TRADE POLICY DEVELOPMENTS

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What is a Countervailable Subsidy?

In their recent preliminary determination of subsidizing of corn from the United States of America, Revenue Canada Customs laid out their criteria for determining whether a program confers a countervailable subsidy.

The concept of what is a subsidy, as defined in Subsection 2(1) of the Special Import Measures *Act* is very broad. Customs has applied certain internationally agreed rules in determining which subsidies are countervailable. They appear to be doing so without any specific statutory guidance. This may well lead to appeals in the future.

In determining whether a program constituted a countervailable subsidy in corn, three criteria were used: whether the program provided a financial or other commercial benefit; whether the program entailed a cost to the government providing the program; and whether the program was targeted.

In subsection 2(1) of the *Act* a subsidy is defined as any financial or other commercial benefit that has accrued or will accrue, directly of indirectly, to persons engaged in the production, manufacture, growth, processing, purchase, distribution, transportation, sale, export or import of goods. To be a countervailable subsidy, a program does not have to provide a benefit directly in respect of the subject goods. The program need only provide a benefit to the person engaged in one of the above activities related to the subject goods.

In determining whether a program constituted a countervailable subsidy, the Department has also taken into account principles which have been generally accepted internationally concerning generally available versus targeted government programs.

A program which is generally available is not considered to be a countervailable subsidy while a program which is targeted is considered to be a countervailable subsidy. The criteria for determining whether a program is generally available include: availability to all persons in an industrial section, e.g., agriculture; availability to similar persons across a range of industrial sectors, e.g., small business development; availability to more than one industrial sector; and general availability within the jurisdiction of the granting authority, e.g., a state or municipality. A program is considered to be targeted if, in design or effect: it is available only to certain enterprises; access to the program is limited; or certain enterprises are excluded from access to the program.

This is a much more restrictive interpretation than in the United States. Canadian officials are trying to avoid countervailing against practices and programs used in Canada. There would not, however, appear to any authority in SIMA to exempt "generally available" subsidies.

Government Slow to Amalgamate Injury Determining Bodies

In his Economic Statement of November, 1984, Finance Minister Wilson announced that Ministers had agreed in principle to amalgamate the Textile and Clothing, Tariff Board and Canadian Import Tribunal. Sources indicate that this has since been confirmed by Cabinet, subject

to officials developing rules about "direct petitioning".

Under existing legislation a surtax (Section 8, *Customs Tariff Act)* or a quota (Section 5 Export and Import Permits Act) can be introduced in respect of imports causing or threatening serious injury to production in Canada. However, the final decision on implementation is a Cabinet decision. And Cabinet has the discretion to determine whether or not a complaint will be referred to the Canadian Import Tribunal pursuant to Section 48 of *SIMA* for an enquiry about injury.

Industry would like to see direct petitioning as it exists in the U.S. system under Section 201 of the *Trade Act of 1974*. Some Canadian Ministers tend to agree with industry provided that such direct petitioning would not apply when on, preliminary review, the Tribunal concluded that the matter would better be addressed under the anti-dumping or countervailing duty provisions of the *Special Import Measures Act.* There would also be a provision for the Tribunal to consider whether or not "adjustment assistance" could be an alternative to protective measures. The aim is to preclude "frivolous" cases.

While Ministers appear to desire wider opportunities for direct access, certain trade officials are less than enthusiastic. Officials in some departments, notably DRIE, support the direct petitioning option. Others, in External and to a lesser extent Finance, are not anxious to see this option become a reality.

These officials for years have been controlling the process by limiting industry access to these provisions. There have been relatively few hearings under Section 18 of the *Anti-dumping Act* and fewer under Section 48 of *SIMA*. These well-meaning officials may, in some cases, be denying Canadian producers access to a process which might alleviate import competition causing serious injury. The decision about whether relief should be granted should rest with Ministers. Access to the system should not be governed by the whims of non-elected officials who brief ministers on these issues, and open the doors to the system only when political pressures build to the point they can no longer be resisted.

While industry may find it easier to access the system, direct petitioning may be a two edged sword. Actions such as the Japanese "voluntary" restraint on auto exports to Canada which were negotiated by Cabinet instruction, without public inquiry, would be brought within the system. And complainants may find that instead of protection, the Tribunal recommends adjustment assistance.

What is Covered by Customs' Preliminary Determinations of Dumping and/or Subsidization

When Customs issues a preliminary determination of dumping or subsidization of significant magnitude, importers/and exporters quite understandably may try to find ways to stay in business by importing closely related products.

Customs tend to look through such attempts and apply anti-dumping or countervailing duties to imports of the "sham" products. They may not be on solid ground in so doing, but this will only be resolved on appeal.

The anti-dumping or countervailing duties should apply only to goods in the product definition at initiation and in the preliminary and final determinations of dumping and/or subsidization.

In **Alpine ski-poles**, the Department took the position that if components were imported for simple assembly in Canada, even if they were imported in separate consignments, anti-dumping duties would apply.

In their notice of acceptance of an undertaking in respect of certain **oil and gas well casings** originating in or exported from Japan, Revenue Canada noted that "green tubes" were not covered by their product definition. Green tubes must be heat treated, quenched and

tempered in order to be usable according to certain API (American Petroleum Institute) specifications.

As the complainant and the Department had limited the product definition to casings meeting certain API specifications, these "green tubes" were clearly outside the scope of the investigation.

In **corn** from the USA the definition changed several times. At initiation on July 2, 1986, the Department referred to grain corn in all forms excluding seed corn, sweet corn and popping corn. They went on to note that the complainants were not interested in products such as corn flour and corn meal.

On November 14, 1986 the Department qualified the product definition as follows:

> The Department has received a number of enquiries concerning the range of goods subject to the application of provisional duties. These enquiries relate to goods such as corn screenings, crushed corn, ground corn, rolled corn, sliced corn, cracked corn, mixed feeds containing corn and cereal products containing corn.
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> The full product definition in this case is, "grain corn in all forms, excluding seed corn, sweet corn and popping corn originating in or exported from the United States of America". The Department's interpretation of the phrase "grain corn in all forms" is that it includes only those goods which are properly classified under tariff item 5500-1, Indian corn, or tariff item 5501-1, Yellow dent corn. Goods which are properly classified under any other tariff item are not considered to be subject goods for purposes of the mentioned preliminary determination.
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> For further clarifications, tariff items 5500-1 and 5501-1 include only whole grain, i.e., only grain corn that has kernel fully intact. The types of goods mentioned in paragraph two above and any other grain corn which has received further processing would not fall within the scope of this investigation and therefore would not be subject to the payment of provisional duty.

On December 1, 1986 the Department again clarified its position in order to neutralize several attempts to create products which appeared to be designed to avoid payment of the very substantial countervailing duty, and to bring the definition much more closely into line with the complainants initial intention. They stated:

> Prior to the preliminary determination of subsidizing and the consequent imposition of provisional duty, the market for corn used as animal feed or in the production of animal feeds consisted primarily of trading in shelled corn. On this basis the Department interpreted the phrase 'grain corn in all forms' as covering grain corn where the kernels had not been fragmented by any processing operation such as grinding, crushing or cracking, except for that occasioned by normal handling.
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> However, since the preliminary determination was made, there is a growing indication of a change in the marketing of grain corn from the United States. By performing certain simple processing operations on the corn or mixing it with other ingredients the resulting product may be claimed to be not subject goods for purposes of the assessment of provisional duty.
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> As a result of this marketing change, it is necessary to adjust our interpretation of the product definition. Accordingly, "grain corn in all forms" is held to include products where all of the constituent parts of the grain corn are present and those constituent parts comprise at least two thirds (2/3) of the entire product by weight. Goods considered to be subject to the provisional duty include those where the kernel is whole, cracked, crushed, ground, rolled, sliced or vitamin enriched, and corn screenings. Further, it includes grain corn in any of the foregoing forms when mixed with other ingredients where the grain corn comprises at least two thirds (2/3) by weight of the mixed product.
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> This interpretation will apply to all subject goods entered on and after November 7, 1986.

These developments underline the need for counsel to define the product carefully in terms of their clients' concerns, and to try to anticipate, through consultation with clients, how the product might be modified in order to avoid payment of anti-dumping or countervailing duties.

U.S. TRADE POLICY TRENDS

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Legislative Trends

Dead Trade Legislation

Congress was unable to bring a trade measure to the Senate floor in 1986. The Senate Finance Committee met on September 18 and 23 for consideration of a staff omnibus proposal, but could not arrive at a consensus on what to include in the trade package. Members of the Finance Committee appeared to lack the political will to pursue a trade bill in the face of the controversy that it aroused, and were preoccupied with various other matters that awaited action prior to adjournment, notably the tax bill and budget resolutions.

U.S. Customs User Fee

Although trade legislation was not enacted this session, a trade-related measure regarding a customs user fee was passed. The recently enacted fiscal 1987 *Budget Reconcilation Bill* creates a customs user fee of 0.22% *ad valorem* which will be imposed on imported merchandise that is formally entered, or withdrawn from warehouse for consumption. after November 30, 1986 and through to the end of fiscal year 1987 (September 30, 1987). The *ad valorem* rate will be lowered to 0.17% (and perhaps lower) after September 30, 1987 and through fiscal year 1989. The fees will not apply to imports subject to the Caribbean Basin Initiative preferences, imports from U.S. insular possessions, imports from the least developed developing countries, informal entries, or articles that are entitled to special treatment under schedule 8 of the Tariff Schedules of the United States.

These *ad valorem* fees will be paid by the importer of record, are tax deductible, and will be based on the value of the merchandise as determined under the appraisal provisions set out in the *Tariff Act of 1930*, 19 U.S.C. §1401a (1986) (as amended in 1979 and 1980 to bring U.S. valuation practices into line with the GATT Customs Valuation Code provisions).

These fees will be in addition to the processing fees required under the present law, and are scheduled to expire at the conclusion of fiscal year 1989. The fees are designed to reflect the actual costs to the U.S. Government for the commercial services provided by the U.S. Customs Service. In fiscal years 1988 and 1989, a special formula will allow fee reductions if necessary to ensure that revenues match actual costs.

Congress has directed the Commissioner of Customs to make certain that no new record keeping or data collection burdens are imposed upon the public, including all shippers, cargo-freight carriers, or related entities.

The Customs User fee has been strongly criticized and characterized as an import surcharge. Canada has filed a formal protest with the GATT (with the support of the E.E.C.) and the U.S. has agreed to consultations.

Buy American Procurement

The Department of Defense will be forced to buy only American or Canadian-made machine tools for use in defense-related facilities in fiscal 1987, according to a provision in the fiscal 1987 appropriations resolution. Supporters designed the amendment as a show of support for the industry and as a way to pressure the administration into rethinking its procurement practices.

Prospects for Trade Legislation in 1987

The results of the November U.S. elections increase the likelihood of passage of omnibus trade legislation in the next term. The Democrats regained control of the Senate by a margin of 55 to 45 seats, and maintained control of the House of Representatives. The new Senate majority

leader, Senator Robert Byrd (D-WV), has stated that trade legislation is a high priority issue now that tax reform is out of the way. There is currently a strong sentiment in Congress that the Administration has not been aggressive enough in dealing with the unfair trade practices of the major U.S. trading partners. Senator Lloyd Bentsen (D-Tx), who is the likely new chairman of the powerful Senate Finance Committee, has been a strong proponent of trade legislation in the past and he will likely pressure the committee to report a trade bill out sometime this spring. Senator Bentsen believes that the U.S. is facing a trade crisis and that legislative action is required to remedy the problem, although he stated on November 26 that he would not propose protectionist measures. He also stated his plans to visit Ottawa to discuss the U.S.-Canada trade negotiation.

Senator Max Baucus (D-Mont.), a leading member of the Senate Finance trade subcommittee, predicts that the next Congress is going to aggressively attack the U.S. trade deficit through tough trade legislation. According to Baucus, this legislation might include "looser" U.S. export controls, and reduced presidential authority to handle unfair foreign trade practices under Section 301. In addition, macroeconomic components of the trade imbalance and the issue of U.S. competitiveness in the world market will be the subject of legislation in the upcoming year.

Currently, it is unclear what approach the Democrats will take towards trade legislation, but any bill reported out will likely have stronger language than that contained in the former Republican-controlled Finance committee's staff draft. Senator Bentsen will reportedly seek bipartisan support for a bill in order to thwart a potential veto by President Reagan. Ultimately, the shift in power in the Senate will force the Administration to pay closer attention to trade issues, particularly since if all 55 Democrats voted to override a presidential veto of a trade bill, only 12 Republicans would be needed for a two-thirds majority. Finally, since the Administration will need "fast-track" negotiating authority from Congress at some point to enable it to participate fully in the new GATT round of talks, it must eventually approve a trade bill. The question is therefore not whether there will be a trade bill, but rather when a trade bill will emerge from Congress that is either acceptable to the Administration, or veto-proof.

TRADE LAW ACTIONS

Canada

Flowers

On October 29, Commerce preliminarily determined that fresh-cut flowers are being dumped at a margin of 11.33 percent for all Canadian companies. The preliminary determination on Canada was based on lack of adequate responses to the questionnaires by the (very small) Canadian exporters.

The recent set of preliminary antidumping determinations on cut flowers from countries other than Canada represents a significant development in the calculation of dumping margins because Commerce for the first time used its authority under Section 620(a) of the *Trade and Tariff Act of 1984* to look at the weighted averages of sale prices in the U.S., rather than each individual sale price. This has a very significant effect in reducing dumping margins, as can be seen in the following mathematical explanation.

COUNTRY	SALES IN U.S.	SALES IN FOREIGN
1 Widget	1.0	1.0
1 Widget	2.0	2.0
Weighted Average	1.50	1.50

Dumping margin, comparing each sale in U.S. to weighted average in foreign country: 16.7 percent.

Dumping margin, comparing weighted averages: zero.

Commerce based its use of weighted averages in the preliminary determinations on two factors: The extremely large number of transactions involved in the cases (260,000 sales in the U.S. during the period being investigated), and the perishability of the flowers, which causes prices to fluctuate enormously within a day or two on any given shipment, which would lead to the creation of unrealistically high dumping margins if compared on a sale-by-sale basis, since about-to-wilt flowers are sold at very low prices. The ideal solution for this particular problem would be an adjustment for differences in quality, but Commerce would consider that too difficult to quantify.

According to Commerce's preliminary countervailing duty determination on October 21, fresh-cut flowers from Canada are being subsidized at a rate of 0.52 percent. Commerce will issue its final CVD determination by January 5, 1987 and its final dumping determination by January 12, 1987. The ITC must render its final decision by February 26, 1987.

Brass Sheet and Strip

In its preliminary determination dated August 18, 1986, Commerce found that Canadian producers of brass sheet and strip were dumping by margins of 1.56-11.89%. Commerce will make its final determination by December 3, 1986, and the ITC will make its final injury determination by February 19, 1987.

Softwood Lumber

The Department of Commerce announced its preliminary determination on October 16 that Canada is subsidizing softwood lumber exports to the U.S. by a net rate of 15%. The Customs Service requires a cash deposit or bond on all imports of softwood lumber equal to the net subsidy. Commerce will issue its final countervailing duty ruling by December 30, 1986. The ITC is expected to issue its final decision on whether the imports materially injure or threaten material injury to the domestic industry by February 17, 1987.

Japan -- Semiconductors

On July 31, the Administration announced an agreement with Japan to enhance the sale of U.S. semiconductors to Japan and to prevent dumping of chips by the Japanese in both U.S. and third country markets. The Administration suspended the pending antidumping cases and the Section 301 investigation. (See September, 1986 issue)

Many feel that the accord reached set a precedent for other industries to seek "managed" agreements from the U.S. government. The agreement requires the Japanese and U.S. governments to monitor the prices of certain semiconductors sold in the U.S. and in third country markets in order to prevent dumping by the Japanese. It also gives a share of private Japanese companies' purchases of chips to private U.S. companies.

The U.S.-Japan semiconductor pact has received a great deal of criticism since its inception. Critics of the agreement, such as the European Economic Community, argue that the two countries have effectively cartelized world trade in semiconductors. In fact, the EEC is considering a dumping investigation on semiconductors from Japan. Meanwhile, U.S. electronics producers who utilize semiconductors in their products criticize the agreement because it raises the prices of chips in the U.S. thus making their industry uncompetitive compared to foreign terms. In addition, the U.S. semiconductor industry claims that the Japanese are still dumping in Japan and third countries.

Threatened Antitrust Suit in Response to Cement Dumping Cases

On October 30, U.S. cement producers filed an antidumping petition against eight countries -- Japan, Korea, Mexico, Venezuela, Columbia, Spain, Greece and France. The petition is controversial because 75 percent of the cement imports are brought in by U.S. producers, thus making it difficult for the domestic industry to prove injury. In addition, a group of U.S.

cement importers has threatened to bring a civil antitrust against the petitioners in response to the dumping suits. A representative of this group stated that "this action is one more example of how some U.S. producers continue to attempt to use the trade and environmental laws to discourage competition." The ITC is expected to make its preliminary injury determination by December 15, 1986.

USTR AND ITC HEARINGS ON U.S. - CANADA TRADE

The Office of the United States Trade Representative sponsored public hearings September 8 and 9 and accepted written comments on the economic effects of a free trade agreement with Canada. The hearings were chaired by the Office of the United States Trade Representative and the panel consisted of other staff-level representatives from several governmental agencies, including chief negotiator Peter Murphy. The goal of the hearings was to provide U.S. businesses with an opportunity to comment on the negotiations.

Spokesmen for many domestic industries presented their views during the sessions, including: footwear, energy chemicals, electronics, printing, minerals, lumber, autos, furniture, dairy and agriculture, computers and beverages. Most of these sectors accused Canada of unfair trade practices such as federal and provincial subsidies, high tariffs, and regulations restricting the entry of U.S. products. The spokesmen generally agreed that the free trade talks provide an ideal forum to discuss unfair trade practices, and urged the Administration to demand that these practices be eliminated through this process.

The International Trade Commission also held hearings on free trade with Canada on September 9 and 10. The comments provided to the ITC in large part paralleled those given to the USTR. The USTR requested that the ITC conduct an investigation on the economic effects of a free trade agreement with Canada, and to provide advice within six months. The ITC is expected to submit its recommendations to the USTR by January 2, 1987.

ITC Investigation on Services Trade

The International Trade Commission ("ITC") received limited public response to its request for written submissions regarding their Section 332 investigation assessing the implications of a free trade arrangement with Canada in services. The ITC is examining the magnitude of US-Canada trade and operations in selected services industries, the competitive postion vis-a-vis Canadian services industries with nontariff measures, and U.S. service industry priorities in such negotiations. The ITC only received submissions from the Manitoba Highway and Transportation Departments, the Transport Institute (waterborne transportation), and the Institute of International Container Lessors. Although the ITC received few public submissions, they have received satisfactory response to questionnaires sent out in September. Questionnaires were sent to leading firms in seven different services industries; including accounting, construction/engineering, computer data processing, advertising, insurance, motor transportation, and telecommunications. The ITC is expected to send its recommendations on services trade with Canada to the U.S. Trade Representatives by March 18, 1987.

USTR Indentified Trade Barriers

The Office of United States Trade Representative released a report on foreign barriers to U.S. exports entitled "National Trade Estimate: 1986 Report on Foreign Trade Barriers" in early November. Under Section 303 of the *Trade Act of 1984*, USTR must submit an annual report to Congress identifying and analyzing the most significant barriers to trade of major U.S. trading partners, in order to facilitate negotiations to reduce or eliminate such barriers. The barriers are described by country along with their distorting impact. In addition, the report outlines the steps

to be taken to eliminate barriers to U.S. trade in goods, services, investment and intellectual property.

USTR Clayton Yeutter indicated that this study will be used during the new round of trade talks under the General Agreement on Tariffs and Trade as a basis for negotiating stronger rules to liberalize world trade. In addition, Yeutter stated that the U.S. is challenging unfair trade barriers listed in the report "through the aggressive enforcement of U.S. laws and through bilateral and multilateral negotiations."

The following is a brief summary of Canadian trade barriers as described in the report:

Tariffs - Despite the large reduction since the Tokyo Round of negotiations, Canadian tariffs remain among the highest of all industralized nations. The U.S. is seeking bilateral elimination of all U.S. and Canadian tariff structures during the current free trade negotiations.

Provincial Liquor Boards - They maintain almost exclusive control of Canada's retail alcoholic beverage sales. U.S. beer, wine and distilled spirits suppliers allege that they have difficulty marketing their products in certain provinces due to certain "listing" practices, discriminatory markups, and limited access to distribution systems.

Canadian Wheat Board Licensing Requirements - The Canadian Wheat Board controls all wheat, oats, barley and related product imports into Canada by issuing import permits or licenses. U.S. exports are limited because permits are issued only when the product cannot be found in Canada.

Footwear The U.S. notified Canada it will seek compensation for extending Canadian footwear quotas against U.S. exports of women's and girl's footwear.

Plywood - Canada should adopt common North American prescriptive/performance standards for all wood-based structural panel products.

Government Procurement - Where GATT Government Procurement Code requirements do not apply, Canadian government entities favor Canadian-based firms through "buy national" or "buy local" policies.

Export Subsidies - Canada's *Western Grain Transportation Act* increases the number of subsidy-eligible products. The freight rate subsidy for certain grains and other feed products gives Canadian exporters a significant advantage in U.S. and third country markets.

Copyright Protection - Canada does not now protect domestic or foreign creators of motion pictures and other television programming against unauthorized cable system retransmissions of broadcast signals containing their works. The failure to protect these works deprives U.S. copyright owners of compensation or control over a significant form of commercial exploitation in Canada.

Compulsory Pharmaceutical Patents Licensing - The U.S. urges speedy passage of modifying legislation to address serious U.S. concerns about the inadequacies of Canadian patent protection for U.S. pharmaceutical interests.

Border Broadcasting - In 1976 Canada adopted a tax provision denying Canadian enterprises tax deductions for the cost of advertising in foreign media when the advertising is directed primarily at Canadians. The main targets of this legislations were ads placed on U.S. television stations beaming programs into Canada.

Restrictions on Canadian Advertising in U.S. Publications Canadian tax law prohibits Canadian advertisers from deducting the cost of advertising in foreign magazines, papers and broadcast media if such advertising is directed primarily at the Canadian market.

Trucking The entry standards for trucking in the U.S. are easier than in Canadian provinces.

Data Processing Requirements The U.S. is concerned with the Canadian law that requires banks to process and maintain Canadian bank operation records in Canada.

Unreasonable Investment Entry Restrictions The *Investment Canada Act* gives the Canadian government significant discretion to limit foreign investment and impose "voluntary" performance requirements on such investment. In addition, Canada pressures existing foreign investors to divest partial ownership to Canadians as a condition for approving indirect acquisitions of oil and gas subsidiaries by other foreign investors.

Lack of National Treatment - The U.S. is concerned with Canada's restrictive treatment of investment in culturally sensitive sectors.

Performance Requirements The U.S. is concerned with Canadian laws which extract commitments from foreign investors to favor Canadian suppliers.

Most of the above-mentioned trade barriers as well as others such as product standards will be included in the free trade negotiations. Resolution of some long-standing disputes is being pursued separately. Although this report cites several barriers to trade, this study is by no means an exhaustive list of trade "irritants" since it does not include such matters as Canadian duty remissions by auto parts.

FUTURE DEVELOPMENTS

Steel Restraints

Administration officials asked Canadian officials for consultations regarding a Voluntary Restraint Agreement ("VRA") on steel imports in response to pressure from the U.S. steel industry. This action was prompted by increases in steel imports in the first nine months of 1986 from countries who do not have a VRA. Canadian trade officials cited discrepencies in the U.S. import statistics.. as the reason for the sudden surge in steel imports.

The two sides have agreed to exchange data on a regular basis in order to minimize differences in import and export statistics. In addition, they told the U.S. officials that a VRA was not desirable and that they would take steps to keep Canadian steel imports at a reasonable level. Canadian integrated steel producers claim that the surge in imports is due to Canadian fabricators who buy raw steel from third countries, and they suggest that the Canadian federal government should tighten export rules on steel in order to reduce shipments to the U.S. USTR and Commerce officials are monitoring the level of imports to ensure that Canadian market share does not increase.