

CANADA

TRADE SUMMARY

The U.S. goods trade deficit with Canada was \$72.8 billion in 2006, a decrease of \$5.7 billion from \$78.5 billion in 2005. U.S. goods exports in 2006 were \$230.6 billion, up 8.8 percent from the previous year. Corresponding U.S. imports from Canada were \$303.4 billion, up 4.5 percent. Canada is currently the largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Canada were \$32.5 billion in 2005 (latest data available), and U.S. imports were \$22.0 billion. Sales of services in Canada by majority U.S.-owned affiliates were \$46.9 billion in 2004 (latest data available), while sales of services in the United States by majority Canada-owned firms were \$36.6 billion.

The stock of U.S. foreign direct investment (FDI) in Canada in 2005 was \$234.8 billion (latest data available), up from \$212.8 billion in 2004. U.S. FDI in Canada is concentrated largely in the manufacturing, finance and mining sectors.

A Trading Relationship Based on Free Trade

The North American Free Trade Agreement (NAFTA) entered into force on January 1, 1994 replacing the U.S.-Canada Free Trade Agreement, which was implemented in 1989. The NAFTA progressively eliminated tariff and non-tariff barriers to trade in goods; improved access for services trade; established rules on investment; strengthened protection of intellectual property rights; and created an effective dispute settlement mechanism. Under the terms of the NAFTA, Canada eliminated tariffs on all remaining industrial and most agricultural products imported from the United States on January 1, 1998. The NAFTA is accompanied by supplemental agreements that provide for cooperation to enhance and enforce labor standards and to encourage environmentally friendly practices and bolster environmental protection in North America.

IMPORT POLICIES

Agricultural Products

Canada closely restricts imports of certain domestic “supply-managed” agricultural products such as dairy products, eggs and poultry through the use of tariff-rate quotas (TRQs). This practice severely limits the ability of U.S. producers to increase exports to Canada above the TRQ levels.

The Province of Quebec applies coloring restrictions on margarine. The province of Alberta, supported by the provinces of Manitoba and Saskatchewan, challenged Quebec's provincial coloring regulations through an inter-provincial trade dispute resolution panel appointed under the Agreement of Internal Trade. In June 2005, the Panel issued its ruling that the Quebec regulations on colored margarine restrict inter-provincial trade and recommended that Quebec amend its regulations to remove the ban on yellow-colored margarine no later than September 1, 2005. To date, Quebec has chosen not to implement the recommendations of the panel.

The Canadian Egg Marketing Agency operates a dual pricing scheme for processed egg products. Under the regime, the domestic Canadian price for shell eggs is maintained at a level substantially above the

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world price. Producers are also assessed a levy on all eggs sold, a portion of which is used to subsidize egg exports. This practice artificially increases Canadian exports of egg products at the expense of U.S. exporters. Canada also maintains a prohibitive tariff of 245 percent on U.S. exports of breaded cheese sticks.

Canada prohibits imports of fresh or processed fruits and vegetables in packages exceeding certain standard package sizes unless the government of Canada grants a ministerial exemption. To obtain an exemption, Canadian importers must demonstrate that there is an insufficient supply of a product in the domestic market. The import restrictions apply to all fresh and processed produce in bulk containers if there are standardized container sizes stipulated in the regulations for that commodity. For those horticultural products without prescribed container sizes, there is no restriction on bulk imports. The restriction has a negative impact on U.S. potatoes, apples and blueberries. 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 partially by Canadian varietal controls. Canada requires that each variety of grain be registered and be visually distinguishable based on a system of Kernel Visual Distinguishability (KVD) requirements. Since U.S. varieties may not be visually distinct, they are not registered in Canada. As a result, U.S. wheat, regardless of quality, is sold in Canada as "feed" wheat at sharp price discounts compared to the Canadian varieties. Extensive consultations were held in 2003 with stakeholders and the Canada Grains Commission (CGC) on the operational details of a Variety Eligibility Declaration system that would require, by law, the use of declarations instead of the KVD system to segregate grain in the handling system. This proposal was eventually scrapped when it was deemed too costly and burdensome for producers and industry. In June 2005, the CGC put out a new discussion paper proposing a different approach, one that would relax KVD registration requirements for minor western Canadian wheat classes, and held a new series of stakeholder consultations. In June 2006, the CGC announced its intention to make changes to western Canadian wheat classes based on these consultations. These changes include the removal of KVD registration requirements from minor wheat classes, as well as the creation of a new General Purpose wheat class, effective August 1, 2008. The KVD requirements for the higher quality wheat, Canada Western Red Spring and Canada Western Amber Durum, will remain. While these policy changes are a step in the right direction, it only opens the door to varietal registration in Canada of lower priced, non-milling U.S. wheat varieties typically used for feed and industrial end-uses (biofuels, etc.).

On September 16, 2005, the Canadian International Trade Tribunal (CITT) and the Canada Border Services Agency (CBSA) launched an investigation into alleged dumping and subsidization of U.S. grain corn imports into Canada, following a petition filed by the several provincial corn producers' associations. The CITT concluded on April 18, 2006, that U.S. grain corn imports are not causing injury and are not threatening to cause injury to Canadian growers. As a result, the dumping and subsidy investigations were terminated and all provisional countervailing and antidumping duties collected by CBSA were refunded. The petitioners have appealed the CITT final determination to Canada's Federal Court of Appeal.

Personal Duty Exemption

The United States has urged Canada to facilitate cross border trade for border residents by relaxing its taxation of goods purchased in the United States by Canadian tourists. While U.S. and Canadian personal exemption regimes are not directly comparable, the United States allows an \$800 per person exemption

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every 30 days, while Canada has an allowance linked to the length of the tourist's absence and allows only C\$50 for tourists absent for at least 24 hours and C\$200 for visits exceeding 48 hours. This practice discourages shopping visits to the United States by border residents.

Wine and Spirits

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

The Canadian Wheat Board and State Trading Enterprises (STEs)

The United States has longstanding concerns about the monopolistic marketing practices of the Canadian Wheat Board. USTR seeks a level playing field for American farmers, including through World Trade Organization (WTO) negotiations. The U.S. WTO agriculture proposal calls for: (1) the end of exclusive STE export rights to ensure private sector competition in markets currently controlled by single desk exporters; (2) the establishment of WTO requirements to notify acquisition costs, export pricing other sales information for single desk exporters; and (3) the elimination of the use of government funds or guarantees to support or ensure the financial viability of single desk exporters. The new Conservative government has begun a review of the Wheat Board that could address many of these concerns.

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 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. Canada's regulatory regime requires that products such as calcium-enhanced orange juice be treated as a drug. The regime forces manufacturers to label vitamin and mineral fortified breakfast cereals as "meal replacements" which imposes costs on manufacturers who must make separate production runs for the U.S. and Canadian markets.

In March 2005, the government of Canada released for public consideration a draft policy on supplemental fortification of food and beverages that reflects the study on Dietary Reference Intakes undertaken by the U.S. Institute of Medicine. Industry welcomed the draft policy as it may offer more latitude to manufacturers for discretionary fortification of foods and beverages than the current regulatory regime. The new policy may reduce the cross-border discrepancy in fortification rules; however, the final regulations based on it have not yet been submitted for public review.

Restrictions on Container Sizes

Canada's Processed Products Regulations (Canada Agricultural Products Act) prescribe standard container sizes for a wide range of processed fruit and vegetable products. No other NAFTA country imposes such mandatory container size restrictions. For example, the Processed Products Regulations require manufacturers of baby food to sell in only two standardized container sizes: 4.5 ounces (128 ml) and 7.5 ounces (213 ml). The requirement to sell in container sizes that exist only in Canada makes it more costly for U.S. producers of baby food to export their products to Canada. Canada claims that the regulations are being rewritten and suggests that U.S. concerns will be addressed. However, it appears that the effort to revise the regulations has stalled, as there has been no progress for the past several years.

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SOFTWOOD LUMBER

The Softwood Lumber Agreement (SLA) was signed on September 12, 2006, and entered into force on October 12, 2006. On October 12, pursuant to a settlement of litigation, the U.S. Department of Commerce revoked the antidumping and countervailing duty orders on imports of softwood lumber from Canada. (The settlement ended a large portion of the litigation over trade in softwood lumber.) Upon revocation of the orders, U.S. Customs and Border Protection ceased collecting cash deposits, and began returning all previously-collected deposits, with interest to the importers of record. At the time of entry into force, there was an injunction preventing liquidation of entries covered by the first administrative review, but the U.S. Court of International Trade subsequently lifted the injunction on October 27, 2006, in order to permit liquidation of those entries. All entries have now been liquidated.

The SLA provides for unrestricted trade in softwood lumber in favorable market conditions. When the lumber market is soft, Canadian exporting provinces can choose either to collect an export tax that ranges from 5 percent to 15 percent as prices fall or to collect lower export taxes and limit export volumes. The SLA also includes provisions to address potential Canadian import surges, provide for effective dispute settlement, and monitor administration of the agreement through the establishment of a Softwood Lumber Committee.

Under the terms of the SLA, Canada also agreed to pay \$500 million to members of the Coalition for Fair Lumber Imports, and \$450 million to promote meritorious initiatives in the United States, which includes educational and charitable causes in timber-reliant communities; low-income housing and disaster relief; and educational and public-interest projects addressing forest management issues that affect timber-reliant communities, or the sustainability of forests as sources of building materials, wildlife habitat, bio-energy, recreation and other values. Further, the SLA encourages interested persons in Canada and the United States to establish a binational industry council, whose objectives are to strengthen the North American lumber industry by increasing the market for its products and to build stronger cross-border partnerships and trust at all levels of the industry.

The first meeting of the Softwood Lumber Committee was held in February 2007. During that meeting, Canada and the United States discussed a wide range of implementation-related issues. In addition, there were comprehensive discussions on two issues of great concern to the United States. First, the United States has expressed its concerns with the announcements by Quebec and Ontario of a number of assistance programs for their provincial softwood lumber industries. Second, the United States is concerned with respect to some aspects of Canada's administration of the export measures. The United States is reviewing the information provided by Canada regarding those two issues in order to determine next steps.

TECHNOLOGY PARTNERSHIPS CANADA (TPC)

TPC is a Canadian government program that supports the research and development activities of select industries. Established in 1996, TPC provided loan funding for so-called "pre-competitive" research and development activities for companies incorporated in Canada. Although TPC was targeted at a number of industries, a disproportionate amount of funding has been provided to aerospace and defense companies. To date, C\$2.7 billion in TPC funding commitments have been made for over 600 projects, of which about 70 percent has been disbursed. According to the Canadian government, about 3 percent of TPC funds have been repaid. The Canadian government restructured the TPC program in 1999 after a WTO Dispute Panel requested by Brazil determined that it provided an illegal subsidy.

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In 2006, Canada's Minister of Industry closed the program to new TPC applicants except for the aerospace and defense sectors. The government announced increased transparency and accountability requirements for all future projects to be funded under the TPC with the aim of better ensuring company compliance with the terms of their TPC contribution agreements. These new contractual requirements provide the government more leverage to act on any breaches of the contribution agreements and will also allow the Minister of Industry to publish the amount of each repayment made by recipient companies that have received investments under the improved agreement. However, these efforts to promote transparency do not remove the potential for trade distortions caused by the TPC and other programs. Of particular concern to U.S. industry is a November 2006 news report that TPC and other government aid may be used to support the launch of a new class of Bombardier "C Series" regional jets and a December 2006 news report of significant TPC funding used to support the development of more efficient aircraft engines. The U.S. Government continues to monitor this program as well as other Quebec provincial programs.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Canada is a member of the World Intellectual Property Organization (WIPO) and adheres to several international agreements, including the Paris Convention for the Protection of Industrial Property (1971) and the Berne Convention for the Protection of Literary and Artistic Works (1971). Canada is also a signatory of the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty (together the WIPO Treaties), which set standards for intellectual property protection in the digital environment. Canada has not yet ratified either treaty. Canada has indicated it is drafting legislation to provide stronger copyright protection. However, no bill has yet been introduced during the current Parliamentary session.

The United States hopes that the expected legislation will not only adequately ratify and implement the WIPO Treaties, including prohibiting the manufacture and trafficking in circumvention devices, but also enact a limitation-of-liability for Internet Service Providers that effectively reduces copyright infringement on the Internet by using the "notice-and-takedown" model, rather than the less effective "notice-and-notice" model.

U.S. intellectual property owners are concerned about Canada's weak border measures and general enforcement efforts. The lack of *ex officio* authority for Canadian Customs officers makes it difficult for them to seize shipments of counterfeit goods. To perform a civil seizure of a shipment under the Customs Act, the rights holder must obtain a court order, which requires detailed information on the shipment. However, Canada's Criminal Code allows for a public officer in the course of duty to seize any item discovered to be in violation of the law. For example, Customs can detain suspected counterfeit shipments and contact the Royal Canadian Mounted Police (RCMP), which can then proceed with investigation under criminal law. The Canadian government is considering ways to tighten border enforcement.

The majority of the pirated goods are high quality, factory produced products from Asia. Aside from pirated software, many stores sell and install circumvention devices, also made in Asia, that allow pirated products to be played in a legitimate console. Once pirated and counterfeit products clear Canadian Customs, enforcement is the responsibility of the RCMP and the local police. The RCMP lacks adequate resources, training and staff. Because Canadian laws are inadequate to address IPR issues, few prosecutors are willing or trained to prosecute the few cases that arise. Where an infringement case has gone to trial, the penalties imposed can be too weak to act as a deterrent; jail time is rarely imposed.

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Camcording

Unauthorized camcording in Canadian movie theaters is an increasing source of international DVD piracy. Although camcording with intent to distribute is considered a crime in Canada, the act of camcording in a theater is not a criminal offense. As Canadian prosecutors find it difficult to prove intent in such circumstances, Canadian law enforcement officials are often reluctant to pursue illicit camcording. Amending the Criminal Code to make the act of camcording in a theater a criminal offense would help address this problem.

Pharmaceuticals

The U.S. pharmaceutical industry has raised concerns about the pricing of patented medicines in Canada and encourages Canada and the Patented Medicine Prices Review Board (PMPRB) to move towards a more market-based review system.

In October 2006, Canada published new data protection measures for pharmaceuticals. The regulations are designed to give new and innovative drugs eight years of market exclusivity, with an additional six months of exclusivity for innovative drugs that are the subject of pediatric studies.

SERVICES BARRIERS

Audiovisual and Communications Services

In 2003, the government of Canada amended the Copyright Act to ensure that Internet retransmitters are ineligible for the compulsory retransmission license until the Canadian Radiotelevision and Telecommunications Commission (CRTC) licenses them as distribution undertakings. Internet "broadcasters" are currently exempt from licensing.

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 CRTC, implements this policy. The CRTC requires that for Canadian conventional, over-the-air broadcasters Canadian programs must make up 60 percent of television broadcast time overall and 50 percent during evening hours (6 p.m. 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 television and direct to home broadcast services, a preponderance (more than 50 percent) of the channels received by subscribers must be Canadian programming services.

Non-Canadian channels must be pre-approved ("listed") by the CRTC. For other services, such as specialty television and satellite radio 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 not show popular foreign feature movies between 7 p.m. and 11 p.m. The only non-Canadian films that may be 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.

Until 1997, CRTC policy in cases where a Canadian service was licensed in a format competing with that of an authorized non-Canadian service was to revoke the license of the non-Canadian service if the new Canadian applicant so requested. In July 1997, the CRTC announced that it would no longer be

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"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 the CRTC will consider removing existing non-Canadian services from the list, or shifting them into a less competitive location on the channel dial, if they change format to compete with a Canadian pay or specialty service.

Radiocommunication Act

A principal concern of the Canadian Cable Telecommunications Association (CCTA) is the spread of unauthorized use of satellite television services. Industry findings, extrapolated on a national basis, estimated that between 520,000 to 700,000 households within cabled areas use unauthorized satellite services. Any survey of the incidence of satellite signal 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 may be 1 million illegal users of U.S. satellite television systems in Canada, resulting in a significant annual loss to the legitimate satellite television 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 remainder subscribing via the "gray market" where the unauthorized user does in fact purchase the signal from a U.S. satellite company for the signal, but only by pretending to be a U.S. resident.

Telecommunications Services

In its schedule of WTO services commitments, Canada retained a 46.7 percent limit on foreign ownership for all facilities-based telecommunications service suppliers except fixed satellite services and submarine cables. 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). As a consequence of foreign ownership restrictions, U.S. firms' presence in the Canadian market as wholly U.S.-owned operators is limited to that of a reseller, dependent on Canadian facilities-based operators for critical services and component parts. This limits those U.S. companies' options for providing high quality end-to-end telecommunications services as they cannot own or operate their own telecommunications transmission facilities.

In 2004, the CRTC decided that telephone communication over the Internet (VoIP) should be subject to the same regulatory regime as conventional telephone systems. In November 2006, however, the new Conservative government overruled the CRTC and determined that Canada will not regulate "access independent" VoIP services, those services that can reach the customer through any broadband Internet connection. "Access dependent" VoIP services, which connect customers over the service provider's own network, are still subject to regulation.

Barriers to Film Exports

The 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 Motion Picture Association members must submit product destined for theatrical release.

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Most of these boards also classify product intended for home video distribution. As a control device to display a video's Quebec classification, the Quebec 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 Quebec.

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, Quebec 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 Quebec 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 screens new or expanded foreign investment in the energy and mining, banking, fishing, publishing, telecommunications, transportation, film, music, broadcasting, cable television and real estate sectors.

Investment Canada Act

The Investment Canada Act has regulated foreign investment in Canada since 1985. Foreign investors must notify the government of Canada prior to the direct or indirect acquisition of an existing Canadian business of substantial size (as defined below). The Canadian government also reviews acquisitions by non-Canadians of existing Canadian businesses or establishments or of new Canadian businesses in designated types of business activity relating to Canada's culture, heritage or national identity 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; is in a business that is identified by regulation to be culturally sensitive; or is in uranium production, financial services or transportation services; or
- Acquire indirect control over 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.

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In 2006, the review threshold for WTO Members was set at C\$265 million, rather than the C\$5 million level applicable to non-WTO investors. In 2007, the review threshold is expected to be C\$281 million. The WTO exemption does not include investments in production of uranium, financial services, transportation services or a cultural business. The dollar threshold varies year-to-year and is a function of Canadian gross domestic product. There is no review process for indirect acquisition of a Canadian business by investors of any Member of the WTO, with the exception of foreign acquisitions of any size in "cultural industries" (publishing, film, music, etc.).

Industry Canada is the reviewing authority for most investments, except for those related to cultural industries, which come under the jurisdiction of Heritage Canada. The ICA sets time limits for the reviews. The Minister of Industry has 45 days to determine whether or not to allow a proposed investment. The Minister can unilaterally extend the 45 day period by an additional 30 days by sending a notice to the investor prior to the expiration of the initial 45 day period. Further extensions are permitted if both the investor and the Minister agree to the extension. In practice, Canada allows most transactions to proceed, though in some instances only after prospective investors have agreed to fulfill certain conditions.

Publishing Policy

Foreign investors may directly acquire Canadian book publishing firms only under certain 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 book publishing and distribution businesses continues to be prohibited, except in extenuating circumstances, such as when the business is in clear financial distress and Canadians have had "full and fair" opportunity to purchase.

Film Industry Investment

Canadian law prohibits 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.

GOVERNMENT PROCUREMENT

As a party to the WTO Agreement on Government Procurement (GPA), Canada allows U.S. suppliers to compete on a non-discriminatory basis for its federal government contracts covered by the GPA. However, we have continuing concerns that Canada has not yet opened "sub-central" government procurement markets (i.e., procurement by provincial governments). 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 in its GPA commitment, 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 U.S. Government 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.

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