CANADA

In 1996, the U.S. trade deficit with Canada was $23.9 billion, an increase of $5.8 billion from the U.S. trade deficit of $18.2 billion in 1995. U.S. merchandise exports to Canada were $132.6 billion, an increase of $5.6 billion (4.4 percent) from the level of U.S. exports to Canada in 1995. Canada continued to be the United States' single largest export market in 1996. U.S. imports from Canada were $156.5 billion in 1996, an increase of $11.4 billion (7.9 percent) from the level of imports in 1995.

The United States continues to be by far the largest foreign direct investor in Canada, which results in high dividend payments by Canadian subsidiaries to their U.S. parents. The stock of U.S. foreign direct investment (FDI) in Canada in 1995 was $81.4 billion, an increase of 8.5 percent from the level of U.S. FDI in 1994. U.S. FDI in Canada is concentrated largely in the manufacturing, financial, and petroleum sectors. In addition, Canada's large external debt, much of which is held by U.S. residents, gives rise to an outward flow of debt service payments to the United States.

The U.S.-Canada Free Trade Agreement and the North American Free Trade Agreement

On January 1, 1989, the United States and Canada began to implement the U.S.-Canada Free Trade Agreement (CFTA), designed to eliminate over a period of ten years virtually all tariff and non-tariff barriers to trade between the two countries. The CFTA was suspended on January 1, 1994, with the inauguration of the North American Free Trade Agreement (NAFTA), which expands the free trade area to Mexico. The NAFTA extends the CFTA to important sectors such as trade in services, investment, and government procurement. The CFTA's bilateral phase-out of tariffs is continuing and will be complete on January 1, 1998.

IMPORT POLICIES

Beer

The U.S. Government successfully challenged Canadian beer practices before the GATT in 1991. A series of negotiations led to the U.S.-Canada Memorandum of Understanding (MOU) on Provincial Beer Marketing Practices in 1993 and an annex to the MOU in April 1994 which significantly improved access to the Canadian market for U.S. beer. However, U.S. exporters remain concerned about provincial minimum price policies and taxes, ostensibly for environmental purposes, on beer cans.

Wine and Spirits

Market access barriers in many provinces continue to hamper exports of U.S. wines and spirits to Canada. These market access barriers include cost-of-service mark ups, listings, reference prices, and discriminatory distribution and warehousing policies.

Canada

On May 28, 1996, Industry Canada issued amendments to the regulations on consumer packaging and labeling that retained the existing standard container sizes for wine. Industry Canada is currently revisiting the issue and hopes to conclude its review by mid-1997. Elimination of standard container sizes in Canada would allow U.S. exporters to ship wine in containers that are common in the United States but are not currently permitted in Canada. The United States will continue to pursue removal of these barriers in appropriate fora.

Supply Managed Products and Barley

As part of its implementation of the World Trade Organization (WTO) Agreements, Canada replaced its import quotas on certain supply managed commodities (dairy, poultry, and eggs) with tariff rate quotas (TRQs). Under the TRQ system, small amounts of imports can enter at low rates of duty, but imports above those limits are subject to prohibitively high duties ranging up to 350 percent. Canada also imposed tariffs on U.S. barley and barley products as well as additional dairy products beginning August 1, 1995. Barley imports from the United States were previously subject to import licensing requirements. Although a panel established under NAFTA Chapter 20 dispute settlement procedures upheld Canada's use of these various tariffs in December 1996, the United States will continue to pursue improved access to the Canadian market for U.S. dairy, eggs, poultry, and barley products. In addition, the United States will continue to review Canada's dairy industry support programs to determine whether they are consistent with Canada's NAFTA obligations and Canada's obligations in the WTO to limit subsidies. The United States and other countries have expressed concern with these programs at the WTO.

Horticultural Import Restrictions

Canadian regulations on fresh fruit and vegetable imports prohibit consignment sales of fresh fruits and vegetables without a prearranged buyer. Other restrictions prohibit bulk produce imports without a special ministerial waiver of Canadian packaging regulations.

Restrictions on U.S. Publications

In 1996, USTR initiated a Section 301 investigation and requested consultations with the Government of Canada to address certain discriminatory practices used by the Government of Canada to unfairly protect Canada's domestic magazine industry. Subsequently, USTR used WTO dispute settlement procedures to challenge these discriminatory practices. Specifically, USTR requested that a WTO panel be formed to consider Canadian measures prohibiting or restricting the importation into Canada of certain periodicals; tax treatment of so-called "split-run" periodicals; and the application of favorable postage rates to certain Canadian periodicals.

Canada prohibits imports of "split-run" editions of magazines (regional editions that include advertising and some content aimed at the regional audience). Magazines are also prohibited from entering Canada if more than five percent of total advertising space contains ads that give Canadian sources of availability or specific conditions relating to the sale or provision of any goods or service in Canada. Moreover, since 1979, Canada Post Corporation (CPC) has applied higher postal rates to foreign publications mailed in Canada than to Canadian publications.

During 1994, in response to the launch of a Canadian edition of "Sports Illustrated," which was electronically transmitted to and printed in Canada, the Canadian Government "clarified" its investment policies on split-run magazines, defining new magazine titles as "investments" subject to review under the Investment Canada Act. Moreover, in 1995, the Canadian Government enacted an excise tax on split-run magazine editions such as “Sports Illustrated” on a per-issue basis at a rate of 80 percent of the amount charged for all advertising appearing in that issue.

The WTO panel’s report, entitled *Canada --Certain Measures Concerning Periodicals,* was circulated to WTO Members on March 14, 1997. The Panel’s findings support the United States on nearly all claims. The panel recommended that Canada bring its practices into conformity with GATT 1994. Either Party may appeal the panel’s decision to the WTO Appellate Body.

GOVERNMENT PROCUREMENT

NAFTA and the CFTA significantly increased the value of the Canadian procurement market open to U.S. suppliers. Goods contracts valued at more than $25,000 (the WTO procurement threshold) are open to U.S. suppliers on a non-discriminatory basis. NAFTA also opens up services contracts and goods and services contracts by the Canadian federal government valued at more than $50,000 ($250,000 for covered government-owned enterprises, or “Crown corporations”) and federal government construction services contracts valued at more than $6.5 million ($8 million for covered Crown corporations). In addition, NAFTA extends coverage to a number of federal entities and some government-owned enterprises (Crown corporations) not covered by the CFTA. NAFTA also builds on the CFTA's effective bid-challenge system and greater transparency.

However, federal and provincial "buy national" or "buy local" policies are still applied to some of Canada's government procurement. For instance, the Canadian Government sources its printing solely from Canadian establishments. Where GATT Government Procurement Code or NAFTA requirements do not apply, some Canadian government entities favor Canadian-based firms. Bids are solicited from vendors on source lists which favor Canadian over foreign-based firms. Generally, if there is sufficient competition from Canadian-based sources, foreign-based firms are not invited to bid.

Sole-source procurements are also used to favor Canadian firms. Canada's industrial benefits policy is also administered through a "procurement review mechanism," which may require a supplier to invest, purchase, and/or hire in Canada as a condition of receiving a large contract.

LACK OF INTELLECTUAL PROPERTY PROTECTION

In 1996, the Canadian Government introduced new copyright legislation which would establish a public performance right for record producers and performers and a levy on the sale of blank audio tapes. The revenues collected from these programs are intended to compensate performers and producers for the performance and unauthorized home-taping of their works in Canada. The United States is extremely concerned that U.S. performers and producers may be denied national treatment under the proposed legislation. USTR is consulting with U.S. industry on next steps should the legislation become law.

Canada

SERVICES BARRIERS

Broadcasting Act

The Broadcasting Act sets out the broadcasting policy for Canada, which lists among its objectives, "to safeguard, enrich and strengthen the cultural, political, social and economic fabric of Canada." The federal broadcasting regulator, the Canadian Radio-Television and Telecommunications Commission (CRTC), is charged with implementing this policy. Under current CRTC policy, in cases where a Canadian service is licensed in a format competitive with that of an authorized non-Canadian service, the Commission can drop the non-Canadian service, if the new Canadian applicant requests it to do so. This policy has already led to one “de-listing” and deterred potential new entrants from attempting to enter the Canadian market.

Direct-to-Home Satellite Broadcasting

In August 1994, the CRTC issued an order that discriminated against U.S.-associated providers of direct-to-home (DTH) satellite broadcasting services seeking to offer such service to Canadian consumers. The CRTC order exempted Canadian DTH providers from licensing requirements, but subjected U.S.-associated DTH providers to lengthy licensing procedures which effectively would have precluded entry into the Canadian market even where U.S. associated providers complied with existing CRTC ownership and content requirements.

In July 1995, the Canadian federal cabinet overturned the CRTC’s DTH policy and ordered that all services be licensed under the same rules. On December 20, 1995, the CRTC issued two national DTH satellite TV licenses, one of which went to U.S.-associated Power DirecTV. However, Power DirecTV has since abandoned its plans to launch a Canadian service because of technological issues, some of which were associated with CRTC regulations.

Simultaneously with the licensing of the two DTH systems, a number of DTH pay-per-view (PPV) services were also licensed. The DTH licenses specify that the only PPV services the two DTH licensees may offer are those services licensed by the CRTC. The PPV licenses are further conditioned in two significant respects.

First, it is a condition of license that feature film rights must be acquired from Canadian distributors except where the film is offered by a foreign distributor who owns worldwide rights or who has provided not less than half of the cost of producing the film. The U.S. Government and the U.S. industry are concerned that this condition of license, in effect, gives Canadian companies monopoly distribution rights with respect to certain films. U.S. industry sources report that it is common practice for film distribution rights to be purchased by different companies for different parts of the world. Under this condition, only Canadian distributors will be allowed to license these films to the Canadian PPV services.

Second, it is a condition of license that 100 percent of revenues earned from the exhibition of Canadian feature films be paid to the producer/distributor. However, revenues earned from the exhibition of all non-Canadian feature films offered on English language services must be split, on a title by title basis, one-third to the DTH service, one-third to the programming undertaking, and one-third to the producer/distributor. U.S. industry sources report that the likely effect of this restriction will be to restrain competition.

The Canadian Motion Picture Distributors Association and a number of U.S.-based studios appealed the licensing conditions to the Federal Court of Appeal on January 26, 1996, and to the Canadian federal Cabinet on February 2, 1996. On March 19, 1996, the Cabinet rejected the appeal, apparently deciding it a matter best dealt with by the court, and on June 26, 1996, the Federal Court of Appeal also ruled against the appeal. A key finding of the court was that the CRTC's action was "directly related to broadcasting, a federal concern, and is not a veiled attempt to regulate film production or film distribution which are under provincial jurisdiction."

USTR will continue to closely monitor the effect of these policies on U.S. interests.

Direct-to-Home Pay-Audio Services

A U.S. Direct-to-Home (DTH) pay-audio service, Digital Music Express (DMX), was granted a license on two occasions by the CRTC over the past several years only to have the license overturned by the government for further examination of whether more Canadian content should be required. USTR persuaded Canada not to overturn the license as requested by Canadian interests for a third time, and as a result, DMX received a license to operate in Canada on October 11, 1996.

Basic Telecommunications Services

In the recently concluded WTO negotiations on basic telecommunications services, Canada made commitments on all basic telecom services, with phase-in of some commitments. For instance, market access to the Canada-non-U.S. international services market and to land submarine cables is not granted until October 1, 1998. Canada adopted the reference paper on regulatory commitments. Canada retained a 46.7 percent limit on foreign ownership, a requirement for "Canadian control" of basic telecom facilities, and a routing restriction to promote the use of Canadian facilities for domestic traffic. The routing restrictions are with regard to both domestic Canadian and international traffic, but the international traffic restrictions will be phased out across time.

Border Broadcasting

In 1976, Canada adopted a tax provision denying Canadian enterprises tax deductions for the cost of advertising in foreign print and broadcast media when the advertising is directed primarily at Canadians. The main targets of this legislation were advertisements placed on U.S. border television stations beaming programs into Canada, but the provision also applies to U.S. periodicals.

Government-to-government and industry-to-industry consultations have failed to provide a compromise solution to this problem. As a result of a 1980 Section 301 determination that the Canadian law both injured and discriminated against U.S. commerce, the United States enacted mirror legislation in the 1984 Trade Act against Canada's broadcast media. However, U.S. legislation was never enacted against Canada's print media.

Canada

Temporary Entry of Goods

Under the temporary importation regulations, Revenue Canada allows the temporary entry, at free or reduced rates, of certain specialized equipment needed to perform short-term service contracts, if such equipment is not available from Canadian sources. Under the NAFTA, Canada has broadened the range of professional equipment allowed temporary duty-free entry, but it has not provided unrestricted access. Presently, in the context of a three-year comprehensive review by the Canadian Government launched in 1994 on ways to simplify the Canadian tariff system, it has been proposed that a single tariff item be introduced to replace a number of current provisions covering temporarily-imported goods. Essentially, the new item would provide conditional free entry, on a most-favored-nation basis, for temporarily-entered goods without regard for whether the goods are available from Canadian sources. Movement by the Canadian Government toward this tariff system revision is expected on January 1, 1998.

Insurance and Banking

U.S. insurance companies may enter Canada as branches, but some provinces bar foreign companies from buying provincially-chartered insurance companies. The "National Treatment Study" published by the U.S. Department of the Treasury on December 1, 1994, provides recent, detailed information on the treatment of U.S. banks and securities dealers in Canada. U.S. banks and securities firms have a clear right of establishment and a guarantee of national treatment. The principal barrier of which U.S. banks have complained is Canada's prohibition on the establishment of foreign bank branches; Canada is the only G-10 country that restricts foreign bank entry to separately organized and capitalized subsidiaries. Canada agreed under Article 1403 of the NAFTA to review this restriction when Canadian banks are allowed to expand through subsidiaries or direct branches "into substantially all of the United States." The United States and other OECD countries have been pressuring Canada to allow foreign bank branching as soon as possible, in conjunction with the 1997 renewal of Canada’s banking legislation. In February 1997, Canada announced that it would introduce legislation by the end of 1997 which would allow foreign banks to branch directly into Canada.

INVESTMENT BARRIERS

General Entry Restrictions

Under the Investment Canada Act and Canadian policies in the energy, publishing, telecommunications, transportation, film, music, broadcasting, and cable television sectors, Canada maintains laws and policies which inhibit new or expanded foreign investment.

Investment Canada Act

The Investment Canada Act requires the federal government to review proposed acquisitions by U.S. and other foreign investors to ensure "net benefit to Canada." Foreign investments in new businesses, direct acquisitions worth less than C$5 million, and indirect acquisitions worth less than C$50 million do not require prior government approval. Under the CFTA, Canada raised the threshold level for review of direct acquisitions by U.S. investors to C$150 million. Under NAFTA, this threshold (currently at C$160 million) will continue to be increased in line with the growth of nominal GDP. Screening of indirect acquisitions by U.S. investors has been eliminated. However, these exemptions do not apply to foreign investments in "culturally sensitive sectors" such as publishing, film, video, music, broadcasting, and telecommunications. Any foreign investment in these sectors is potentially subject to review.

Publishing Policy

Prior to 1992, when ownership of a firm engaged in the publication, sale, or distribution of books, magazines, periodicals, or newspapers in Canada passed to foreign investors as a result of mergers and acquisitions of parent firms outside of Canada ("indirect acquisition"), Canada required divestiture of control to Canadian investors.

Since January 1992, Canadian book publishing and distribution firms that fall into foreign hands through indirect acquisition need not be divested to Canadian control, but the foreign investor must negotiate specific commitments to promote Canadian publishing. Foreign investors may directly acquire Canadian book firms under limited circumstances. Also, since 1993, Canada treats the publication of any new magazine title by foreign-owned firms as a new investment subject to review. Under current policy guidelines, approval for a new magazine title would not be granted. The United States is monitoring the effect of these new policies on U.S. interests.

Film Industry Investment

Canadian policies prohibit foreign takeovers of Canadian-owned film distribution firms. They allow investment to establish new distribution firms for proprietary products only. Indirect or direct takeovers of foreign distribution firms operating in Canada are only allowed if the investor undertakes to reinvest a portion of its Canadian earnings in a manner specified by the Canadian Government.

Performance Requirements

Reviews of prospective foreign investments involve an examination of the investor's business plan by Investment Canada. Approval of the investment creates a legal obligation on the part of the investor to fulfill the business plan, which may include commitments in areas such as research and development or the promotion of Canadian authors. The United States successfully concluded a GATT case requiring Canada to stop extracting commitments from foreign investors to favor Canadian suppliers. The CFTA made major progress toward ending the imposition of performance requirements on U.S. investors, and on third country investors when U.S. trade interests would be affected. The United States will continue to pursue the elimination of investment restrictions, including performance requirements, both bilaterally and multilaterally.

Canada

OTHER BARRIERS

Canadian Wheat Board

The Canadian Wheat Board (CWB) has exclusive authority to market western Canadian wheat, durum wheat, and barley for export. It also controls milling wheat and malting barley sales domestically. The United States has been working to have the export activities of state trading enterprises, such as the CWB, addressed in the WTO Committee on Agriculture. In the October 1995 report of the private, binational Joint Commission on Grains (JCG), the JCG also recommended that both countries "eliminate the excessive discretionary pricing practices of their institutions" which for Canada would mean "placing the CWB at risk of profit or loss in the marketplace, or conducting itself in an equivalent manner."