CANADA

Canada continues to be the United States' foremost export market and single largest trading and investment partner. In 1998, the U.S. trade deficit with Canada was $20.7 billion, a decrease of $2.8 billion from the 1997 deficit. U.S. merchandise exports to Canada were $154.2 billion during 1998, an increase of $4.0 billion from the level of U.S. exports to Canada in 1997. Canada was the United States' largest export market in 1998. U.S. imports from Canada were $175.0 billion in 1998, up 4 percent from 1997.

The United States continues to be by far the largest foreign direct investor in Canada. At the end of 1997, the stock of U.S. foreign direct investment was an estimated $100 billion. U.S. investment in Canada, which is a major contributor to the U.S. non-merchandise trade surplus with Canada, is concentrated in manufacturing, natural resources and financial sectors.

A Trading Relationship Based on Free Trade

On January 1, 1994, the entry into force of the North American Free Trade Agreement (NAFTA) superseded the U.S.-Canada Free Trade Agreement (CFTA) and expanded the free trade area to Mexico. The NAFTA extended the CFTA to important sectors such as trade in services, investment, and government procurement. The bilateral phase-out of tariffs between Canada and the United States outlined in the CFTA and now the NAFTA was completed on January 1, 1998, except for certain supply managed products in Canada and dairy, sugar, peanuts and cotton in the United States. However, some non-tariff barriers remain at both the federal and provincial levels, impeding access to the Canadian market for U.S. goods and services.

Also, liberalization of cross-border trade has drawn increased attention within Canada to certain long-standing barriers to trade in goods and services among Canadian provinces, notably those affecting government procurement and professional services. While provincial governments reached an agreement in 1994 to work toward the removal of these barriers between them, there has been little further progress in these areas, which is indicative of the difficulties in obtaining the elimination of barriers at the provincial level.

IMPORT POLICIES

Supply Managed Products

Canada closely restricts imports of certain "supply-managed" agricultural products whose domestic production is limited by quota (dairy products, eggs and poultry), severely limiting the ability of U.S. producers to export to Canada.

As part of its implementation of the World Trade Organization (WTO) Agreements in 1995, Canada replaced its import quotas on these commodities with tariff rate quotas (TRQs). Under the TRQ system, small amounts of imports can enter at a relatively low rate of duty, but imports above those limits are subject to prohibitively high duties ranging up to 300 percent.

Despite its Uruguay Round commitments, Canada does not allow access for commercial fluid milk imports. Canada's system of special milk classes also allows processors to purchase milk at prices that are below the comparatively high domestic milk prices in Canada. Without milk at such discounted prices, Canada's dairy product exports would be uncompetitive.. Canada viewed the creation of such special classes of milk as an acceptable method to maintain Canadian dairy exports, without the use of producer levies.

In October 1997, the United States requested consultations under GATT Article 22 pertaining to Canada's compliance with its WTO obligations to limit dairy export subsidies and to provide access in the form of a TRQ for its fluid milk market. In December 1997, New Zealand also requested consultations with Canada on the same matter, excluding the TRQ issue. A panel was established in March 1998, and issued its final report in March 1999. The panel found that Canada's milk system constitutes an export subsidy within the meaning of the WTO Agreement on Agriculture because of the significant involvement of government authorities in the provision of milk inputs to dairy product exporters at prices substantially below the levels otherwise available in Canada. The panel also found that the restrictions that Canada placed on the scope of access under its tariff rate quota for milk were inconsistent with its obligations under the GATT 1994. The panel recommended that Canada take action to conform both of the relevant measures to its WTO obligations.

Horticultural Import Restrictions

Canadian regulations prohibit consignment sales of imported fresh fruits and vegetables without a prearranged buyer. Other restrictions prohibit bulk produce imports without a special ministerial waiver from Canadian packaging regulations. Canada imposes extensive requirements on U.S. exports of seed potatoes into Canada. U.S. seed potatoes must meet complicated and unnecessary testing requirements.

Other Products

The Province of Quebec continues to apply coloring restrictions on dairy margarine. In addition, provincial marketing restrictions to butter/margarine blends or imitation dairy products have served as a limitation and in certain cases, prohibition to the sales of these products into many provinces.

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, resulting in top quality wheat being sold in Canada as "feed" wheat at sharp discounts to the Canadian varieties.

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 Working Party on State Trading Practices on Agriculture.

In October 1998, the GAO released a study on the CWB which concludes that little information on CWB contracts is publicly available. The U.S. grain industry has expressed concern that a lack of price transparency makes it difficult to determine whether the CWB is operating within its international obligations.

Under the December 1998 Record of Understanding, the United States and Canada agreed to at least quarterly consultations on Canada's grain exports to the United States. In addition, , the United States has established a special inter-agency group to monitor Canadian wheat imports and implmentaton of the December 4, 1998 Record of Understanding on agricultural trade in an effort to ensure that the Canadian Wheat Board is not pricing grain unfairly into the U.S. market.

EXPORT SUBSIDIES

The Canadian Egg Marketing Agency (CEMA) maintains an export subsidy for processed egg products. Under that regime, the domestic Canadian price for shell eggs is maintained at a level substantially above the world price. At the same time, producers are assessed a levy on all eggs sold and a portion of the levy is used to subsidize the exports of eggs. This practice artificially increases Canadian exports of egg products.
Provincial governments in Canada are believed to provide a variety of aids that support production and exports. Many of these mechanisms are not reported by Canada in its WTO notifications. For instance, producers and processors may benefit from credit assistance programs and preferential energy supply policies.

BARRIERS TO NON-AGRICULTURAL GOODS

Restrictions on U.S. Publications

In March, 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 requested that a WTO panel be formed to consider Canadian measures prohibiting or restricting the importation into Canada of "split-run" and other imported magazines, including a ban on imports of magazines with advertising directed at Canadians, a special excise tax on "split-run" magazines, and discriminatory postal rates on imported magazines.

WTO panel findings, as amended by the WTO Appellate Body, supported all U.S. claims. The panel recommended that Canada bring its practices into conformity with its WTO obligations. The parties agreed on a 15-month time frame (from July 30, 1997) for Canada to implement the panel recommendations. In October 1998, Canada tabled legislation which will have effects similar to the previous measures, by making it a criminal offense for foreign publishers to supply advertising services directed at the Canadian market to Canadian advertisers. As of March1999, this legislation was still before Parliament, although it has passed the lower Chamber.

Barriers to Film Exports

Film classification, for the purpose of theatrical and home video distribution in Canada, is within the exclusive jurisdiction of the provinces. There are presently seven different provincial classification boards to which member companies must submit product destined for theatrical release, five of which also classify product intended for home video distribution. The Province of Quebec requires that all video product bear a government issue classification sticker. U.S. exports are burdened by this added regulatory requirement resulting in fewer titles being made available. The lack of a national system and the negative precedent established by the Quebec stickering procedures, continues to create significant consumer confusion and administrative expense resulting in fewer U.S. exports.

LACK OF INTELLECTUAL PROPERTY PROTECTION

On April 25, 1997, Royal Assent was given to Bill C-32, legislation containing extensive amendments to Canada's Copyright Act. Bill C-32 was intended to further modernize Canadian copyright law and harmonize it with certain international copyright conventions.

The United States has expressed concerns to Canada because Bill C-32 potentially denies U.S. copyright holders certain broadcast rights and blank tape levy payments. These payments technically are supposed to be collected and distributed to Canadian copyright holders and to other copyright holders who are members of the Rome Convention. Under Bill C-32's provisions affecting "neighboring rights" and recording media, U.S. performers and producers will be denied proceeds, which is a denial of national treatment to U.S. copyright holders. The USTR announced on April 30, 1997, that due to these provisions, Canada was placed on the Special 301 Watch List, where it remained as of early 1999.

On September 1, 1997 the neighboring rights sections of the legislation were promulgated, and on January 1, 1999 the recorded media sections were promulgated. However, Canada has yet to determine the size of the levy payments for either section, and while both are legally in effect, neither neighboring rights fees nor recorded media levies have been implemented. The two governments are exploring mechanisms that would grant U.S. copyright holders equal treatment. USTR remains concerned by Canada's denial of national treatment of U.S. companies and artists, and will continue to monitor Canada's implementation of the law.

Concerns are increasing over continued cable and satellite signal piracy and we seek intensified efforts by the Government of Canada to aggressively enforce its anti-piracy laws.

In the field of patents, Canada has yet to correct its failure to grant a TRIPs-consistent term of protection for pharmaceutical products, which were under patent as of the date Canada’s WTO/TRIPs obligations came into force.

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 Canadian broadcasts make up 60 percent of television broadcast time -- 50 percent during prime time hours (6 p.m. to midnight). It also requires that 35 percent of musical selections broadcast on radio should qualify as "Canadian" under a Canadian Government-determined points system.

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 drop the non-Canadian service, if the new Canadian applicant requested it to do so. This policy led to one "de-listing" in 1995, and 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 actions. Nonetheless, Canadian licensees may still appeal the listing of competitive non-Canadian services. Also, the CRTC will consider the removal of existing non-Canadian services from the list if they change format so as to compete with a Canadian pay or specialty service.

The Broadcasting Act requires Canadian cable television providers to carry a majority of Canadian signals and services -- although service packages which are not "programming" may consist entirely of non-Canadian material. Also, U.S.-originated signals on non-basic pay television must be selected from a CRTC-approved list, from which U.S.-based services which are deemed to be competitive with already-licensed Canadian services are excluded.

Direct-to-Home Satellite Broadcasting

On December 20, 1995, the CRTC issued two national direct-to-home (DTH) satellite TV licenses, one of which went to U.S.-associated Power Direct TV. However, Power Direct TV 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.

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 believe 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 Canadian 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 that the matter would best be dealt with by the courts. On June 26, 1996, the Federal Court of Appeal also ruled against the appeal.

Canada also imposes specific and extensive content requirements on television and cable broadcasting. DTH broadcasts must contain a preponderance (more than 50 percent) of Canadian content. For some specialty services like pay audio services, the applicable percentage of Canadian content is subject to change. USTR will continue to closely monitor the effect of these policies on U.S. commercial interests.

Basic Telecommunications Services

Canada's recent liberalization of telecommunications opened both long-distance and local telephone services to competition. Canada's Telecommunications Act allows the federal regulator, the Canadian Radio-Television and Telecommunications Commission (CRTC), to "forbear" from regulating competitive segments of the industry, and exempts resellers from regulation. The use of pay telephones to provide services on a resale basis is not permitted. Some U.S.-based entrants have expressed concern that "forbearance" is being applied prematurely, which may allow incumbent firms to engage in anti-competitive behavior.

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. Canada also retained a requirement for "Canadian control" of basic telecom facilities (at least 80 percent of the members of a board of directors must be Canadian citizens), and a routing restriction to promote the use of Canadian facilities.

In September 1998, Canada eliminated third country routing restrictions for international traffic routed to and from Canada through the United States. Teleglobe Inc. is no longer the sole overseas facilities-based provider as of January 1, 1999, and licenses to land submarine cables are no longer limited. Telesat Canada will relinquish its monopoly control of fixed satellite space segment facilities used to provide national and U.S.-Canada telecommunications services on March 1, 2000.

The 1976 tax provision denying Canadian enterprises tax deductions for the cost of advertising in foreign print and broadcast media, aimed primarily at U.S. border television stations, remains in effect. U.S. legislation enacted in 1984 to mirror the Canadian measure also remains in force.

Banking and Insurance

The banking industry in Canada is governed by the Federal Bank Act, which is currently undergoing review and reform by the Government of Canada. At present, a foreign bank wishing to conduct business in Canada must establish a subsidiary (a Schedule II bank) under Canadian law. However, as part of the WTO Financial Services Agreement signed in December 1997 (which Canada has introduced legislation to ratify), Canada agreed to permit foreign branch banking by July 1999. Legislation to put this into effect was delayed pending the completion of a report by a federal Task Force on the Future of the Canadian Financial Services Sector. This report, issued on September 14, 1998, recommended that foreign branch banking be permitted.
The government has since stated that it supports liberalization of the banking sector and enhancing competition because it is in the public interest. Canada undertook obligations to liberalize branching effective June 30, 1999. Changes which would allow foreign branch banking were introduced to Parliament in February 1999.

Currently, U.S. insurance companies may enter Canada as branches, but some provinces bar foreign companies from buying provincially-chartered insurance companies. Following a recommendation by the 1998 Financial Services Task Force, on November 30, 1998, legislation was proposed in Parliament to allow demutualization of large Canadian life insurance companies, which the government expects to pass into law during 1999.

Electric Power

Electric power generation and distribution in Canada has traditionally been dominated by provincial government-owned monopoly utilities, several of which export significant amounts of power (totaling about US$1 billion annually) to the United States under long-term contracts, but import only a fraction of this amount on a short-term basis, mainly to satisfy peak demand loads.

Several of the larger provinces (including Alberta and Ontario) are now planning to move toward fully competitive electricity markets, including cross-border competition from U.S. firms. Some major utilities (including B.C. Hydro) have already obtained wholesale power marketer licenses from the U.S. Federal Energy Regulatory Commission, a condition of which is that they allow reciprocal open access to their distribution grids for wholesale power. Meanwhile, U.S. utilities and power brokers have been obtaining export licenses from the U.S. Department of Energy in anticipation of being able to compete in Canadian power markets. The restructuring of electric power markets is expected to continue at a rapid pace, benefiting consumers and industries in both countries.

INVESTMENT BARRIERS

General Entry Restrictions

Under the Investment Canada Act and specific 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

Foreign investors must notify the Canadian Government within thirty days of making an investment in Canada. The Investment Canada Act requires the federal government to review certain proposed foreign investments in order to ensure "net benefit to Canada." In 1998, for foreign investors from WTO member countries, indirect acquisitions were not reviewable but direct acquisitions worth over $179 million (asset values, in Canadian dollars) were reviewable unless specifically exempted. For acquisitions in uranium production, financial or transportation services, or cultural businesses, direct acquisitions worth over C$5 million and indirect acquisitions worth over C$50 million were reviewable.

In "cultural businesses," which include publishing, film, video, music and broadcasting, any directly or indirectly acquired foreign investment may be reviewed, if the Cabinet so decides and if the investor is notified within 21 days of the notification of investment. This regime effectively allows Canadian officials to impose conditions on prospective foreign investments on a case-by-case basis.

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 foreign parent firms or "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 policies on U.S. interests.

Film Industry Investment

Canadian policies prohibit foreign acquisitions of Canadian-owned film distribution firms and allow foreign investors to establish new distribution firms only for 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.

The Canadian Government is currently considering a range of possible policies to encourage more Canadian film production. Simultaneously, its broadcasting regulator, the CRTC, is reviewing both the television industry and the "new media" industries. We are monitoring closing changes in this area.

Performance Requirements

Reviews by Investment Canada of prospective foreign investments involves an examination of the investor's business plan. 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. NAFTA made 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.

ELECTRONIC COMMERCE

There are currently few barriers to U.S.-based electronic commerce in Canada. In the WTO context, Canada has been supportive of a duty free cyberspace. Canada also hosted the October 1998 OECD electronic commerce ministerial, contributing significantly to further progress on advancing barrier-free electronic commerce. The conference articulated a "shared vision" for global electronic commerce which includes the following elements: building trust for users and consumers; establishing ground rules which keep legal frameworks transparent, consistent and predictable; enhancing infrastructure through effective competition in telecommunications; and maximizing the benefits of the digital economy.

Several Canadian policy initiatives are underway in this area. These include a proposed new federal privacy law (Bill C-54), and a CRTC review of "new media" which is expected to address the question of regulatory jurisdiction over the Internet. The United States is monitoring the possible effects of these initiatives on U.S. interests.