

## CANADIAN COMPETITION RECORD

**FEATURE ARTICLE**

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As we predicted in our previous annual **Strategico Report**, 1993 has proved to be the year free trade came of age. When the agreements negotiated this year are finally implemented, Canadian trade will move more freely than at any time over the past 150 years. Recent developments include the following:

- Capping seven years of negotiation, the Uruguay Round of the General Agreement on Tariffs and Trade (GATT) has agreed to reduce tariffs further and liberalize trade around the world, beginning on 1 July 1995.
- After intense debate, the North American Free Trade Agreement (NAFTA) has been approved by the legislatures in the three partner countries, and will enter into force on New Year's Day 1994.
- In this, its fifth year of operation, the benefits of the Canada-USA free trade agreement (FTA) have become increasingly apparent and incontestable.
- A number of major bilateral trade disputes continue to plague the Canada-USA relationship—lumber, steel, wheat—despite the efforts of the binational panels, as American unfair trade laws are applied unfairly.

In this, the fifth annual **Strategico Report** on free trade, we assess these developments and attempt to forecast future trends.

**Free Trade in Perspective**

In our strategic advice to Canadian corporate clients, we have found that it is essential to keep trade policies and negotiations in perspective. Canada depends on external markets for more than one-third of our total production and consumption. Trade is obviously of direct and vital importance. Trade also bears on the two principal and related problems on the national agenda: the lack of economic growth; and the mountain of debt overhanging federal and provincial governments.

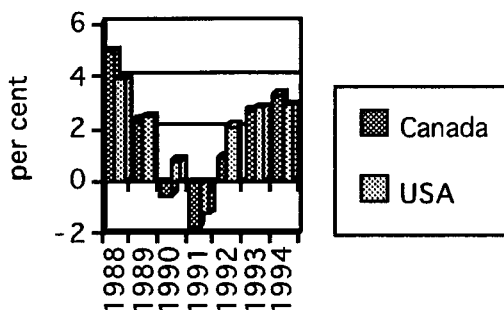
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Canada is only now emerging from the recession. After stagnating in 1990 and falling sharply in 1991, it was not until the middle of 1993 that output exceeded the pre-recession volume. Much of this output growth came through increased productivity, reflecting investment in machinery and equipment and the restructuring of plants, companies and whole sectors of industry to meet the international competitive challenge. This has left Canada with an unacceptably high and persistent level of unemployment. At the close of 1993, more than 1.5 million Canadians were without work, representing 11 per cent of the labour force. Despite signs of increased employment opportunity, we do not expect the unemployment rate will move into single digits for several years.

The Liberal Government, swept to power on 25 October 1993, hopes to stimulate the economy to increase unemployment. But the traditional fiscal policy prescription of keynesian deficit financing is foreclosed by the highly dangerous debt situation of the federal and provincial governments. Combined public debt exceeds the total annual output of the economy. An alarmingly high proportion of the provincial component is held in foreign currencies. Further deficit financing is thus out of the question. Indeed, we expect substantial government expenditure cuts, of the order of \$10 billion per annum federally and half that much in the provinces.

Canadians therefore find themselves in the position described by songwriter and poet Leonard Cohen, "Waiting for the Miracle to come." One possible "miracle" is the rapid upsurge of Canadian exports to meet the demand of foreign markets, particularly the United States. This has, to date, been the principal factor pulling Canada out of the depths of the recession.

Growth Rates of National Output

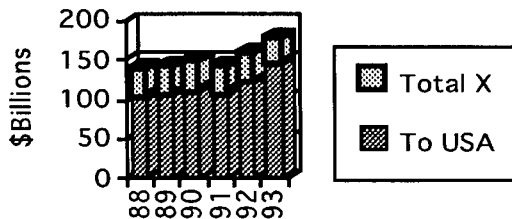


This strong showing should continue for at least another several years as the American economy expands relatively rapidly. For Canada to continue to profit from this opportunity, it will be essential to:

- maintain free access to the American market for goods and services;

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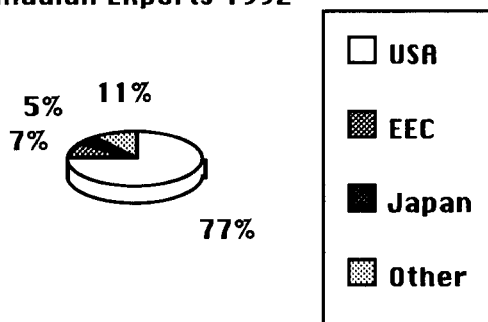
Canadian Exports



- secure that access, to the extent possible, from protectionist harassment by “fair trade” actions; and,
- above all, maintain Canadian competitiveness in production, marketing and distribution.

During this period, Canada must also seek improved access to other markets, in the Americas, in Europe and, above all, in Japan and other parts of Asia. Together, these other markets account for less than one-quarter of Canada’s exports. They remain significant, however, for their growth potential and the possibility of increased diversification of Canadian trade.

Canadian Exports 1992



### THE G.A.T.T.

The fundamental framework for this freer trade is the General Agreement on Tariffs and Trade, known as the GATT. The Uruguay Round of negotiations under the GATT was launched seven years ago. Finally, on 15 December 1993, this mammoth enterprise was completed in Geneva as 114 countries signed the agreement with appropriate fanfare. It is planned to enter into force in July 1995.

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To reach such a global agreement is an important achievement in itself. Despite all the hooplah, the results inevitably fall short of original hopes and expectations. Tariffs will be reduced, by around one-third at the end of five years. There has been some progress in working out new rules to govern trade in services, intellectual property rights and investment regulations.

These are of limited direct importance to Canada. After all, we already enjoy free trade in goods and significantly better rules on trade in services with the market taking more than 75 per cent of our exports, the United States. A more modest liberalization of access to markets accounting for the remaining one-quarter of our trade is not to be neglected, but it is hardly revolutionary.

### 1. Trade in Agriculture

On the two issues of greatest importance to Canada, the results are most unsatisfactory. The first is agricultural trade. Canada joined with other major agricultural exporters, the so-called Cairns Group, in pressing for the dismantling of the export subsidy arsenal that has so disrupted world agricultural markets. The main protagonists, the United States and the European Union, have clashed on this issue throughout the negotiations.

In the end, the subsidy disciplines will be much more modest than originally demanded. The Europeans (notably the French) will actually be permitted to increase their exports of subsidized grains for the first few years under the deal. This is a painfully hollow victory.

Meanwhile, Canada was reasonably successful in protecting the supply management systems designed to protect domestic producers of dairy and poultry products. For the first seven years of the negotiations, these producers demanded and their representatives pledged that the supply management systems would be protected under a strengthened GATT Article XI. At the close of the negotiations, it became apparent that the Canadian position was isolated and indefensible. (**Strategico** was called in at this point to advise certain of these industries on salvaging what they could.)

The result of the negotiations was to replace the traditional system of quotas with a new regime of tariffs designed, initially, to offer the equivalent level of protection. These tariffs will be reduced progressively by a total of 15 per cent over the next six years. The consequence will be that there will be no need for dramatic restructuring of the Canadian supply managed industries before the year 2001.

This despite a last minute claim by the Americans that these tariffs should be governed not by the GATT but by the FTA schedule and thus eliminated entirely by 1998. The proposition is patently absurd. In agreeing to tariffication, both Canada and the United States have accepted the GATT schedule for tariff reduction for those commodities previously protected under GATT Article XI. This protection does not apply to American restrictions on sugar and peanut butter nor, arguably, Canadian ice cream and yogurt.

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<b>Tariff Equivalents for Supply Managed Commodities</b>		
	<b><u>1995</u></b>	<b><u>2001</u></b>
<b>Eggs</b>	<b>192</b>	<b>163</b>
<b>Chicken</b>	<b>280</b>	<b>238</b>
<b>Milk</b>	<b>283</b>	<b>241</b>
<b>Butter</b>	<b>351</b>	<b>298</b>

### 2. Unfair Trade Rules

The second issue of critical importance to Canada is the system of trade rules under the GATT. These rules lay the basis for national legislation. They establish the starting point for negotiation of improved arrangements within free trade areas. Canada led the way by proposing a permanent Multilateral Trade Organization (MTO), to replace the "transitional" (45 year old) institutions of the GATT. The GATT rules would be applied by panels, modeled after the FTA mechanisms, whose decisions would for the first time be binding on member governments. Finally, the rules themselves would be substantially improved. There was even some hope that these improvements would be sufficient to eliminate the need for the working party negotiations under the NAFTA.

It became increasingly obvious that this was wishful thinking. The Americans were reluctant from the start to engage in serious commitments in this area. As late as the beginning of December, they launched a major counter-offensive designed to gut these proposals, scrapping the MTO, weakening the panel system and leaving the rules unchanged for the application of anti-dumping duties. The result is significant progress but falls well short of Canadian ambitions:

- a permanent institution will be established under the name of the World Trade Organization
- the dispute settlement process will become more automatic in setting up panels and in requiring compliance with the panel determinations
- at American insistence, however, the panels will be barred from "second-guessing" the administrators by assessing the facts for themselves
- the rules on applying countervailing duties will be improved significantly by outlawing such duties against
  - research and development grants
  - regional development assistance
  - assistance worth less than 1 per cent of sales
- these rules will protect provincial as well as federal programs that fall under these permitted categories
- the rules on anti-dumping duties have been very little changed in the face of American intransigence

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It is too early to assess the value of these changes. The move to a permanent institution with greater authority is clear progress. But it will be only as good as the rules it has to administer. On the issue of countervailing duties against subsidies, the improvements appear to be significant. On anti-dumping, the American protectionists have clearly won a major victory in defending their continuing capacity to harass legitimate imports—at enormous cost to American consumers.

### **3. Reduction of Tariffs**

The most tangible benefit to Canadian producers comes through the reduction of tariffs in foreign markets, notably in Europe and Asia. To put this in perspective, the total value of the tariffs taken off Canadian exports to foreign countries by the end of the transition period will be a fraction of the total value eliminated under the Canada-USA agreement.

Meanwhile, our preferential advantage in the far more important North American market (Canada, the United States and Mexico), will also be reduced by one-third in the Uruguay Round. In other words, our European and Japanese competitors will be able to attack those markets over lower tariff walls. It is far from clear that Canadian producers gain more (from access to overseas markets) than they will lose (from reduced protection in North America).

### **4. Overall Impact on Canada**

Analysis by the Organization for Economic Cooperation and Development suggested the benefit to Canada would be of the order of US\$4 Billion over the next 10 years. This is equivalent to about 0.1 per cent per annum added to national income, a not insignificant gain. This is roughly one-fifth the benefit imputed to the FTA.

The politics of the GATT deal are obviously much more attractive than the objective results. There is genuine concern that Canada has become much too dependent on the well-being, and the goodwill, of a single economic partner. We attach high importance to increased diversification of our markets through expanded exports to Europe and Asia. Of course, this over dependence is the direct result of our success in penetrating the American market and their willingness to accept our products. If their market were closed, we would become much more diversified—and much poorer—as a direct result.

**The real significance of the GATT deal lies in the framework it will continue to provide for future trade relations among the three major regions—Europe, Japan Asia and the Americas.**

With the GATT, there is at least some scope for trade to proceed under agreed rules. Without GATT, there would be the prospect of destructive trade wars resulting in managed trade in which a country like Canada

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would be among the biggest losers, despite the protections of our own regional arrangements, the Canada-USA free trade agreement and the NAFTA.

### **The NAFTA**

The North American Free Trade Agreement will come into force on 1 January 1994. It has not been without controversy. During his election campaign, Bill Clinton had been critical of the NAFTA's lack of protection against bidding for investment through lax enforcement of environmental or labour standards. Once elected, President Clinton assigned his U.S. Trade Representative, Mickey Kantor, to negotiate side agreements to the NAFTA to address this issue.

It soon became evident that a hidden purpose of such side agreements was to provide a pretext for re-introducing tariff barriers and other restrictions against imports from Mexico. Canada risked being caught up in such a system. Eventually, Mexico and the United States agreed to permit trade sanctions against their exports if elaborate NAFTA machinery found them systematically guilty of non-enforcement of standards. After protracted and heated negotiations, Canada obtained arrangements under which the enforcement of environmental and labour standards was left to the Canadian courts. Furthermore, the provisions of the agreement would not apply to most Canadian firms and workers unless and until Ontario and a number of other provinces decided to accede to the accord—which is not an immediate likelihood. This was a significant—if purely defensive—negotiating victory for Canada.

### **1. The NAFTA Debate**

In the NAFTA as negotiated, Canada had agreed to release the United States from the FTA commitment to negotiate a new, bilateral set of trade rules to replace existing unfair trade laws. In other words, Canada was apparently content to continue to rely on the FTA panel system and its NAFTA successor. As the lumber, steel and pork cases amply demonstrated, that was simply not good enough. Former trade minister Wilson never adequately explained why he made this concession, nor what he believed he had obtained in return.

Liberal leader Jean Chrétien seized on this as one of the fundamental flaws in the NAFTA. If these flaws were not corrected, he promised, he would not proclaim the NAFTA if he were elected. Mr Chrétien made clear in the closing weeks of the election campaign that he would require agreement to negotiate a new set of trade rules, appropriate to a free trade area. He pointed out during the televised Leaders' Debate that this commitment was not new—it had been contained in Article 1906 of the Canada-USA free trade agreement. On 25 October, Jean Chrétien and his Liberals swept to power with a substantial majority while the Progressive Conservative party was reduced to just two seats in the House of Commons.

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Meanwhile, the Americans had engaged in a debate over NAFTA—starkly reminiscent of the debate in Canada in 1988 over the original FTA. Both parties were badly split, with the majority of Democrats opposed to the NAFTA. The billionaire demagogue, Ross Perot, made considerable political mileage out of his opposition to the deal.

The Administration engaged in extensive consultations with the Congress over the legislation to implement the NAFTA. As it took shape, the draft legislation would, in the name of free trade, have introduced a number of new restrictions including measures affecting specific Canadian industries—from wheat to peanuts—and further eroding the panel system's capacity to protect Canadian exporters from harassment. Canadian business, including the most vocal supporters of the NAFTA, was outraged, but the representations of Canadian officials were largely ignored.

During the transition between his election and the swearing-in of his government, Mr Chrétien conveyed in no uncertain terms his refusal to accept these bootleg measures. The final legislation was largely purged of these offensive provisions. There remained a good deal of inflammatory language in the accompanying Statement of Administrative Action which was, however, judged to be largely "sound and fury signifying nothing." Following some low grade political theatre, the House of Representatives moved to approve the NAFTA legislation by a sizeable margin.

### **2. The Canadian Conditions**

Attention then turned to the remaining conditions for Canadian approval. Mr Chrétien accepted that the side agreements met his minimum requirements for environmental and labour protection. He demanded and obtained agreement from his NAFTA partners on a joint statement that restated the obvious: nothing in the agreements impinged on any country's sovereign control over water in its natural state. He further made a unilateral statement of masterful ambiguity that asserted that Canada would protect Canadian interests in the event of an energy shortage.

The new Canadian trade minister, Roy Maclaren, moved quickly to agree with his American and Mexican counterparts to set up working groups to negotiate new trade rules within two years. One group is to examine the application of anti-dumping duties; the other, countervailing duties. It remains to be seen whether the Americans will participate in these negotiations in good faith.

There was some hope that progress on a subsidies code in the GATT would ease the way on countervailing duties. The GATT result on anti-dumping makes the task of the working party, if anything, more difficult. The importance of the task is obvious from the record under the existing FTA panel system for resolving trade disputes, discussed below.

Once these matters were resolved, the Government of Canada decided to bring NAFTA into force on schedule. The American and Mexican governments quickly followed suit.

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### 3. Impact of NAFTA on Canada

As discussed in last year's report, the direct impact of NAFTA on Canada will be modest. The extension of the free trade area to include Mexico will be of some value to specific Canadian firms exploiting niches for trade and investment. Several of **Strategico's** clients have examined such opportunities. There is certainly grounds for substantial growth, from a painfully small base, as Mexico last year bought around \$500 million-worth from Canada, down from the year before. This represents less than one per cent of Canada's exports under NAFTA; the remaining 99+% will be destined for the United States.

The impact of NAFTA on Canadian sales to the United States will be limited. The rules of origin should offer some improvements, overall, but will restrict exports in at least two industries, clothing and automotive (particularly by Japanese owned firms). There will be some opportunities to sell goods and services to the U.S. government although these will be hedged about with a variety of restrictions and "set-asides." As noted above, the environmental and labour deals will have little or no direct impact while the working groups on trade laws will not complete their negotiations for some time. Finally, for most Canadian companies, Mexican competition for sales in the United States will be marginal.

The indirect impact may prove substantially more important. If President Clinton had been defeated on NAFTA he would have been crippled in any future dealings with the Japanese and Europeans. The victory was costly and painful and the Administration may not be in a hurry to repeat the experience. Nonetheless, it preserved America's negotiating credibility in the GATT negotiations and reinforced the American commitment to the Canada-USA free trade agreement.

#### The Canada-USA Free Trade Agreement

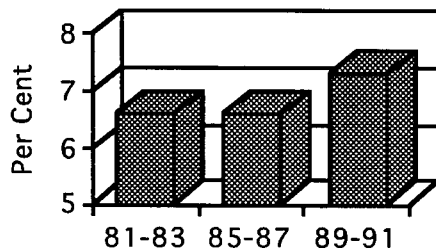
We originally forecast that it would take five years for the results of the Canada-USA free trade agreement to become clear. That time is now up. The recession in North America swamped the initial impact of the FTA: when American output fell, Canadian exports declined; now America is growing, our exports are booming. It would be as wrong to credit the FTA with all the increase as it was to blame it for the decline. Nonetheless, the results are now in. Serious analysis is now possible. We have some compelling answers to the question: How has free trade served Canadian interests to date?

#### 1. Canadian Market Shares

The most compelling evidence emerges from a recent comprehensive study by Statistics Canada of market shares. The study covered three periods, including the three years before, and the three years after, the FTA's entry into force. The results are striking.

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Canadian Share of Combined  
Canadian + American Market



Among the major points to emerge from the analysis of the post-FTA period:

- After losing share in the home market during the years before the FTA, Canadian manufacturers generally held on to their market share under the FTA, despite the increased American competition.
- The biggest gainers were the transportation equipment industries, led by the automotive sector, where production expanded rapidly to capture an increased share of the Canadian market.
- Meanwhile, Canadian producers did much better in the American market under the FTA, significantly increasing their share overall and making gains in most sectors.
- Taking the two markets together, the Canadian share, which had leveled off around 6.6 per cent before the FTA, vaulted to 7.3 per cent, an increase of more than 10 per cent overall.
- Virtually every sector gained market share including transportation equipment, beverages, fabricated metals, electrical and electronics, printing and publishing, plastics, machinery, non-metallic minerals, wood, clothing, and chemicals.

The significance of these findings is clear. Through the recession, Canadian producers were forced to sell into declining markets at home and in the United States against intense American competition. Against these odds, they held their share of the home market, despite predictions they would be inundated with imports from the United States. Better still, they significantly expanded their share of the American market, right across the board.

It should be remembered that during this period, the value of the Canadian dollar was rising sharply and Canadian labour costs were increasing, imposing a significant double handicap on Canadian producers competing at home and in American markets. **These results are consistent with only one conclusion: under the FTA, Canadian producers substantially improved their performance, through the depths of the recession.**

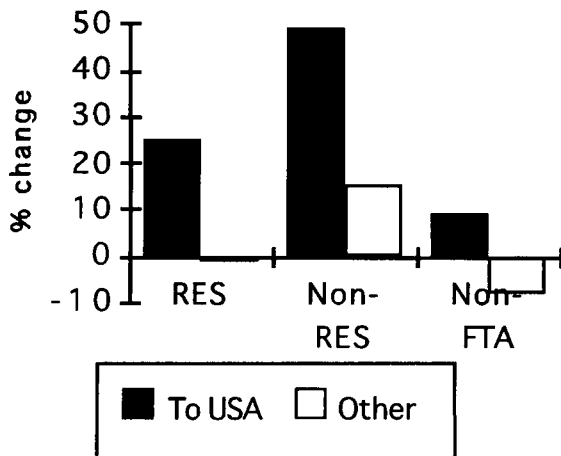
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### 2. Trade Performance under FTA

In September 1993, the C. D. Howe Institute published an update of its assessment of the Canada-USA free trade agreement, prepared by Daniel Schwanen. His findings are as follows:

- “The statistics do not support the view that the net impact of the FTA on Canada’s economic output has been negative. Instead, the unfolding patterns of trade suggest that free trade will be of long-term benefit to Canada, as its supporters predicted.”
- “Although certain industries have suffered from sharply increased import penetration, a number of the Canadian exporters that gained freer access to the US market also experienced a large increase in sales in that market, contrasting with the generally poor performance of Canadian products in other markets.”
- “Furthermore, the composition of the exports that have expanded under free trade is very significant: it consists of the higher value-added sectors of the Canadian economy, such as processed natural resources, high-technology industries and the business services sector.”

Canadian Exports  
1989-1992



- “While it is not yet possible to conclude that the jobs created or maintained by the expanding export industries have compensated for those lost by import-competing industries, it is a fact that the sectors that are expanding under free trade pay, on average, higher wages per employee than do those that have been hurt by the agreement.”
- “It appears that the scenario presented by the supporters of free trade is currently unfolding: that most of the benefits would come not only from expanded trade volumes but especially from a greater specialization of the economy into areas of higher productivity and incomes.”

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The Canada-USA free trade agreement was a structural policy initiative and, as such, will continue to have a significant impact on the Canadian economy for years to come. In the first few years, the adjustments have been wrenching for many firms and individuals, especially in the highly labour intensive, low wage and low technology sectors. **Nonetheless, to date, the evidence is overwhelming that the *net* impact has been beneficial: the FTA has increased Canadian production, significantly expanded exports to the United States and, in the process, generated additional employment in the higher paid, higher value-added industries.**

### Outstanding Bilateral Disputes

Inevitably, with this huge volume of trade, there will be disputes. The Canada-USA relationship is no exception. Even under the FTA, these disputes have been painful and prolonged. At any point, the trade affected is relatively small compared to the overall volume—generally under 5 per cent of total trade. This seriously understates the importance of these disputes. For obvious reasons, these disputes usually involve:

- the most successful Canadian export industries, which have managed to increase sharply their share of the American market and thus pose a greater threat to the domestic producers; or
- the most strategic investments, which are dependent on secure access to the American market for their viability as a large-scale operation serving the entire North American market.

The latter are often the most difficult to identify. A company may simply decide not to put the plant in Canada because of the risk of unfair trade action. That risk will be evaluated as most significant when there are a number of highly visible cases of protectionist action against established Canadian exporters.

### 1. Softwood Lumber

This long-running dispute has taken on the cast of the old silent film serial, "The Perils of Pauline." The heroine survives, more or less intact, from one episode only to be plunged into mortal peril in the next. In October 1991, Canada invoked its right to terminate the Memorandum of Understanding on Softwood Lumber on grounds that it was no longer, if ever, warranted. The Bush Administration responded with interim customs measures, which have since been determined by the GATT to have been entirely illegal, but have yet to be rectified. (Note: **Strategico** was retained to advise the Canadian industry coalition, the Council of Forest Industries of Canada.)

Meanwhile, the Administration self-initiated a countervailing duty case against Canadian softwood lumber, the third such case in the past 10 years. Predictably, the Department of Commerce in its preliminary determination slapped a duty of 14.5 per cent on imports from Canada. In its final determination, this rate dropped to 6.5 per cent in May 1992. The case was put to binational panels under the FTA, established

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to review whether Commerce and the International Trade Commission (ITC) had fairly applied American law. In our fourth annual report, we anticipated that the case would be resolved by the Fall of 1993.

In May 1993, the FTA panel examining Commerce's subsidy finding remanded the case to the department with a caustic questioning of the validity of the determination, observing that Commerce had failed even to consider the fundamental economic analysis of the issue. Commerce responded by re-affirming its original position and, to add insult to injury, jacking the rate back up to 11.5 per cent.

Meanwhile, the Commerce Department proceeded as if nothing had happened and, incredibly, launched its first annual review of its original determination, requiring Canadian producers and provincial governments, in effect, to begin the case all over again.

**On 17 December the FTA panel issued its final decision. It directed Commerce to acquit the Canadian lumber industry on all counts. It threw out the department's contention that provincial stumpage programs and B.C. log export controls were benefits provided to a "specific" enterprise or industry. The Commerce Department has 20 days to comply with this direction.**

Given the political profile of the issue, it was perhaps inevitable that the Administration would make an "extraordinary challenge" to the ruling of the FTA panel. This route has been followed on two past occasions, and in both cases the American claim was summarily thrown out. **The Americans have proved to be "sore losers" when they are forced to play fair.**

The likelihood of such a challenge has unfortunately been increased by the dissenting opinion of the two Americans forming the minority on the panel. In language clearly designed to trigger such a challenge, they allege the Canadian majority incorrectly applied the standard of review and thereby exceeded its jurisdiction. The expected challenge will be simply another step in the American effort to emasculate the FTA panel system.

Meanwhile, the panel examining the injury determination by the ITC remanded that decision, with the most serious questions about the analysis adopted by those commissioners who found that injury had indeed occurred. The ITC stubbornly re-affirmed its original determination and the issue is now back before the panel which was to announce its decision on 24 January 1994. We expected this decision, too, would almost certainly direct the ITC to exonerate the Canadian industry. The decision will presumably now be put on hold, pending the outcome of the challenge of the subsidy ruling.

This is a vitally important case for the Canada-USA free trade agreement. It affects one of Canada's most important industries. It also was recognized from the outset as the "test case" for the value of the agreement. In defending the FTA panel system, Canadian official spokesmen, including the Prime Minister, proclaimed

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that abuses such as the previous lumber countervailing duty case (which had given rise to the MOU) would not recur or, if they did, would soon be corrected by the FTA panels.

The good news is that the FTA panels have demonstrated, yet again, that the application of American law by the Commerce Department and the International Trade Commission is heavily biased against the importer. The bad news is that, after more than two years and enormous legal costs, the Canadian industry is still under a restriction which it, and the Canadian government, consider to be quite unfounded and unfair.

### 2. Flat Rolled Steel

The North American steel market is virtually as fully integrated as its principal market, the automotive sector, which has enjoyed free trade for a quarter century under the AutoPact. In response to competitive pressures from imports, American steel producers initiated a series of anti-dumping complaints in mid-1992. These were ostensibly aimed at overseas producers but, as is so often the case, Canada was the principal victim. (Note: **Strategico** was retained by a major Canadian steel producer to advise on the management of the dispute.)

The situation would have been unbelievable as a comic farce. American authorities wrapped up their determinations on the four original cases in mid-1993:

- The International Trade Commission found that imports of Canadian cold-rolled and hot-rolled steel products were not injuring American producers. In an unusual move, the **American** producers have appealed the case to **U.S.** courts.
- For galvanized steel and steel plate, imports from Canada were subjected to heavy dumping duties. Canada has appealed the cases to bi-national panels, with decisions due by mid-1994.

Meanwhile, the Department of Commerce has determined "preliminarily" that steel wire rod from Canada was being dumped into the United States. This case is proceeding.

To counter the American moves, the Canadian steel industry initiated a number of cases of their own. To this point:

- The Canadian International Trade Tribunal (CITT) acquitted imports of hot-rolled steel from the United States. In another unusual development, the **Canadian** industry has appealed the non-injury decision to FTA panels.
- For their part, American producers have appealed the dumping duties imposed on cold-rolled steel to FTA panels.

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- On steel plate, a **combined** panel is reviewing the appeal by **American** producers of the dumping determination and the appeal by **Canadian** producers over the CITT decision that these imports did not cause them injury.

Meanwhile, another case has been launched, against imports of galvanized steel from the United States and other countries.

The situation would be humorous if the consequences were not so serious. So long as both countries have on their books anti-dumping laws that are totally at variance with sound economics—let alone with a free trade arrangement—such cases will be used as a tool for handicapping the competition. It is, after all, much cheaper than taking the steps necessary to become more competitive. (It is estimated that it costs at least five times as much to defend a case than to initiate it in the United States.) Meanwhile, an integrated market for a vital industry is being torn apart and a large number of workers, communities and companies are at serious risk.

### 3. Durum Wheat

Stimulated by the Export Enhancement Program (EEP), American exports of subsidized wheat have increased significantly. One consequence has been to open up expanded opportunities for Canadian sales of high quality durum wheat into the American market. This did not sit well with the American wheat growers, and their congressional representatives. They alleged that these increased imports were fuelled by Canadian subsidies, notably for grain transportation and through the operations of the Canadian Wheat Board. In May 1992, the U.S. demanded and Canada agreed to a review of the situation by a panel established under Chapter XVIII of the Canada-USA free trade agreement.

The panel unanimously threw out the American claim. It did, however, recommend that a bi-national working group be established to oversee periodic audits of durum wheat sales by the Board into the American market. The Americans responded aggressively. Legislation introduced by a leading protectionist, Senator Max Baucus, proposed introducing barriers against imports of wheat from Canada, requiring end-user certificates for Canadian grain and committing \$1 Billion to special payments under the EEP that could be used to displace Canadian wheat from its traditional Mexican market. The U.S. Agriculture Secretary responded by extending EEP subsidies to the Mexican market. Canada protested that this action was in direct violation of the FTA. The outgoing Conservative trade minister announced that Canada's would demand an FTA panel on the issue

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In buying congressional votes for NAFTA, the Administration went further to accommodate these protectionist pressures. President Clinton demanded bilateral consultations on the issue with Canada. If the U.S. was not satisfied with the results within 60 days, the International Trade Commission was to begin an investigation of imports of Canadian wheat which could result in import restraints—contrary to the FTA and NAFTA. The Administration is also proceeding with end-user certificates as demanded by the domestic industry.

It is too early to judge how the dispute will ultimately play out. The fact that the Canadian practices have already been determined to be fully compatible with the Canada-USA free trade agreement will not deter the protectionists. To date, the Administration has fought a rear-guard action, lending vocal support to the protectionist demands but limiting direct trade action to a minimum. If, however, the Administration continues to give ground under pressure, the dispute could become very serious indeed, disrupting not only cross-border trade but exports to other traditional markets.

#### **4. The FTA Panel System**

These cases bring into focus both the strengths and weakness of the FTA system for the settlement of disputes. The panels on unfair trade actions have done a competent job of scrutinizing administrative decisions and questioning injustices. They have regrettably taken considerably longer than originally prescribed.

The best testimony to their effectiveness is, however, the systematic attempt by the U.S. Administration to weaken the force of panel decisions through refusing to give them any precedential value, resisting any correction of systematic abuses and attempting to limit the panels to the most legalistic scope. In any event, the fundamental problem remains that the panels are only as good as the rules they have to apply—and the existing antidumping and countervailing duty laws in Canada and particularly the United States are antithetical to free trade.

On more general disputes, the picture is mixed. Bi-national panels have done a reasonable job of clarifying issues and pointing the way to possible solutions. The decisions of these panels—even when unanimous—are, however, not legally binding on both governments. The U.S. Administration is liable to succumb to protectionist pressures, as the wheat case has shown, even if this means ignoring or flouting the panel verdicts.

## CANADIAN COMPETITION RECORD

**DECISION-MAKER'S SUMMARY  
FREE TRADE YEAR FIVE: COMING OF AGE**

- **When the agreements negotiated this year are finally implemented, Canadian trade will move more freely than at any time in the past.**
- **The upsurge of exports to meet the growing demand of foreign markets, particularly the USA, will help promote Canada's recovery from crippling problems of unemployment and public debt.**

**GATT's Uruguay Round**

- **The GATT agreement concluded in mid-December will be of limited *direct* importance to Canada** since we already enjoy free trade in goods and significantly better rules on trade in services with the market taking more than 75 per cent of our exports—the USA.
- **The agricultural deal largely preserves the *status quo* through the year 2001** as (i) subsidy disciplines, notably on grains, will be much more modest than originally sought and (ii) the high level of "tariffication" will ensure that there is no need for dramatic restructuring of Canada's supply managed industries.
- **The American claim that the resulting Canadian tariffs must be eliminated by 1998 under the NAFTA is patently absurd.** The GATT schedule will govern those products—dairy, poultry and eggs—currently protected under GATT Article XI import quotas (the same does not apply to the American attempt to maintain tariffs on sugar or peanut butter, which are clearly illegal under NAFTA.)
- **The move to a permanent World Trade Organization is positive but it will be only as good as the rules it has to administer:**
  - on the issue of countervailing duties against subsidies, the improvements appear to be significant, but
  - on anti-dumping duties, the American protectionists have clearly won a major victory in maintaining their ability to harass legitimate imports.
- **The total value of the tariffs taken off Canadian exports to foreign countries by the end of the transition period will be a fraction of those eliminated under the Canada-USA free trade agreement.**
- **Meanwhile, our preferential advantage in the far more important North American market (Canada, the USA and Mexico) will also be reduced, increasing competition from European and Asian imports.**
- **The real significance of the GATT deal lies in the framework it will continue to provide for future trade relations between the three major regions—Europe, Japan/Asia and the Americas.**

## CANADIAN COMPETITION RECORD

### The North American Free Trade Agreement

- **Mr Chrétien has met his commitment to address the principal flaws identified in the NAFTA itself:**
  - **the working parties on unfair trade rules commit the three countries to negotiating, in good faith, rules more appropriate to a free trade arrangement—sorely needed as disputes over lumber, steel, pork and wheat have demonstrated**
  - **the trilateral statement on water confirms the obvious—that nothing in the NAFTA impinges on any country's sovereign control of its water resources**
  - **the unilateral statement on energy confirms that Canada will interpret and apply the NAFTA in a way which maximizes energy security for Canadians**
- **The *direct* impact of NAFTA on Canada will be relatively modest**, given the small volume of our exports to Mexico (less than one per cent of our exports to the USA), the limited competition Canadian products face from Mexico in the American market, and the mixed impact on Canadian access to the United States market itself.

### The Canada-USA Free Trade Agreement

- **The initial impact of the FTA was largely swamped by the recession in North America**, as Canadian exports fell when the USA economy shrank and are now expanding as the USA is recovering.
- **Through the recession, Canadian producers held their share of their home market**, despite predictions they would be inundated with imports from the USA, and, better still, **they significantly expanded their share of the American market, right across the board.**
- **The evidence is overwhelming that the *net* impact has been beneficial** as the FTA has increased Canadian production, significantly expanded exports to the United States and, in the process, generated additional employment in the higher paid, higher value-added industries.

### Bilateral Trade Disputes: Lumber, Steel and Wheat

- **The lumber case was recognized from the outset to be the critical test. In mid-December, an FTA panel directed the U.S. Commerce department to acquit Canadian lumber of all charges.**
- **The Americans have proved to be sore losers when they are forced to play fair.** But even if the Americans make an “extraordinary challenge” of this ruling, the matter should finally be settled in Canada's favour by March 1994.

## CANADIAN COMPETITION RECORD

- **This shows the value—and the limitations—of the FTA panel system: after more than two years and enormous legal costs, the Canadian industry has finally won a case which should never have been brought in the first place, under defective American trade laws.**
- **The flood of steel cases, on both sides of the border, would be comic if the consequences were not so devastating, as an integrated market for a vital industry is being torn apart and a large number of workers, communities and companies are at serious risk.**
- **So long as both countries have on their books anti-dumping laws that are totally at variance with sound economics—let alone with a free trade arrangement—such cases will be used as a tool for handicapping, rather than meeting, competition from imports.**
- **The fact that Canadian wheat selling and transportation practices have already been determined to be fully compatible with the FTA will not deter the American protectionists and, if the Administration continues to give ground under pressure from domestic producers, the dispute could disrupt not only cross-border trade but exports to other traditional markets.**



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