

CANADA

TRADE SUMMARY

The U.S. goods trade deficit with Canada was \$32.5 billion in 2012, down \$2.0 billion from 2011. U.S. goods exports in 2012 were \$291.8 billion, up 3.9 percent from the previous year. Corresponding U.S. imports from Canada were \$324.2 billion, up 2.8 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 \$56.1 billion in 2011 (latest data available), and U.S. imports were \$28.0 billion. Sales of services in Canada by majority U.S.-owned affiliates were \$117.3 billion in 2010 (latest data available), while sales of services in the United States by majority Canada-owned firms were \$68.9 billion

The stock of U.S. foreign direct investment (FDI) in Canada was \$319.0 billion in 2011 (latest data available), up from \$289.5 billion in 2010. U.S. FDI in Canada is led by the nonbank holding companies, manufacturing, and finance/ insurance sectors.

The North American Free Trade Agreement

The North American Free Trade Agreement (NAFTA), signed by the United States, Canada, and Mexico (“the Parties”), entered into force on January 1, 1994. At the same time, the United States suspended the United States-Canada Free Trade Agreement, which had entered into force in 1989. Under the NAFTA, the Parties progressively eliminated tariffs and nontariff barriers to trade in goods among them, provided improved access for services, established strong rules on investment, and strengthened protection of intellectual property rights. After signing the NAFTA, the Parties concluded supplemental agreements on labor and environment, under which the Parties are, among other things, obligated to effectively enforce their environmental and labor laws. The agreements also provide frameworks for cooperation among the Parties on a wide variety of labor and environmental issues.

In 2012, Canada and Mexico became participants in the Trans-Pacific Partnership (TPP) negotiations, through which the United States and 10 other Asia-Pacific partners are seeking to establish a comprehensive, next-generation regional agreement to liberalize trade and investment. This agreement will advance U.S. economic interests with some of the fastest-growing economies in the world; expand U.S. exports, which are critical to the creation and retention of jobs in the United States; and serve as a potential platform for economic integration across the Asia-Pacific region. The TPP agreement will include ambitious commitments on goods, services, and other traditional trade and investment matters. It will also include a range of new and emerging issues to address trade concerns our businesses and workers face in the 21st century. In addition to the United States, Canada and Mexico, the TPP negotiating partners currently include Australia, Brunei, Chile, Malaysia, New Zealand, Peru, Singapore, and Vietnam.

IMPORT POLICIES

Tariffs

Canada eliminated tariffs on all industrial and most agricultural products imported from the United States on January 1, 1998, under the terms of the NAFTA. Canada has been phasing out the remaining MFN tariffs on imported machinery and equipment and intends to complete this process by 2015.

Agricultural Supply Management

Canada uses supply management systems to regulate its dairy, chicken, turkey, and egg industries. Canada's supply management regime involves production quotas, producer marketing boards to regulate price and supply, and tariff-rate quotas (TRQs). Canada's supply management regime severely limits the ability of U.S. producers to increase exports to Canada above the TRQ levels and inflates the prices Canadians pay for dairy and poultry products. One of the barriers facing U.S. exports of dairy products is a 245 percent *ad valorem* tariff on breaded cheese sticks. The United States is pressing for expanded in-quota quantities for these products.

Canada's compositional standards for cheese entered into force on December 14, 2008, and further restrict U.S. access of certain dairy products to the Canadian dairy market. These regulations limit the ingredients that can be used in cheese making, set a minimum for raw milk in the cheese making process, and make cheese importers more accountable for ensuring that the imported product is in full compliance. The regulations also are applicable to cheese that is listed as an ingredient in processed food.

Canada announced in 2008 its intention to implement the Special Safeguard (SSG) under the WTO Agreement on Agriculture for supply-managed goods. The SSG is a provision that would allow additional duties to be imposed on over-quota trade when import volumes rise above a certain level, or if prices fall below a certain level. Canada continues to work on the details of this mechanism and monitor over-quota trade, but has not established a timeframe for announcing the SSG price and volume triggers.

The Canadian Wheat Board

The United States has had longstanding concerns about the monopolistic marketing practices of the Canadian Wheat Board. Canada passed the *Marketing Freedom for Grain Farmers Act* in 2011 to transition the Canadian Wheat Board from a crown corporation to a commercial entity over a five-year period. The legislation allowed Western Canadian farmers to sell wheat on the open market beginning August 1, 2012.

Since the changes brought about by the Marketing Freedom for Grain Farmers Act are important to stakeholders involved in U.S.-Canada trade of grains and oilseeds, several not for profit associations from both the United States and Canada created a task force in order to provide information to facilitate the marketing of grain and seed between the United States and Canada.

Restrictions on U.S. Grain Exports

Canada has varietal registration requirements for wheat and barley. Canada eliminated a portion of the varietal controls in 2008 by no longer requiring that each registered variety of grain be visually distinguishable based on a system of Kernel Visual Distinguishability (KVD). This KVD requirement limited U.S. export access to Canada's grain market because U.S. varieties are not visually distinct and cannot be registered for use in Canada. While this policy change is an improvement, it will take years before U.S. wheat varieties are able to complete the necessary field trials to determine whether they will be registered for use in Canada. In the meantime, due to "grown in Canada" requirements, U.S. wheat, regardless of quality, will continue to be sold in Canada as "feed" wheat at sharp price discounts compared to Canadian varieties. U.S. members of the task force described above would like to have a working group established to look at issues concerning varietal declarations and foreign origin. Legislation to amend the Canada Grains Act is currently under consideration in the Canadian Parliament.

Restrictions on U.S. Seeds Exports

Canada's *Seeds Act* prohibits the sale, advertising for sale in Canada, or importation into Canada of seed varieties that are not registered in the prescribed manner. In order to apply for seed varietal registration, which is a long and cumbersome process, the applicant must reside permanently in Canada. This poses a trade barrier for the many U.S. seeds that are not one of the registered Canadian varieties. Wheat and barley seeds, among others, are covered under the *Seeds Act*.

Personal Duty Exemption

On June 1, 2012, Canada increased the cross-border shopping limit for tax-free imports of goods purchased in the United States. Canadians who spend more than 24 hours outside of Canada can now bring back C\$200 worth of goods duty-free (the previous limit was C\$50). Canada raised the duty-free limit for trips over 48 hours to C\$800, an increase from a C\$400 limit for stays of up to one week and a C\$750 limit for stays longer than seven days. The United States provides similar treatment for its returning travelers, but with a much more generous limit of \$200 of duty-free goods after visits of less than 24 hours. However, the United States will continue to press Canada on the lack of parity in the personal duty exemptions for day shoppers. Canada currently provides no duty-exemption for returning residents who have been out of Canada less than 24 hours.

Wine and Spirits

Most Canadian provinces restrict the sale of wine and spirits through province-run liquor control boards. Market access barriers in those provinces greatly hamper exports of U.S. wine and spirits to Canada. These barriers include cost-of-service mark-ups, listings, reference prices, labeling, discounting, distribution and warehousing policies. As noted above, Canada increased its personal duty exemption limit in June 2012. However, Canadian tourists still face high provincial taxes on personal imports of U.S. wines and spirits upon their return to Canada from the United States, which inhibit their purchases of U.S. alcoholic beverages.

SOFTWOOD LUMBER

On January 23, 2012, the United States and Canada signed an agreement to extend the Softwood Lumber Agreement (SLA) for an additional two years, until October 13, 2015. The SLA entered into force on October 12, 2006 and was set to expire after October 12, 2013. The 2006 SLA settled extensive litigation and resulted in the revocation of U.S. antidumping and countervailing duty orders on softwood lumber from Canada. The SLA is designed to create a downward adjustment in Canadian softwood lumber exports to the United States through the imposition of Canadian export measures when U.S. demand is low. The SLA also provides for binding arbitration to resolve disputes regarding interpretation and implementation of the agreement. Under the SLA, arbitration is conducted under the rules of the LCIA (formerly the London Court of International Arbitration). The bilateral Softwood Lumber Committee, established pursuant to the SLA, meets to discuss a range of implementation issues and Canadian provincial assistance programs for softwood lumber industries. The Softwood Lumber Committee last met in October 2012, in Quebec City.

On July, 18, 2012, a tribunal issued its finding in an SLA dispute regarding the apparent underpricing of timber in the interior of British Columbia. At issue was whether British Columbia was justified in selling increasing amounts of publicly-owned timber in its interior – most of which was used to make softwood lumber products – at salvage rates. While the tribunal acknowledged the dramatic increase in the amount of timber sold at salvage prices, and reviewed a number of actions by British Columbia that the United States had explained helped account for that increase, the tribunal did not find a conclusive link between

the increase and actions taken by British Columbia. British Columbia has issued an update with regard to its timber pricing systems and the United States will be monitoring the resulting pricing closely.

Canada continued to collect duties in 2012 resulting from a 2011 arbitration award under the SLA. A tribunal convened under the LCIA found that certain provincial assistance programs in Quebec and Ontario provide benefits to the Canadian softwood lumber industry in breach of the SLA, and Canada has imposed additional export charges to collect \$59.4 million as compensation for this breach. Canada began collecting the additional charges on March 1, 2011.

DOMESTIC SUPPORT MEASURES

Aerospace Sector Support

Canada released a comprehensive review of its aerospace and space programs in November 2012. The review offered 17 recommendations intended to strengthen the competitiveness of Canada's aerospace and space industries and guide future government involvement in both sectors. Recommendations called on the Canadian government to create a program to support large-scale aerospace technology demonstration, co-fund a Canada-wide initiative to facilitate communication among aerospace companies and the academic community, implement a full cost-recovery model for aircraft safety certification, support aerospace worker training, and co-fund aerospace training infrastructure.

The review also recommended that the Canadian government continue funding the Strategic Aerospace and Defense Initiative (SADI). The SADI provides repayable support for strategic industrial research and pre-competitive development projects in the aerospace, defense, space, and security industries, and has authorized over \$827 million to fund 26 advanced research and development (R&D) projects since its establishment in 2007.

The Canadian federal government and the Quebec provincial government announced aid to the Bombardier aircraft company in 2008 not to exceed C\$350 million (federal) and C\$117 million (provincial) to support research and development related to the launch of the new class of Bombardier C-Series commercial aircraft. According to the Public Accounts of Canada, the federal government has disbursed C\$203 million dollars to Bombardier from April 2008 through March 2012. The United States continues to express its concerns to the government of Canada that any launch aid associated with the C-Series must be consistent with Canada's international trade obligations.

The United States also has expressed concern over the possible use of Export Development Canada (EDC) export credit financing to support commercial sales of Bombardier C-Series aircraft in the U.S. market. The United States continues to urge the government of Canada to refrain from distorting market competition in accordance with the purpose and principals of the OECD Aircraft Sector Understanding (ASU).

Canada committed approximately \$3.25 million per year from 2009 to 2013 to support the Green Aviation and Research and Development Network and provides additional funding to the National Research Council's Industrial Research Assistance Program to support R&D in Canada's aerospace sector.

Risk Management Programs for Canadian Pork Producers

Canada provides an array of business risk management programs for its pork producers. The AgriStability program provides financial assistance to producers when income falls below 70 percent of a producer's

limited historical reference margin¹, at a compensation rate of 70 percent. This reflects adjustments to the program that will be effective as of April 2013. The AgriInvest program aims to cover small income declines by providing matching government funds based on producer contributions. It is essentially a producer-government savings account. Both AgriStability and AgriInvest are cost-shared 60/40 by the federal and provincial governments, respectively.

Provincial governments also provide significant subsidies in the form of price stabilization programs and preferential loans and loan guarantees. Quebec's Farm Income Stabilization and Insurance Program (ASRA) provides direct payments to hog farmers. The ASRA program is designed to guarantee a positive net annual income. One-third of the premium comes from producer participants and two-thirds comes from the Quebec government.

Ontario established a price protection program similar to ASRA, called the Ontario Risk Management Program (ORMP), in June 2011. The support level directly relates to the cost of production (a greater cost of production translates into a greater support level). The program offers producer support of 40 percent from the Ontario government. The federal government does not participate, because of trade related concerns.

The United States will continue to raise these issues with Canada, including in the U.S.–Canada Consultative Committee on Agriculture.

Ontario Feed-In Tariff Program

In December 2012, a WTO panel found that Canada breached its obligations under the *General Agreement on Tariffs and Trade 1994*, due to particular local-content requirements in Ontario's *Green Energy and Green Economy Act of 2009* ("Green Economy Act") that treat imported equipment and components less favorably than domestic products (*see Canada – Certain Measures Affecting the Renewable Energy Generation Sector* (WT/DS412) and *Canada – Measures Relating to the Feed-In Tariff Program* (WT/DS426)). On February 5, 2013, Canada appealed the panel reports in both disputes to the WTO Appellate Body. Japan and the European Union each brought the dispute in 2011 against certain provisions of Ontario's feed-in tariff program that require the use of renewable energy generation equipment made in Ontario, to the exclusion of competing products, including clean energy equipment manufactured in the United States. The United States participated in the dispute as a third party. A Texas-based renewable energy firm initiated an investor-state claim under NAFTA chapter 11 against Canada in July 2011, claiming the Green Economy Act violates Canada's obligations under the NAFTA to provide investors with fair and equitable treatment.

Port Hawkesbury Paper Mill

The United States is investigating the nature and extent of assistance provided by the Province of Nova Scotia to the Port Hawkesbury paper mill following a bankruptcy settlement that resulted in the sale of the mill to a Canadian firm. Provincial assistance provided through the settlement has made possible the continuation of significant productive capacity that otherwise would not exist.

¹Under the Agristability and Agrinvest programs, "margin" refers to a producer's allowable revenue less allowable expenses. The historical reference margin is calculated as the average program margin in three of the past five years, with the highest and lowest years dropped.

GOVERNMENT PROCUREMENT

Canada is a signatory to three international agreements relating to government procurement (the WTO Agreement on Government Procurement (GPA), the NAFTA, and the 2010 United States-Canada Agreement on Government Procurement). The agreements provide U.S. businesses with access to procurement conducted by most Canadian federal departments and a large number of provincial entities. However, U.S. suppliers have access under trade agreements to procurement of only seven of Canada's Crown Corporations.

INTELLECTUAL PROPERTY RIGHTS PROTECTION

Canada has been included since 2009 on the Special 301 Priority Watch List. The 2012 report cited concerns related to Canada's copyright laws, border enforcement, and failure to implement the World Intellectual Property Organization (WIPO) Internet Treaties, which Canada signed in 1997. Canada's enforcement against trade in counterfeit goods remains insufficient. On June 29, 2012, Canada adopted the *Copyright Modernization Act*. The Act will come into force following additional legislative procedures and regulatory action. The United States urges Canada to enact further legislation to give customs officers *ex officio* authority to take action against counterfeit and pirated goods.

Canada, the United States and other key trading partners, signed the Anti-Counterfeiting Trade Agreement (ACTA) in October 2011. Canada has yet to ratify the agreement, but introduced domestic legislation to meet its ACTA commitments. ACTA establishes an international framework that will assist parties in efforts to effectively combat the infringement of intellectual property rights, in particular, the proliferation of counterfeiting and piracy, which undermines legitimate trade and the sustainable development of the world economy.

U.S. stakeholders also have expressed strong concerns about Canada's current administrative process for appeals of the regulatory approval of pharmaceutical products, and limitations in Canada's trademark regime. In addition, recent decisions by Canadian courts regarding pharmaceutical patents have raised concern in the U.S. pharmaceutical industry. In November 2012, one U.S. pharmaceutical company formally served a notice of intent to submit a claim to arbitration under NAFTA Chapter 11, stemming from a Canadian court's decision invalidating the company's patent. Also in November 2012, the Supreme Court of Canada held that another U.S. pharmaceutical company's patent covering a major pharmaceutical product was void.

SERVICES BARRIERS

Telecommunications

Canada maintains a 46.7 percent limit on foreign ownership of suppliers of facilities-based telecommunications services, except for submarine cable operations. This is one of the most restrictive regimes among developed countries. Canada also requires that at least 80 percent of the members of the board of directors of facilities-based telecommunications service suppliers be Canadian citizens. As a consequence of these restrictions on foreign ownership, 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. 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). This limits those U.S. companies' options for providing high

quality end-to-end telecommunications services, since they cannot own or operate their own telecommunications transmission facilities.

Canada amended the *Telecommunications Act* in June 2012 to rescind foreign ownership restrictions to carriers with less than 10 percent share of the total Canadian telecommunications market. Foreign-owned carriers are permitted to continue operating if their market share grows beyond 10 percent provided the increase does not result from the acquisition of, or merger with, another Canadian carrier. Canada announced in March 2012 that it would cap the amount of spectrum that large incumbent companies could purchase at the next spectrum auction in an effort to facilitate greater competition in the sector. Canada has announced it will hold the next 700 MHz spectrum auction on November 13, 2013, to be followed by the 2500 MHz spectrum auction within a year.

In 2009, a cell phone service provider with significant U.S. financial backing was permitted to acquire wireless spectrum rights in Canada. This represented a rare new entry into a telecom sector dominated by several large Canadian-owned firms. The provider has since faced numerous legal challenges from its competitors, who claim that the company violates the Canadian ownership requirements in the *Telecommunications Act*, because a foreign conglomerate controls a majority of its debt. Canada's Federal Court of Appeal ruled in the provider's favor in June 2011, securing the company's right to operate in Canada. An appeal against this decision was filed to the Supreme Court of Canada; however, the Supreme Court announced it would not hear the case in April 2012.

Canadian Content in Broadcasting

The Canadian Radio-television and Telecommunications Commission (CRTC) imposes quotas that determine both the minimum Canadian programming expenditure (CPE) and the minimum amount of Canadian programming that licensed Canadian broadcasters must carry (Exhibition Quota). Large English language private broadcaster groups have a CPE obligation equal to 30 percent of the group's gross revenues from their conventional signals, specialty and pay services. The Exhibition Quota for all conventional broadcasters is fixed at 55 percent Canadian programming as part of a group, with a 50 percent requirement from 6 p.m. to midnight.

Specialty services and pay television services that are not part of a large English language private broadcasting group are subject to individual Canadian programming quotas (time or expenditure or both), which vary depending upon their respective license conditions.

For cable television and direct-to-home broadcast services, 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. Canadian licensees may appeal the listing of a non-Canadian service that 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.

The CRTC also requires that 35 percent of popular musical selections broadcast on the radio should qualify as "Canadian" under a Canadian government-determined point system.

INVESTMENT BARRIERS

General Establishment Restrictions

Under the *Investment Canada Act* (ICA), 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.

The ICA 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. Canada reviews the acquisition by non-Canadians of existing Canadian businesses and the establishment 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 is in the public interest.

On December 7, 2012, Canada issued new rules to supplement its guidelines for investment by foreign state-owned enterprises (SOE), including the stipulation that future SOE bids to acquire control of a Canadian oil-sands business will be approved on an "exceptional basis only."

The threshold for review of investments/acquisitions by companies from World Trade Organization (WTO) Member States was \$330 million. Canada amended the ICA in 2009 to raise the threshold for review to \$1 billion over a four-year period. The new thresholds will come into force once regulations are drafted and published; however future bids by foreign SOEs will remain subject to the current \$330 million threshold. Industry Canada is the reviewing authority for most investments, except for those related to cultural industries, which come under the jurisdiction of the Department of Heritage. Foreign acquisition proposals under government review must demonstrate a "net benefit" to Canada to be approved. The ICA sets time limits for the reviews. Once an application for review is received, the Minister has 45 days to determine whether or not to allow the investment. A 30-day extension is permitted if the investor is notified prior to the end of the initial 45-day period. Reviews of investments in cultural industries usually require the full 75 days to complete.

The ICA was amended in June 2012 to allow the Industry Minister to disclose publicly that an investment proposal does not satisfy the net benefit test and publicly explain the reasons for denying the investment so long as the explanation will not do harm to the Canadian business or investor. Another amendment allows the Industry Minister to accept security payment from investors when found by a court to be in breach of their ICA undertakings. Canada also introduced guidelines that provide foreign investors with the option of a formal mediation process to resolve disputes when the Industry Minister believes a non-Canadian investor has failed to comply with a written undertaking.

Under the ICA, the Industry Minister can make investment approval contingent on meeting certain conditions such as minimum levels of employment and research and development. Since the global economic slowdown in 2009, some foreign investors in Canada have had difficulties meeting these conditions. Canada blocked a \$38.6 billion hostile takeover by an Australian company in 2010 of Potash Corp. of Saskatchewan as not being of "net benefit" to Canada under the ICA. This was only the second time an investment has been blocked since 1985. The United States has long expressed concerns that Canada's net benefit test is overly broad, lacks transparency, and has the potential to extend into every sector of the Canadian economy and to implicate issues unrelated to national security, such as competitiveness and protectionism.

OTHER BARRIERS

Cross-Border Data Flows

The strong growth of cross-border data flows resulting from widespread adoption of broadband-based services in Canada and the United States has refocused attention on the restrictive effects of privacy rules

in two Canadian provinces - British Columbia and Nova Scotia. These two provinces have laws mandating that personal information in the custody of a public body must be stored and accessed only in Canada unless one of a few limited exceptions applies. These laws prevent public bodies such as primary and secondary schools, universities, hospitals, government-owned utilities, and public agencies from using U.S. services when personal information could be accessed from or stored in the United States.

The Canadian federal government is consolidating information technology services across 63 email systems under a single platform. The request for proposals for this project includes a national security exemption which prohibits the contracted company from allowing data from going outside of Canada. This policy precludes some new technologies such as “cloud” computing providers from participating in the procurement process. The public sector represents approximately one-third of the Canadian economy, and is a major consumer of U.S. services. In today’s information-based economy, particularly where a broad range of services are moving to “cloud” based delivery where U.S. firms are market leaders, this law hinders U.S. exports of a wide array of products and services. The United States will continue seeking to work with Canadian authorities to identify means of addressing this issue.

Container Size Regulations

Canada announced in its 2012 budget that it would repeal standardized container size regulations for food products. The Canadian government has stated that these regulations do not provide a food safety benefit and that the elimination of such regulations would remove an unnecessary barrier for the importation of new products from international markets. The timeline for implementing the new regulations continues to be extended, however, and the regulations have not been repealed to date. The Canadian Food Inspection Agency announced in November 2012 its plans to launch formal consultations in 2013 as part of the regulatory amendment process. Existing regulations for food container sizes will remain in force until the review process is complete.