CANADA

TRADE SUMMARY

Canada has an affluent, high-technology, market-oriented economy. Its proximity to the United States and its generally liberal trade regime has resulted in the volume of two-way bilateral trade surpassing that of the United States with any other single country. The economic slowdown, and terrorist attacks of 2001 in the United States are primarily responsible for a decline in trade, though numbers remain strong. The U.S. trade deficit with Canada was $49.8 billion in 2002, a decrease of $3.1 billion from $52.8 billion in 2001. U.S. goods exports in 2002 were $160.8 billion, down 1.6 percent from the previous year. Corresponding U.S. imports from Canada were $210.6 billion, down 2.6 percent. Canada is the largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Canada were $24.3 billion in 2001 (latest data available), and U.S. imports were $18.1 billion. Sales of services in Canada by majority U.S.-owned affiliates were $44.3 billion in 2000 (latest data available), while sales of services in the United States by majority Canada-owned firms were $51.3 billion.

The United States and Canada also share one of the world's largest bilateral direct investment relationships. In 2001, the stock of U.S. foreign direct investment (FDI) in Canada was $139 billion, up from $128.8 billion in 2000. U.S. FDI in Canada is concentrated largely in manufacturing, finance and petroleum sectors. Canadian foreign direct investment in the United States was $108.6 billion. U.S. investment in Canada, which is a major contributor to the U.S. non-goods trade surplus with Canada, is concentrated in manufacturing, natural resources, and the Canadian financial sector.

A Trading Relationship Based on Free Trade

The North American Free Trade Agreement (NAFTA) came into force on January 1, 1994 and replaced a bilateral free trade agreement implemented in 1989. The bilateral phase-out of tariffs between Canada and the United States was completed on January 1, 1998, except for tariff-rate quotas (TRQ) that Canada has not eliminated on certain supply-managed agricultural products. However, Canada still maintains some non-tariff barriers of concern at both the federal and provincial levels, impeding access to the Canadian market for U.S. goods and services.

IMPORT POLICIES

Supply-Managed Products

Canada closely restricts imports of certain "supply-managed" agricultural products (the domestic production of which is limited by quota, i.e., dairy products, eggs and poultry) through tariff-rate quotas, severely limiting the ability of U.S. producers to increase exports to Canada above the TRQ.

Dairy: As part of its Uruguay Round WTO obligations, Canada agreed to specific limits on export subsidies for dairy products. In 1995, Canada replaced its subsidy payments on all dairy exports, which were financed by a levy on dairy producers, with a new system. However, this system let Canadian processors buy lower-priced milk and use it to make cheese and other dairy products for export. The United States challenged this system in the WTO.

In 1999, a WTO panel and the Appellate Body found that Canada's special milk class system, which provides discounted milk for export, was indeed an export subsidy. The WTO panel and the Appellate Body also found that Canada was violating its obligations under the WTO Agreement on Agriculture by shipping more subsidized dairy exports than it had agreed to.

In response, Canada introduced its "commercial export milk" scheme. A WTO panel agreed in July 2001 that Canada's new system continued to provide an export subsidy in the form of discounted milk to Canadian dairy processors. Canada appealed the panel's findings. In July 2002, a new panel concluded that Canada was continuing to provide illegal export subsidies to Canadian dairy processors with the discounted milk. A December 2002 Appellate Body report affirmed that panel's findings. The United States has requested authorization to retaliate. Canada has indicated it will comply with the Appellate Body's findings and is in the process of re-regulating dairy product exports on a provincial basis.

Margarine: The Province of Quebec continues to apply coloring restrictions on dairy margarine. In addition, provincial restrictions on the marketing of butter/margarine blends and imitation dairy products have served to limit and, in certain cases, prohibit the sales of these products into many provinces. The provinces of Ontario, Manitoba and Saskatchewan are challenging Quebec's provincial coloring regulations.

Cheese snack foods: Canada remains unwilling to resume duty-free trade in cheese snack foods between the United States and Canada. Prior to 1999, cheese snack foods were traded duty-free between the United States and Canada. Canada ceased issuing duty-free import permits, effective September 1, 2001, and initiated a tariff of 245 percent on U.S. exports of breaded cheese sticks to Canada. Canada was responding to a 1999 U.S. Customs Service reclassification of cheese sticks, which subjected imports to a TRQ and over-quota tariff. USTR completed consultations with Congress on November 7, 2001, and is prepared to request that the President issue a Proclamation to return duty- and quota-free treatment to Canadian cheese sticks, provided Canada commits to providing the same tariff treatment for imports of similar U.S. cheese snack foods. In early January 2002, the Department of Foreign Affairs and International Trade informed USTR that Canada had no intention of reducing its duties or entering into negotiations with the United States.

Processed egg products: The Canadian Egg Marketing Agency maintains a dual pricing scheme for processed egg products. Under that regime, the domestic Canadian price for shell eggs is maintained at a level substantially above the world price. Producers are also assessed a levy on all eggs sold and a portion of the levy is used to subsidize exports of eggs. This practice artificially increases Canadian exports of egg products at the expense of U.S. exporters.

Horticultural Import Restrictions

Canada continues to restrict international trade of bulk produce. Importers may request waivers, but Canadian federal and provincial authorities may deny such requests if an equivalent supply is available from domestic sources. In addition, Canadian regulations on fresh fruit and vegetable imports prohibit consignment sales of fresh fruit and vegetables in the absence of a pre-arranged buyer.

Restrictions on U.S. Grain Exports

U.S. access to the Canadian grain market has been limited due in part to Canadian varietal controls. Canada requires that each variety of grain be registered and be visually distinguishable. Because U.S. varieties may not be visually distinct, they are not registered in Canada. As a result, U.S. wheat is being sold in Canada as "feed" wheat at sharp price discounts compared to the Canadian varieties.

Wine and Spirits

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

The Canadian Wheat Board and State Trading Enterprises

The Canadian Wheat Board (CWB) continues to enjoy government-sanctioned monopoly status as well as other privileges that restrict competition. In February 2002, the Administration announced a four- prong plan, which it has pursued aggressively over the past year.

First, the plan called for the examination of a possible WTO challenge. On March 6, 2003, USTR announced it would seek formation of a World Trade Organization dispute settlement panel to examine the wheat trading practices of the Government of Canada and the CWB. The United States' panel request also challenges Canada's requirements to segregate imported wheat in the Canadian grain handling system and Canada's discriminatory policy that affects the access of U.S. grain to Canada's rail transportation system.

Second, the Administration committed to work with the U.S. industry to examine the possibility of filing antidumping and countervailing duty petitions. The North Dakota Wheat Commission filed petitions on September 13, 2002. On March 4, 2003, the U.S. Department of Commerce issued a preliminary determination in the countervailing duty investigation, announcing a 3.94 percent countervailing duty to be applied provisionally while the dumping and countervailing duty investigations continue.

Third, USTR announced that it would work with the U.S. industry to identify impediments to U.S. wheat entering Canada. The elements of the WTO case regarding Canada's grain segregation requirements and rail transportation rules are a direct result of those efforts.

Fourth, the United States committed to seek reform of state trading enterprises through the adoption of new rules in the WTO agriculture negotiations, which are part of the Doha Development Agenda launched in November 2001. The United States is aggressively pursuing this negotiating objective. In particular, the United States has proposed eliminating export monopolies so that any producer, distributor, or processor can export agriculture products. The United States has also proposed ending special financial privileges which are granted to state traders and expanding their WTO transparency obligations.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Restrictions on Fortification of Foods

Canadian requirements for foods fortified with vitamins and minerals have created a costly burden for some American food manufacturers who export to Canada. Health Canada restricts marketing of breakfast cereals and other products, such as orange juice, that are fortified with vitamins and/or minerals at certain levels. The current regulatory regime requires that products such as calcium-enhanced orange juice be treated as a drug, and forces manufacturers to label vitamin and mineral fortified breakfast cereals as "meal replacements." These standards impose costs on manufacturers who are forced to make separate production runs for the U.S. and Canadian markets.

A U.S. company may request a Temporary Marketing Authorization Letter (TMAL) from Health Canada which may grant a 2-3 year marketing authorization when the benefits of a product are clear, but the potential risks to a consumer are still under study. However, U.S. companies have encountered difficulties with consistency and transparency in this process, and many breakfast cereals are still prohibited from entering Canada without extensive re-labeling and without incurring associated marketing expenses, to re-brand breakfast cereal as, for example, "meal replacements." A joint effort conducted under the auspices of the U.S. Institute of Medicine (IOM) is expected to lead to greater Canadian-American harmonization of nutrient levels in food. According to Health Canada, the target date for new Canadian fortification regulations which reflect the IOM effort is October 2004.

GOVERNMENT PROCUREMENT

As a Party to the WTO Government Procurement Agreement (GPA), Canada allows U.S. suppliers to compete on a non-discriminatory basis for its federal government contracts covered by the GPA. However, Canada has not yet opened "sub-central" government procurement markets (i.e., procurement by provincial governments), despite commitments in the GPA to do so no later than July 1997. Some Canadian provinces maintain "Buy Canada" price preferences and other discriminatory procurement policies that favor Canadian suppliers over U.S. and other foreign suppliers. Because Canada does not cover its provinces, Canadian suppliers do not benefit from the United States' GPA commitments with respect to 37 state governments' procurement markets. In recent years, several U.S. states and Canadian provinces have cooperated to make reciprocal changes in their government procurement systems that may enhance U.S. business access to the Canadian sub-federal government procurement market. However, the Administration and a number of U.S. states have expressed concern that Canadian provincial restrictions continue to result in an imbalance of commercial opportunities in bilateral government procurement markets.

EXPORT SUBSIDIES

Softwood Lumber

The 1996 U.S.-Canada Softwood Lumber Agreement expired on March 31, 2001. This bilateral agreement was put in place to mitigate the effects of subsidies in several Canadian provinces. Upon expiration of the Agreement, the U.S. lumber industry filed antidumping and countervailing duty petitions regarding Canadian softwood lumber. Preliminary investigations found both dumping and subsidies, and led to the imposition of preliminary duties. On March 22, 2002, the U.S. Department of Commerce announced its final, company-specific antidumping duties and a countrywide (except for the Maritime provinces) countervailing duty determination. On April 26, 2002, the Commerce Department announced amended final antidumping rates ranging from 2.18 percent to

12.44 percent and an amended final countervailing duty rate of 18.79 percent.

Canada is challenging the underlying Commerce Department and ITC investigations in the WTO and NAFTA. On November 1, 2002, the WTO Dispute Settlement Body officially adopted a panel report which addressed the Canadian challenge of the Commerce Department's preliminary countervailing duty determination. The report is a victory for the U.S. on two key issues: Canadian provinces' sale of timber from public lands can constitute a subsidy under the WTO Subsidies Agreement; and U.S. laws governing reviews of countervailing duty orders are consistent with the WTO Subsidies Agreement.

Negotiations in early 2003 to find a durable solution as an alternative to the cycle of trade cases and litigation progressed significantly and narrowed differences in several areas. No agreement has been reached at this time, however. The United States continues to encourage Canadian provinces to implement market-based pricing for sales of timber from public lands. In the absence of an agreement on basic reforms, the United States will effectively enforce U.S. trade laws to address the U.S. industry's concerns about subsidies to, and dumping of, Canadian softwood lumber.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Canada is a member of the World Intellectual Property Organization (WIPO), and adheres to a number of international agreements, including the Paris Convention for the Protection of Industrial Property (1971), the Berne Convention for the Protection of Literary and Artistic Works (1971), and the 1952 Universal Copyright Convention (UCC). Canada is also a signatory of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty (together, the WIPO Treaties), which set the standards for intellectual property protection in the digital environment. The United States has ratified both treaties and would like Canada to do the same.

To date, however, Canada has not introduced draft legislation that would ratify the WIPO treaties. While Canada was a strong supporter of both treaties, which led to it becoming a signatory, intense lobbying by Canadian broadcasters and Provincial Education Ministers has prevented Canadian ratification. In the legislated five-year review of the 1997 Copyright Act, published in October 2002, Canada listed ratification of the WIPO Treaties as the top copyright priority, and plans to develop the necessary legislation within the next two years.

Canada's Copyright Act contains two provisions under which Canada applies reciprocal rather than national treatment. The first provision is for the payment of a neighboring rights royalty to be made by broadcasters to artists. Under Canadian law, those payments are only guaranteed to artists from countries that are signatories of the 1961 Rome Convention. The United States is not a signatory of the Convention, and Canadian authorities have still not determined whether U.S. artists will receive national treatment in the distribution of these royalties. The second provision is for the payment of a levy by manufacturers and importers of blank analog and digital tapes and diskettes to artists from countries that provide an equivalent payment to Canadian artists. Canada's copyright law stipulates this reciprocity criterion in distribution of the blank tape levy to foreign artists. The United States does not impose a levy on analog tape, only on digital audio recording media, with proceeds distributed to applicable artists, including Canadians. The United States perceives Canada's reciprocity requirement for both the neighboring rights royalty and the blank tape levy as denying national treatment to U.S. copyright holders. Consequently, USTR has placed Canada on its Special 301 "Watch List" for the past four years. While Canada may grant some or all of the benefits of the regime to other countries, if it considers that such countries grant or have undertaken to grant equivalent rights to Canadians, Canada has yet to announce a determination with regard to the United States.

Canada's border enforcement measures have been the target of criticism by American intellectual property owners who express concern with the low rate of prosecution arising from counterfeit goods seizures. Deficiencies in border enforcement are compounded by the failure, or lack of resources of law enforcement authorities to conduct follow-up investigations of many illegal import cases.

The United States is also monitoring Canadian policies with respect to patent and data protections. Canadian patent protection has improved following two WTO cases in which Canada agreed to, among other things, amend its patent law to provide 20-year patent protection to all patents filed before October 1989. Canada also has eliminated its regulations which previously allowed generic manufacturers to stockpile pharmaceuticals before a patent expired. However, Canadian enforcement of its TRIPS obligations continues to be a source of concern. Although Canada has statutory data protection, several judicial rulings have cast doubt on how well these protections are being enforced as required by TRIPS article 39.3. Canadian authorities allow parties other than the rights holder effectively to gain marketing approval in direct reliance on protected confidential data and it appears Canada may be in violation of 39.3. In addition to this perceived discrepancy between the standard applied by Canadian courts and that provided under the TRIPS and the NAFTA, Canada apparently is failing to apply its "linkage regulations" effectively. Such regulations require that Health Canada determine if the marketing of generic pharmaceuticals infringes on existing name-brand patents.

SERVICES BARRIERS

Broadcasting

The Broadcasting Act 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. The CRTC requires that for Canadian conventional, over-the-air broadcasters, Canadian programs make up 60 percent of television broadcast time overall and 50 percent during evening hours (6 pm to midnight). It also requires that 35 percent of popular musical selections broadcast on radio should qualify as "Canadian" under a Canadian Government-determined point system. For cable TV and direct to home (DTH) broadcast services, a preponderance (more than 50 percent) of the channels received by subscribers must be Canadian programming services. For other services, such as specialty television and pay audio services, the required percentage of Canadian content varies according to the nature of the service.

The CRTC also requires that the English and French television networks operated by the Canadian Broadcasting Corporation (CBC) not show "popular foreign feature movies" between 7 pm and 11pm. The only non-Canadian films that maybe broadcast during that time must have been released in theaters at least two years previously, and not be listed in the top 100 of Variety Magazine's top grossing films for at least the previous ten years.

Under previous CRTC policy, in cases where a Canadian service was licensed in a format competitive with that of an authorized non-Canadian service, the Commission could revoke the license of the non-Canadian service, if the new Canadian applicant requested it to do so. This policy led to one "de-listing" in 1995, and has deterred potential new entrants from attempting to enter the Canadian market. In July 1997, the CRTC announced that it would no longer be "disposed" to take such action. Nonetheless, Canadian licensees may still appeal the listing of a non-Canadian service which is thought to compete with a Canadian pay or specialty service, and the CRTC will consider removing existing non-Canadian services from the list if they change format so as to compete with a Canadian pay or specialty service.

Radiocommunication Act

One of the first initiatives of the Canadian Cable Television Association (CCTA) was to conduct a survey to determine the incidence of unauthorized use of satellite services. Industry findings, extrapolated on a national basis, established that 520,000-700,000 households within cabled areas use unauthorized satellite services. Any survey of the incidence of satellite theft outside cabled areas would add to these numbers.

This survey, combined with information obtained through Canadian film producers' investigations and related Internet Newsgroups, supports the conclusion that there are approximately 1,000,000 illegal users of U.S. satellite systems in Canada, resulting in a significant annual loss to the legitimate satellite industry. Of this number of illegal users, it is estimated that over 90 percent are involved in the "black market" (i.e., signal theft without any payment to U.S. satellite companies), with the remaining 10 percent subscribing via "gray market." "Grey market" signal theft is less attractive because of the unfavorable currency conversion in U.S. dollars. These survey results have led the Motion Picture Association to recalculate total losses to the U.S. motion picture industry due to signal theft in Canada. Annual losses to the U.S. motion picture industry due to audiovisual piracy in Canada were estimated by U.S. industry to be $122 million in 2002.

Basic Telecommunications Services

Under the terms of the WTO Agreement on Basic Telecommunications Services, Canada's commitments permit foreign firms to provide local, long distance, and international services through any means of technology, on a facilities or resale basis. However, Canada retained a 46.7 percent limit on foreign ownership for all services except fixed satellite services and submarine cables. Industry Canada announced in November 2002 that it was reviewing these ownership restrictions and seeking input from interested parties. In addition to the equity limitations, Canada also retained a requirement for "Canadian control" of basic telecommunications facilities which stipulates that at least 80 percent of the members of a board of directors must be Canadian citizens. These restrictions prevent global telecommunications service providers from managing and operating much of their own telecommunications facilities in Canada. In addition, these restrictions deny foreign providers certain regulatory advantages only available to facilities-based carriers (e.g., access to unbundled network elements and certain bottleneck facilities).

Canada has revised its universal service system. Previously, contributions to universal service funds were based upon on a per-minute assessment. This system potentially overcompensated incumbent local suppliers, who also competed in the long distance sector. The Canadian regulator, CRTC, established rules for a more competition-neutral collection system as of January 1, 2001. On May 30, 2002, the CRTC released its price caps decision, which cut contribution rates by 10 percent to 20 percent. This new regime extends through 2006.

Internet Services

A recent Canadian Federal Court of Appeals ruling concerning "caching" has the potential to stifle the development of a vibrant Internet services market in Canada. Caching is a way for Internet Service Providers (ISPs) to store content in a local server to enable users to retrieve it quickly without having to access such content from a distant host. It is a more efficient means by which ISPs provide access to data. The Court ruling essentially requires the ISPs to pay royalties if they cache copyrighted materials. The case is pending before the Supreme Court of Canada and its ruling, if upholding the lower Court's decision, could adversely impact the free flow of Internet traffic, Internet usage, and hinder the growth of electronic commerce.

Barriers to Film Exports

Classification Procedures: Classification of theatrical and home video product distributed in Canada is within the exclusive jurisdiction of the provinces. There are six different provincial or regional classification boards to which MPA members must submit product destined for theatrical release. Most of these boards also classify product intended for home video distribution.

As a control device, and to display a video's Québec classification, the Québec Cinema Act requires that a sticker be acquired from the Régie du Cinéma and attached to each pre-recorded video cassette and DVD at a cost of C$0.40 per unit. The Québec Government proposes to reduce the sticker cost to C$0.30 for English and French versions of films dubbed into French in Québec. In addition to the direct cost of acquiring the stickers, there are the administrative costs of attaching stickers to each unit and removing them from all returns, plus the per-title, per-distributor administrative fee of C$55.00 charged by the Régie.

In an effort to create a uniform, consumer-friendly classification system that more readily comports with national advertising campaigns and other practical concerns of the industry, the Canadian video distribution industry has initiated a voluntary national classification system for works distributed on videocassette and DVD. Under this system, a film's national rating is determined by averaging its provincial ratings and is displayed on the packaging. While some provinces accept the average national classification for the purpose of providing consumer information on pre-recorded video material, three of the provincial/regional boards -- Manitoba, Québec, and the Maritime Provinces (New Brunswick, Nova Scotia and Prince Edward Island) also require that their own classification be displayed.

The lack of unanimous acceptance of the voluntary national classification, and the negative precedent established by the Québec stickering regime continue to create significant consumer confusion and expense.

INVESTMENT BARRIERS

General Establishment Restrictions

Under the Investment Canada Act, the Broadcasting Act, the Telecommunications Act and standing Canadian regulatory policy, Canada maintains restrictions which inhibit new or expanded foreign investment in the energy, publishing, telecommunications, transportation, film, music, broadcasting, and cable television sectors.

Investment Canada Act

The Investment Canada Act (ICA) is intended to regulate foreign investment in Canada. The Government of Canada reviews the direct or indirect acquisition by a non-Canadian of an existing Canadian business of substantial size (as defined below). It also reviews the specific acquisition of an existing Canadian business or establishment of a new Canadian business by a non-Canadian in designated types of business activity relating to Canada's culture, heritage or national identity (as described below) where the federal government has authorized such review as being in the public interest. The Government of Canada must be notified of any investment by a non-Canadian to:

- establish a new Canadian business (regardless of size); or
- acquire direct control of any existing Canadian business which either has assets of C$5 million or more or is in a business that is identified by regulation to be culturally sensitive or in uranium production, financial services or transportation services; or
- acquire the indirect control of any existing Canadian business, the assets of which exceed C$50 million in value in a non-cultural business, or between C$5 million and C$50 million in a cultural business.

The C$5 million threshold was increased to C$218 million beginning in 2002 in cases where the country of the acquiring non-Canadian investor is a member of the World Trade Organization (WTO). In addition, there is no review process applicable to an indirect acquisition of a Canadian business by a non-Canadian whose country is a member of the WTO. The reviewing authority is the Department of Canadian Heritage in the case of investments related to cultural industries, and the Department of Industry in other cases. In practice, Canada has allowed most transactions to proceed, though in some instances only after compliance by the applicant with certain undertakings. The ICA sets strict time limits within which the reviewing authority must respond, in an effort to ensure that the legislation does not unduly delay any investment in Canada.

Publishing Policy

Since January 1992, Canadian book publishing and distribution firms that would transfer to foreign ownership as a result of an indirect acquisition need not be divested to Canadians, but the foreign investor must negotiate specific commitments to promote Canadian publishing. Foreign investors may directly acquire Canadian book firms under limited circumstances. Under an agreement on periodicals reached with the United States in May 1999, Canada permits 100 percent foreign ownership of businesses to publish, distribute and sell periodicals. However, direct acquisition by foreign investors of existing Canadian-owned businesses continues to be prohibited.

Film Industry Investment

Canadian policies prohibit foreign acquisitions of Canadian-owned film distribution firms. A new distribution firm established with foreign investment may only market its own proprietary products. Indirect or direct acquisition of a foreign distribution firm operating in Canada is only allowed if the investor undertakes to reinvest a portion of its Canadian earnings in a manner specified by the Canadian Government.

ELECTRONIC COMMERCE

There are currently few barriers to U.S.-based electronic commerce in Canada. In the WTO context, Canada has consistently supported the U.S. initiative for duty-free cyberspace. The CRTC announced in 1999 that it would not attempt to regulate the Internet.

CANADA

Early in 2000, Canada passed a new personal information protection law, the Personal Information Protection and Electronic Documents Act, which took effect on January 1, 2001. It requires persons or firms which collect personal information in the course of commercial activities to inform the subject of all purposes to which the data may be put, and to obtain informed consent for its use. This law initially applies only to the federally regulated private sector (e.g., airlines and telecommunications) and companies and interprovincial trade of personal information (e.g., companies which sell mailing lists). Application of the law will expand to other commercial activities in 2003, or when provincial governments pass similar legislation, as some have already done.