohibitions found in the EO.

The term "subject to the jurisdiction of the Government of Iran" is defined in the EO to include any "person organized under the laws of Iran or any jurisdiction within Iran, ordinarily resident in Iran, or in Iran, or owned or controlled by any of the foregoing." However, the terms "ordinarily resident in Iran" and "controlled" are not explicitly defined. Prior to the enactment of the ITRSHRA, foreign subsidiaries of US companies were permitted in certain circumstances to have Iranian nationals on their staff. Now, if an Iranian national is working in Germany for a subsidiary of a US company, and the Iranian national does not have permanent residency status in Germany, the new EO could be interpreted to require that the German subsidiary terminate the employment of the Iranian national since the Iranian national might not be considered "ordinarily resident" in Germany with only a temporary visa. Furthermore, if the German subsidiary of a US person has a long-standing business relationship with a UAE/Iranian joint venture that is 51% owned by the UAE entity, but is controlled in fact by the Iranian partner, the new EO may require that the German subsidiary terminate its business relationship with the joint venture since the joint venture is controlled by the Iranian entity, even though the

entity is majority owned by the UAE company. In both of these examples, the German company could apply for a license from OFAC. TSRA license requests related to the export of agricultural commodities, medicines, or medical devices are likely to be favourably considered, but OFAC's licensing policy with respect to non-TSRA activity is less likely to be favourable. In addition, it is possible that license applications submitted to OFAC may not receive a response prior to the February 6, 2013 deadline.

The EO does allow US entities to avoid liability by distancing themselves from their foreign affiliates engaged in Iran-related activity within a certain time period following the enactment of the EO; however, this provision could benefit from further clarification. Specifically, Section 4(c) of the EO provides that civil penalties will not apply "if the United States person that owns or controls the entity divests or terminates its business with the entity not later than February 6, 2013." While it would seem that the intent of the EO is to pressure US companies to require their foreign subsidiaries to terminate all business with Iran, the wording of this section is unclear. It appears that the EO is requiring the US person to divest or terminate its business with its own foreign subsidiary. While divestiture can be accomplished (though the US person would be given very little time to complete the sale), the termination of business with one's own subsidiary could be more difficult and raises additional practical questions. For example, what if the parent terminates its business (e.g., the supply of parts or components) with its subsidiary, and the parent merely receives revenues from the subsidiary? In that case, the new EO has accomplished little since the foreign subsidiary was already required by US law to operate independently of the US parent with respect to its Iran-related business. The administration should clarify this requirement in the coming weeks so companies have time to implement the necessary changes. If the US parent does not have time to implement these changes, it could potentially request a license that would allow some additional time, but OFAC may not grant such a license or even act upon the request prior to the February deadline.

Finally, it appears that the EO does not permit grandfathering of existing contracts. Under Section 4(d) of the EO, the prohibitions of Section 4 apply "notwithstanding any contract entered into… prior to the date of this order." As such, if a foreign subsidiary did not negotiate early termination clauses based on changes to applicable export control and sanctions laws, the subsidiary risks facing either commercial penalties for early termination of agreements, or civil penalties imposed on their US parent. Even if a company does not have a foreign subsidiary which is doing business with Iran, this new EO should serve as a reminder of the importance of contractual protections relating to changes in export control and economic sanctions laws.

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