ANNEX B

RESPONSES TO QUESTIONS OF THE PANEL IN THE CONTEXT OF THE SECOND SUBSTANTIVE MEETING

The *CGA* requires that CGC inspectors be present at terminal elevators to monitor the flow of grain into elevators, for both Canadian and foreign grain.[2]

74. With reference to Canada's reply to Question 13(d), how common is CGC monitoring of receipt or discharge and who pays for this in cases where such a requirement is imposed?

12. Nothing in Canadian law or regulations requires CGC monitoring of receipt or discharge of grain at elevators and indeed it is very rare that the CGC imposes this type of condition either for Canadian grain or for foreign grain. In those rare cases where an inspection condition is imposed, for example in the case of Starlink maize, the elevator pays the cost of CGC monitoring.

75. With reference to Canada's reply to Question 14(c), at what stage and where do the type of inspections referred to in section 32 of the *Canada Grain Act* occur?

13. Official inspections are always required for grain going into and out of terminal elevators. At transfer elevators, official inspections are generally required on discharge from the transfer elevator, and on request, are conducted on receipt of the grain into the elevator. Official inspections may also occur at primary elevators on request.

76. Canada indicates in its responses to Questions 16(b) and 59(a) that there is no authorisation requirement for the mixing of different grades and classes of foreign grain. Could Canada explain why section 72(2) of the *Canada Grain Act* does not apply in such cases? Furthermore, if there is no requirement for the mixing of different grades and classes of foreign grain, would Canada nevertheless impose a requirement that such mixeuirement is impt thc 2.beTD 0.0188

78. With reference to section 151 of the *Canada Transportation Act,* please clarify element "E". In particular:

(a)

and the Peace River area of the Province of British Columbia) that is sold either for export of for domestic human consumption. In respect of wheat and barley, Section 57 of the *CGA* and segregation requirements ensure that foreign grain maintains its identity so

interpretation in customary international law. The ordinary meaning of the words indicates that this requires: (1) an investment measure, that is, a measure that has an investment objective such as encouraging the development of local capacity; and (2) that this investment measure be related to trade in goods and not, for example, trade in services. This phrase, which defines the scope of the TRIMs Agreement, can also be understood in light of the Illustrative List, which is part of its context and provides examples of the type of investment measures related to trade in goods that are contemplated as falling within the scope of the Agreement.

33. An example of a trade related investment measure is the measure at issue in *Indonesia - Autos*.[10] In making the determination that there was an investment measure at issue, the panel noted that the car programme was

> aimed at encouraging the development of a local manufacturing capability for finished motor vehicles and parts and components in Indonesia. Inherent to this objective is that these measures necessarily have a significant impact on investment in these sectors ... we emphasize that our characterization of the measures as "investment measures" is based on an examination of the manner in which the measures at issue in this case relate to investment.[11]

34. In this case, the measures at issue deal with handling of grain in elevators and with

because of the rail revenue cap, Canada recalls the finding of the *Indonesia - Autos* panel that "[t]he TRIMs Agreement is not concerned with subsidies … as such but rather with local content requirements, compliance with which may be required through providing any type of advantage."[13]

85. How do the parties define the term "use" in Item 1(a) of the Illustrative List contained in the Annex to the TRIMS Agreement?

38. The term "use" in Item 1(a) of the Illustrative List can be understood as consuming, processing or transforming the product. Grain elevators and railways do not "use" grain but rather provide a service (handling, cleaning or transportation) in respect of grain. In contrast, a flourmill would be "using" wheat to produce flour and an oil seed crushing facility would be "using" soybeans

enterprise must take into account in imposing terms and conditions on the transaction they *make*: these considerations must be *commercial.* If the terms and conditions for one sale are different from those for another, the difference must be in accordance with commercial considerations, such as the factors set out in the subparagraph.

44. This, however, leaves the other situation of potential discrimination: where a Member and its enterprises are entirely excluded from even *competing* for purchases (from export monopolies) or sales (to import monopolies). In these circumstances, the issue is not the *terms and conditions* of a purchase or sales agreement (in which the factors mentioned in the first clause would be highly relevant), but rather the very chance, the opportunity to compete for such transactions. The second clause of subparagraph (b) addresses a situation where no purchase or sale has taken place because a state trading enterprise refuses to consider even allowing a purchaser or seller the opportunity to compete for participation in its purchases or sales. In this context, the factors set out in the first clause – such as price and quality of the product at issue – are not immediately relevant. And so, Article XVII:1(b) provides that for such an *exclusion from consideration* to be consistent with Article XVII:1, it must be in accordance with customary business practice. Accordingly, refusal by a state trading enterprise to consider even the opportunity for such purchases or sales by enterprises of a Member *not* based on customary business practice would result in the violation of Article XVII:1.

97. With reference to para. 39 of Canada's second written submission, is Canada suggesting that in respect of export sales by an STE, the MFN principle set out in Article I would not prohibit the selling at a <u>lower</u> price or under less stringent terms and conditions in one market than when selling in another?

45. The most-favoured-nation principle under Article I provides that any "advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in, or destined for, the territories of all other contracting parties."

46. Under Article XVII, the application of the most-favoured-nation principle in respect of exports sales by a state trading enterprise would require that the state trading enterprise provide any *advantage*, *favour* or *privilege* granted in respect of products destined for purchasers in one WTO Member immediately and unconditionally to products destined to purchasers in other WTO Members.

> [t]he charging by a state enterprise of different prices for its sales of a product in different markets is not precluded by the provisions of this Article, provided that such different prices are charged for commercial reasons, to meet conditions of supply and demand in export markets.

The Note makes clear that the charging of different prices in different markets is not discrimination under Article XVII:1, as long as it is based on commercial reasons.

98. With reference to para. 95 of Canada's second written submission, does not, or might not, a condition to keep foreign grain separate from domestic grain entail costs for an elevator operator, including the costs of separate/additional bins, etc.?

50. The requirement to keep foreign grain separate from Canadian grain does not entail extra costs for an elevator operator. Elevators in Canada are constructed to be able to handle numerous segregations of grain – for example, between different *types* of grain as well as different *grades* of a type – and elevator operators are experienced in managing elevator capacity to handle a large number of segregations. Being required to keep foreign grain separate from Canadian grain is simply one segregation amongst many that occur in elevators.

99. Could Canada elaborate upon, including by providing the legislative basis for and the practicalities associated with, the inspection and reporting requirements with respect to Canadian grain referred to in response to Questions 14(c) and 15? Do these requirements apply to foreign grain as well?

51. Official inspection and other grading requirements are found at Sections 61 of the CGA for primary elevators and at Section 70 of the *CGA* for terminal and transfer elevators. With respect to Section 70 of the *CGA*, official inspections at terminals are required both upon receipt of the grain into the terminal and upon discharge from the terminal; for transfer elevators, official inspection is only required upon discharge.

52. Foreign grain is not graded by the elevator on receipt into primary elevators, nor is it officially inspected by the CGC at transfer and/or terminal elevators.

53. The reporting requirements are based on Sections 79-80 of the *CGA* and Sections 23-27 of the Regulations. Details of reporting requirements, reporting forms and instructions can be found at http://www.grainscanada.gc.ca/regulatory/licensees/forms-e.htm.

54. Reporting requirements also apply to foreign grain. However, because foreign grain is not subject to the same quality assurance system prior to its entry into Canadian elevators, relying on reporting is not sufficient in the case of foreign grain to address potential concerns.

100. With reference to section 32 of the Canada Grain Act:

(a) Does this section cover cases where grain has been mixed? If so, what types of mixing are covered (i.e., mixing foreign grain with domestic grain, etc.)?

55. Section 32(1)(a) covers cases where Canadian grain has been mixed with other Canadian grain. Section 32(1)(b) covers cases where Canadian grain has been mixed with foreign grain or foreign grain mixed with other foreign grain.

(b) Are section 32 inspections undertaken only in case of grain destined for export?

56. No. Official inspections are conducted for export of grain but they are also conducted where grain moves to domestic end-users through a terminal elevator. A significant volume of grain

destined from Western Canada to the domestic market in Eastern Canada moves via the terminal elevators in Thunder Bay and is therefore inspected. Official inspections also occur on request for grain not destined for export; for example, in order to meet customer demand.

101. With reference to section 56(1), are there any conditions that operators of transfer elevators need to satisfy in order to benefit from the advance mixing authorisation other than the fact that grain needs to be "eastern grain"?

57. No, but the mixed Eastern grain will be officially inspected upon discharge and will be assigned the grade for which it qualifies.

102. With reference to Canada's replies to Questions 13(b), 13(c) and 15, how does Canada control shipments of foreign grain for GMO and SPS problems where foreign grain is shipped to the end-user directly rather than through the bulk grain handling system?

58. SPS problems are usually dealt with at the border. There is a requirement for an SPS certificate both for grain going to end-users and for grain entering elevators. However, no country's border controls are infallible. Given the importance of maintaining the quality and reputation of Canadian grain exports, there are greater concerns for grain entering the bulk grain handling system (which is geared towards exports) than for grain, whether domestic or imported, shipped directly to an end-user. The entry of foreign grain into the bulk grain handling system can raise SPS concerns that are additional to any SPS concerns arising from the mere importation of foreign grain into Canada.

59. Similarly, as regards GMOs, Canada may not have concerns about certain GMOs going directly to end-users. However, Canada may want to protect grain in the bulk grain handling system from genetically modified events not approved in Canada or in other countries, given that most of the grain entering the system is destined for export, including to countries that do not accept GMOs and that have a very low tolerance level for GMO "contamination". Canadian exports could be have a Tjon".

62. Foreign grain is also subject to SPS controls at the border.

63. No importer or exporter of US grain to Canada has to apply for an import permit in respect of plant health issues, unless the grain originates in the states of California, Arizona, New Mexico or Texas. Therefore, while US grain shipments are accompanied by phytosanitary certificates indicating freedom from certain diseases or pests, they are not subject to the same scrutiny as imports from most other countries where import permits are required by CFIA.

105. Why are Alberta, British Columbia, Manitoba and Saskatchewan the only provinces with loading sites eligible for the producer railcar programme?

64. Section 87 of the *CGA* does not limit "eligible loading sites" to these provinces but simply limits producer cars to "producers". There is no geographical limitation in law, regulation, or in the CGC Producer Car Allocation Orders.

106. With reference to Canada's Article XX defence, please provide your views on the alternative measures referred to by the EC in its written third party submission at paras. 31 and 32.

65. Paragraphs 31 and 32 of the EC submission seem to rely on*CGA*
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69. In any event, in order to mix Eastern grain and Western grain in transfer elevators (the only location where there is both Eastern grain and Western grain) an authorization from the CGC is necessary pursuant to Section 72 of the *CGA* and Section 56 of the *Regulations*.

ADDITIONAL PANEL QUESTION POSED AFTER THE SECOND MEETING

For Canada:

109. With reference to Canada's defence under Article XX(d), could Canada please indicate the level of compliance section 56 of the *Canada Grain Act* and section 57 of the *Canada Grain Regulations* seek to secure with the various laws referred to in Question 80? Please provide support for the level indicated.

70. Canada takes significant steps to protect the quality and reputation of Canadian grain exports. Canada is also committed to protecting the CWB's exclusive jurisdiction over the export and sale for domestic consumption of Western Canadian wheat and barley. In addition, Canada prohibits misrepresentation of products: it does not want to reduce the level of misrepresentation but to eliminate all misrepresentation with respect to grain. In light of this, Section 57 of the *CGA* and the segregation requirements are designed to secure a very high level of compliance with the grading provisions of the *CGA*, the *CWB Act* and the *Competition Act*.

ANNEX B-2

RESPONSES OF THE UNITED STATES TO QUESTIONS POSED IN THE CONTEXT OF THE SECOND SUBSTANTIVE MEETING OF THE PANEL

(29 October 2003)

Question 68: With reference to the US reply to Question 11 and para. 19 of the US second oral statement, is the United States claiming that section 87 is inconsistent with Article III:4 because producers of foreign grain are legally precluded, pursuant to section 87, from having access to producer cars, or because they are in fact denied such access in view of the fact that the producer car loading sites are located in certain areas?

4. The United States is claiming that Section 87 is inconsistent with Article III:4 because foreign grain is legally precluded from having access to producer cars and is thereby accorded less favourable treatment than like Canadian grain.

5. As evidence that foreign grain is legally precluded from having access to producer cars and is thereby accorded less favourable treatment than like Canadian grain, the United States has shown that producer cars are only available to Canadian grain producers located in certain Canadian provinces. The United States also has pointed out Canadian Government statements that the producer car benefit is only available to producers of Canadian grain.[2] It can therefore be concluded from this evidence – indeed, there is no other logical conclusion that can be drawn – that US grain is legally precluded from receiving the producer car benefit, since Canadian grain producers do not produce US grain.

Questions for both Parties:

Question 82: Please elaborate on what is an investment measure related to trade in goods within the meaning of Article 1 of the TRIMs Agreement.

6. At the outset, we wish to note that it is not clear whether the TRIMs Agreement requires a separate analysis of whether a measure is a trade-related investment measure. The panel in *Indonesia – Autos* expressly declined to reach this issue.[3] Nevertheless, whether or not the TRIMs Agreement in fact demands a separate analysis of this issue, the measures in this dispute are investment measures related to trade in goods within the meaning of Article 1 of the TRIMs Agreement. Because Canada's grain segregation and transportation measures require elevator operators, shippers and sellers/purchasers of grain to use domestic grain in order to obtain cost advantages, these measures necessarily have investment consequences for those enterprises and are investment measures for purposes of the TRIMs Agreement. These grain segregation and transportation measures also are clearly related to trade in goods, as they affect the sale, purchase, transportation, distribution and/or use of grain and favour use of domestic grain over foreign grain.

Question 83: With reference to paras. 1 and 2 of the Illustrative list annexed to the TRIMs Agreement which contain the word "local production", is the investment contemplated in these paras. investment pertaining to local production of goods, or could investment pertaining to the local supply of a service also qualify as "investment" within the meaning of the TRIMs Agreement?

[2] The United States has offered the web page of Agriculture and Agri-Food Canada as evidence that Section 87 of the Canada Grain Act provides less favourable treatment for foreign grain, and Exhibit US-23 should remain before the Panel for consideration, notwithstanding Canada's attempts to suggest otherwise. Canada repeatedly referred to government web sites during consultations as authoritative descriptions of Canadian measures. Canada also has itself provided the Panel with numerous web pages as evidence (*see, e.g.*, Exhibits CDA-60, CDA-61, CDA-62, and CDA-66). At the second panel hearing, Canada attempted to blur the distinction between measures on the one hand and evidence on the other by referring to Exhibit US-66)

see, e.g60, CDA

7. Only paragraph 1(a) of the Illustrative List is relevant to this dispute, and the phrase "local production" is not applicable to the measures at issue here. In this dispute, the grain segregation and rail transportation measures require the purchase or use of domestic grain. These measures do not state this requirement in terms of a proportion of the value of local production. The Panel need not examine the term "local production" in order to conclude that Canada's grain segregation and transportation measures fall under paragraph 1(a) of the Illustrative List and inconsistent with Article 2 of the TRIMs Agreement.

Question 84: With respect to the rail revenue cap, it would appear that an advantage, if any, could accrue to Western Canadian grain and its purchasers/sellers, but not to the railway companies transporting it. Is such an advantage covered by the provisions of Item 1(a) of the Illustrative List annexed to the TRIMS Agreement?

8. Canadian grain and its purchasers/sellers who use the rail transport system to ship Canadian grain obtain an advantage under the rail revenue cap in the form of lower rail transport rates for Canadian grain. This advantage is only obtained when domestic rather than foreign grain is transported, and it is an advantage that is covered by paragraph 1(a) of the Illustrative List. Compliance with the rail revenue cap measure is necessary in order for Canadian grain and its gr -12.75 TD -0.165e fo12.7a027 Tw measure in order for the advantage24u7 T74d( ) Tj 62erdoet applp6cmcerail r

with commercial considerations, but, instead, to act consistently with the policy objectives set forth in the Canadian Wheat Board Act. The CWB does in fact act according to this legal mandate. The CWB's rational behaviour under the Canadian Wheat Board Act results in the CWB maximizing sales, rather than profits, in furtherance of Canada's policy objectives but not in accordance with commercial considerations. This behaviour is inconsistent with the obligations set forth in Article XVII:1(b).

15. An STE may make full use of its special and exclusive privileges to gain market share in particular markets, for example, by discounting prices to make sales – but that behaviour would not be commercial. "Commercial considerations" in XVII:1(b) specifically references consideration of price, quality, availability, etc. Commercial behaviour driven by these considerations would result in actions that reflect market realities and are consistent across all actors in a given industry or market sector. The special and exclusive privileges granted to the CWB permit it to operate without the normal commercial constraints faced by a fully commercial actor – for example, the reduced risk faced by the CWB because of the government

19. Contrary to Canada's assertions, Article XVII:1(b) permits the use of special and exclusive privileges within certain parameters. For example, the CWB can exercise its government-granted monopoly privilege related to the sale of western Canadian wheat for domestic human consumption and export. Article XVII:1(b) does not require the CWB to let other entities sell western Canadian wheat, it merely requires the CWB to sell western Canadian wheat in accordance with commercial considerations and in a manner that affords the enterprises of other members an adequate opportunity to compete for participation in those sales.

20. Indeed, the Ad Note to Article XVII supports the US interpretation and provides an example of an STE's use of special and exclusive privileges that is consistent with Article XVII:1(b). The Ad Note states that an STE with special and exclusive privileges is not precluded from price discrimination between markets as long as "such different prices are charged for commercial reasons, to meet conditions of supply and demand in export markets."[11]

Question 89: Would the United States agree that export STEs compete not only with private enterprises that enjoy no government-conferred privileges and are constrained by market forces, but possibly also with private enterprises that may be dominant firms with market power in their home markets, private enterprises that engage in sustained or repeated dumping in third country markets within the meaning of Article VI of the GATT 1994 (but cause no material injury or cause material injury in a country that has no anti-dumping legislation or chooses not to counter such dumping), private enterprises that export agricultural products the exportation or production of which has been subsidized (and do so consistently with the Agreement on Agriculture, for instance), etc.?

21. In theory, both an export STE and a private corporation compete with the enterprises described above. But the nature of the players in the market does not in any way caveat or alter the obligation under Article XVII:1(b) to act in accordance with commercial considerations. Just as a private corporation would have no choice but to act according to commercial considerations regardless of the players in the market, an STE also must act solely according to commercial considerations. The Article XVII:1(b) standard remains the same whether or not the enterprises listed above compete in the market.

22. In practice, regarding private enterprises that are dominant firms with market power in their home markets and private enterprises engaged in sustained and repeated dumping in third country markets, the United States does not agree that the CWB is in fact competing with such enterprises. These two hypothetical scenarios are unlikely to exist in the world bulk grain sector. This is because private enterprises selling grain on the world market do not have a guaranteed access to supply and must compete with other entities in order to secure a supply of grain. In countries without monopoly STE's, all enterprises exporting grain must compete for supplies to sell. The grain export sector in most major grain exporting countries includes major international grain companies, as well as small, more specialized exporters who trade in only a few grain commodities and sell to selected markets. Given the nature of the grain market, none of these private enterprises can be characterized as a dominant firm with market power in its home market.

23. Concerning a private enterprise that engages in sustained or repeated dumping in third country markets in the wheat sector, we would first note that Members have condemned dumping that causes or threatens material injury under Article VI:1 of the GATT 1994. That condemnation exists whether or not a particular importing Member has anti-dumping legislation or chooses to take corrective action. Accordingly, the United States would hope that this would be a rare enterprise and there would not be sustained or repeated dumping.

[11] *Ad Note Article XVII*, para. 1.

Question 90: With reference to footnote 15 of the US second written submission, please provide a complete copy of CWB Marketing Panel Report (exhibit US-12). Also, please explain how the passage quoted in footnote 15 supports the view that No. 2 CWRS was actually sold at prices below No. 3 CWRS. Finally, if it did do so, why did the CWB have sold No. 2 CWRS at prices below No. 3 CWRS?

24. A complete copy of the CWB Marketing Panel Report is provided as Exhibit US-24.

25. In the passage quoted in footnote 15 of the US second written submission, the CWB describes the "value" of CWB pooling for the Canadian wheat farmer. Canada explains that a farmer should *not* assume that just because he delivered No. 2 CWRS to the CWB, his return is equal to the weighted average of all CWB sales of No. 2 CWRS during a given year. The CWB explains that this would be a false assumption because No. 2 CWRS (a higher quality wheat) might have been sold by the CWB at lower prices than the prices at which all the No. 3 CWRS (a lower quality wheat) was sold. Considered in context, one can infer that the CWB does in fact engage in such pricing schemes. The description is not posed merely as a hypothetical, but as an explanation of CWB activities. This statement also corroborates other evidence that the CWB gives away quality and protein in its sales. Given the CWB's secrecy surrounding its sales data, relying on such CWB statements is one means of demonstrating that the CWB engages in sales that are inconsistent with Article XVII:1.

26. Regarding why the CWB would sell No. 2 CWRS at prices below No. 3 CWRS in a given market, such behaviour precludes another competitor from competing in that market because the competitor cannot sell comparable high-quality wheat at a low-quality wheat price without taking a loss. The CWB engages in such behaviour to increase its sales and market share. It is able to do so without concern for the losses faced by private competitors because the CWB's special and exclusive privileges provide the CWB with mechanisms to adjust its pools in a way a private enterprise cannot. For example, the CWB adds its net interest earnings to its pool accounts, using the net interest earnings to inflate the pool revenue so that the CWB can increase returns to farmers irrespective of the actual revenue earned from current grain sales.[12]

Question 91: At para. 25 of the US first written submission, the Unites States asserts that, over the past 15 years, the CWB's initial payments have been "well below full market value". On the other hand, at paras. 12 and 13 of the US second written submission and in its reply to Question 35, the United States asserts that the CWB during 1992-1997 paid premiums to Western Canadian farmers for high-quality wheat, thus giving an incentive for farmers to over-produce such wheat. Could the United States explain how "below-full-market value" initial prices have induced over-production of high-quality wheat?

27. These two CWB behaviours demonstrate how the CWB's sales are inconsistent with Article XVII:1 standards. Initially, the advantage gained by the CWB as a result of the initial price payment mechanism should be analyzed separately from the CWB practice of encouraging excess production of high-quality wheat. Under the initial price payment mechanism, the CWB can acquire wheat for as little as two-thirds of the expected full market value of the wheat. This provides the CWB with maximum pricing flexibility in making sales. The initial price payment mechanism means that the CWB – for an entire marketing year – knows at exactly what price it can acquire wheat, and its monopsony procurement right means the CWB knows approximately how much wheat is available for purchase. This provides the CWB with significant pricing flexibility and decreased risk exposure.

28. To ensure there are sufficient quantities of high-quality wheat, the CWB's pooling mechanism, in combination with the varietal control system, encourages production of high quality wheat (see response to question 90, above). "On average, the amount of high-quality wheat produced in Western Canada has been larger than the demand that has been willing to pay a commercial

[12] *See* US Second Written Submission, paras. 16-17.

premium for it."[13] To the extent that such production exceeds world demand, the CWB engages in price discounting to move the high-quality wheat into export markets.

29. It is only through the combination of special and exclusive privileges that this seemingly anomalous situation occurs. The CWB pays less than full value to acquire wheat from producers, and depending on its selling practices and supply and demand conditions in a particular marketing year, the CWB will return to the farmer a higher price than the CWB sold the wheat for in an export market. The CWB has a large supply of high quality wheat that it can "price to move," depending on world market conditions. The CWB continues to encourage the excess production of high-quality wheat by rewarding farmers through price premiums, even if those price premiums are not warranted by market conditions.

30. For example, the CWB states that it bases its pricing on the Minneapolis Grain Exchange (MGE). Therefore one can assume that the premiums for high-protein wheats offered by the CWB should be similar to the premiums posted at the MGE. However, this is not the case. For marketing years 1995/96, 1996/97 and 1997/98, the protein premium spreads in Canada for No. 1 Canadian Western Red Spring were over 20 per cent greater than the similar protein Westerit gr

cars or ownership costs like depreciation and interest, farmers will ultimately bear

LIST OF EXHIBITS

US-24	Canadian Wheat Board, "The Role of the Canadian Wheat Board in the Western Grain Marketing System (23 Feb. 1996).
US-25	Canadian Wheat Board, "Grain Matters: Sale of the Federal Hopper Car Fleet," (July-Aug. 2002).
US-26	Transport Canada, Press Release No. H034/00, "Government of Canada Announces Measures to Improve Western Grain Handling and Transportation System," (10 May 2000).
US-27	Canadian Pacific Railway, "CPR Reports Increased Second Quarter Operating Income of $206 Million," (19 July 2001).

ANNEX B-3

CANADA'S COMMENTS ON THE ANSWERS OF THE UNITED STATES TO THE PANEL'S QUESTIONS FROM THE SECOND SUBSTANTIVE MEETING

(4 November 2003)

law that prohibits or restricts access to producer cars for either foreign grain or foreign grain producers. In advancing its case, the United States provides an interpretation of Canadian law that is not based on any accepted principle of statutory interpretation. Rather, it relies exclusively on an Agriculture and Agri-Food Canada website as evidence for its interpretation of Section 87 the *CGA*. As a preliminary matter, information materials on a website cannot and do not limit the scope of Canadian legislation. In addition, Agriculture and Agri-Food Canada is not responsible for the producer car programme and so any information on its website is of limited relevance to the administration of the programme. Finally, the information contained on the website has now been removed because it was incorrect.[1]

to the US assertion, therefore, the Panel should interpret the term "investment measure" before it proceeds to apply the Agreement.

8. The United States is, of course, well aware of this logical sequence, even as it invites the

milk in the tanker. A moving and storage company that stores furniture and personal goods of the people it moves does not "use" their beds, dining tables, linen and cutlery.[4]

For the United States:

86. Could the United States elaborate on what it means when it says that the CWB Export Regime "necessarily results" in CWB export sales that are not in accordance with the Article XVII standards? (*see* US second written submission, para. 3; US reply to Question 1(a))? Is the United States arguing that non-conforming CWB export sales are an inescapable consequence of the CWB Export Regime, or is the United States arguing that it can be presumed, in the light of the various aspects of the CWB Export Regime discussed by the United States, that the CWB will make sales that are not in accordance with the Article XVII standards (*see* US first written submission, para. 70)?

14. The United States asserts that the CWB has a statutory mandate to "maximize sales of Canadian wheat on the world market". The United States does not cite where in the *Canadian Wheat Board Act* ("*CWB Act*") or any other Canadian statute such a mandate is set out.

15. The US assertion is factually incorrect. Section 5 of the

(a) How should the word "commercial" be interpreted?

(b) The US can be understood as arguing that it may be "rational" for an export STE to use its special privileges to gain a competitive advantage in the marketplace *vis-à-vis* its competitors, but that export sales made in this manner would not be based on "commercial" considerations. In other words, the US appears to argue that the "commercial considerations" criterion requires more than rational competitive behaviour. (*see* US reply to Question 23, US second written submission, para. 19) If that is correct, could the United States explain how the word "commercial" in Article XVII:1(b) supports this view?

(c) With reference to the US reply to Question 22(d), would the United States accept that a private monopolist that is able, due to barriers to entry, to extract monopoly rents in its home market is acting on the basis of what is described as "commercial considerations" in Article XVII:1(b)?

19. Article XVII:1(b) provides that a state trading enterprise that engages in discriminatory practices not in accordance with Article XVII:1(a), is nevertheless acting consistently with Article XVII if it acts in accordance with commercial considerations. The United States has not at any point given a proper interpretation of what constitutes "commercial considerations". It has repeatedly stated that a state trading enterprise that does not have the same commercial constraints of certain private traders *necessarily* does not act in accordance with commercial considerations. It has also asserted that "revenue maximising" and "maximising sales" are not "commercial considerations", and in support it has adduced a study that has noted that "revenue maximising" conduct potentially results in higher production than "profit maximising conduct". The United States has not adduced evidence or argument why the report in question, even if correct, is in any way support for the proposition that revenue maximising conduct is not acting in accordance with commercial considerations. Finally, although the United States repeatedly refers to what private traders can or cannot do, it has not once adduced any evidence of such conduct. Indeed, when faced with evidence that *its own* multinationals *in the same sector* use programmes that are substantially similar to the measures at issue, the United States has adopted an attitude of stony silence.

20. From the outset, the position of Canada, amply supported by the language of the treaty and by common sense, has been that Article XVII:1(b) does not set out a standard of specific behaviour (for example, profit maximising or revenue maximising). The conduct of a private trader in the market is dictated by any number of short-term and long-term considerations based on market conditions, as well as its structure and objectives – the total ensemble of these considerations is referred to as "commercial considerations." A state trading enterprise is no different. "Revenue maximization" may be perfectly commercial conduct for one private trader, but ruinous to another; a trader in possession of a highly perishable commodity at the end of its life has every incentive to "maximise sales" for reasons that a coal dealer would not have to deal with. Finally, as any business model based on "rational" conduct sets out, to seek short-term profit maximisation at the cost of long-term consumer loyalty could be disastrous to a private trader. Thus, a trader – whether private or a state trading enterprise – that does not act rationally but rather "commercially" in the very narrow US sense of "profit maximization" may well find itself out of business soon after the profits are realised.

21. What Article XVII:1(b) requires, then, is simply that state trading enterprises take into account certain factors ("commercial considerations") in making purchases or sales, and not others (non-commercial considerations – for example, political ones). That is, they should base their decisions on the same sort of factors that private traders take into account in making purchases or sales. These factors include, but are not limited to, "price, quality, availability, marketability, transportation and other conditions of purchase or sale." In the same vein, the manner in which a state trading enterprise, or any enterprise for that manner, responds to such factors depends on the

environment and circumstances in which it operates. For a state trading enterprise, its environment and circumstances necessarily include the exclusive or special privileges that it enjoys.

22. The United States asserts that the CWB does not act in accordance with commercial

Written Submission, the United States again wilfully misrepresents the statement at page 15 of the CWB Marketing Panel Report.[6]

26. By creatively dropping certain words, the United States completely changes the meaning of the text. Read in its entirety, the meaning is clear: the CWB's statement corrects a *hypothetical misunderstanding* that pooling is the weighted averaging of CWB sales prices for a given type, class, and grade of grain over a given year. The CWB explains that *if* pooling were indeed (and it is not) the weighted averaging of CWB sales, then:

> … somebody who had delivered No. 2 CWRS 13.5 per cent protein wheat during 1994-95 would have ended up receiving the weighted average of all sales of No. 2 CWRS 13.5 per cent protein wheat during that year. The problem with that type of system would be that all or most of the No. 2 CWRS 13.5 might have been sold at lower prices than the prices at which all the No. 3 CWRS wheat was sold. The result of this would be that the average return for No. 3 CWRS wheat would be higher than that for No. 2 CWRS 13.5 wheat, *even though No. 2 CWRS 13.5 was worth more in the market than No. 3 CWRS at all times throughout that year*. That would obviously not be a proper market relationship between these two grades of wheat.
>
> The averaging of prices is not what happens in the CWB pooling system. Instead, as the CWB sells wheat and barley throughout the crop year, the revenue from those sales is deposited into four pool accounts: the wheat account or "pool", the durum wheat pool, the designated barley pool (barley sold for human consumption purposes, primarily malting barley), and the feed barley pool. Revenues from the sales of each of these four commodities are pooled separately in the appropriate account.
>
> Pooling is a mechanism both for collecting and – more to the point – for distributing to farmers who delivered to the CWB in the course of the year the results of sales the CWB made on their behalf. All farmers in the wheat pool, for instance, will end up sharing in the results of all wheat sales made throughout the crop year. The actual pool return that is established for any particular class, grade, or protein level of wheat, on the other hand, will be determined by the price relationships for the various wheats that existed in the world markets over the course of that year. The CWB keeps track of these price relationships in the market as it makes sales throughout the year to ensure that when the crop year is over and everything is paid out of the pool accounts, it will have reflected to farmers the proper market relationships between the various classes and grades.[7]

27. The United States asserts that its selective quotation of this statement "corroborates other evidence that the CWB gives away quality and protein in its sales."[8]

28. The United States has once again undermined its own arguments. The Marketing Report proves the opposite of what the US claims: the CWB does not give away quality and protein in its

producers may apply to the Commission for producer railway cars and the absence of a reference to foreign grain producers on that site?

29. Under Canadian law, web site information is irrelevant to the interpretation of a law. While governments use web sites to provide information to the public, these web sites are of no relevance to the interpretation of the law and cannot modify or restrict the terms of the law.

93. With reference to the US reply to Question 54, is there evidence that the railway companies are in fact charging lower rates for government rail cars than for other types of rail cars?

30. The US Panel Request did not include a challenge to the provision of *government railcars* but only the provision of *producer cars*. In fact, the second bullet of Claim 2 of the

contracts that was skewed because it included contracts for *two* classes of Canadian wheat, but only *one* class of US wheat.[11]

38. In any event, over-delivery of protein amounts to a "giveaway" as the United States alleges *only* if the final contract price is not adjusted upwards to reflect the additional protein delivered. The United States adduces no evidence to support such a conclusion, which would, in any event, be incorrect. Indeed, the ITC study showed that for the export markets examined, the contract price was adjusted upwards in 47 per cent (43 of 92) of contracts involving Canadian wheat, but only 13 per cent (15 of 117) of contracts involving US wheat.[12] To the extent, therefore, that the data in this study permit any conclusions about protein "giveaways" in the eight export markets, the practice was more common in contracts for US wheat than Canadian wheat.

39. In addition, with respect to the US market, for which the underlying data were much more robust, the results of the study unambiguously refute the US allegation that the CWB consistently over-delivers protein. The data demonstrated a *lower* percentage of over-delivery for Canadian wheat, as the following passage attests:

> To assess the extent of over-delivery of protein content in domestic wheat purchases, the Commission analyzed differences in contracted and delivered protein in 615 Durum, HRS, and CWRS wheat contracts reporting both sets of data. For all but # 1 CWRS wheat, most contracted purchases were shown to have a tendency toward over-delivery of protein content. However, all contracts for all comparable wheat grades and classes tended to meet or exceed the contracted protein specification for final delivery of the product. Out of 510 reported US shipments of HRS and US Durum wheat, 65 per cent reported protein over-delivery, while 54 per cent of 105 reported CWRS and Canadian Durum contracts reported over-delivery of protein. Most of these differences were found to be within a 1.0 percentage points range above the contracted protein specification, and nearly all were within 1.5 percentage points, for both US and Canadian wheat.[13]

[11] See Exhibit CDA-70, Table 5-9.
[12] See Exhibit CDA-70, Table 5-7.
[13] See Exhibit CDA-71.

ANNEX B-4

UNITED STATE'S COMMENTS ON THE ANSWERS OF CANADA TO THE PANEL'S QUESTIONS FROM THE SECOND SUBSTANTIVE MEETING

(4 November 2003)

Questions for Canada:

Question 69: With reference to the possibility to condition the receipt of foreign grain on it being kept separate from Canadian grain in authorising such receipt under section 57(c) of the *Canada Grain Act* (see, e.g., Canada's second written submission, para. 95), does the power to impose such a condition derive from section 57 itself or is there a provision elsewhere in the Act and/or regulations that provides for this?

1. The United States wishes to emphasize, as mentioned in paragraph 26 of our second written submission, that Section 57(c) of the Canada Grain Act ("CGA"), on its face, prohibits the entry of all foreign grain into Canadian grain elevators. If an elevator operator wishes to receive foreign grain, Section 57 provides for an exception to this general prohibition. The elevator operator must apply to the Canadian Grain Commission ("CGC") and request a special entry authorization for the foreign grain. This special authorization is a regulatory hurdle not required for like domestic grain.

Question 70: With reference to the separate keeping in elevators of domestic grain of different types, grades, protein content and origin, as referred to at paras. 247 and 248 of Canada's first written submission, is such segregation/separate keeping a commercial practice by elevators or a legal requirement? If the latter, please provide the relevant legal text. Also, please indicate whether there is a difference in this regard between different types of elevators (primary, etc.).

2.

elevators and the mixing of foreign grain. Any special authorization required to overcome these *de jure* prohibitions is an additional burden placed on foreign grain that is not placed on Canadian grain.

4. It is not surprising that, as Canada states, "if there is no request for mixing from the elevator, the entry authorization requirement includes a condition that the foreign grain be kept separate," since under Section 56(1) there is a legal prohibition on the mixing of foreign grain. The United States disagrees with Canada's characterization that this prohibition occurs "as a matter of practice." Section 56(1) clearly sets forth a legal requirement that mixing may only take place if neither of the grains to be mixed is foreign grain.

5. As for Canada's assertion that 12 per cent of entry authorization requests include a request to mix foreign grain with Canadian grain, Canada provides no evidentiary support for this figure.

Question 72: What is the legal relationship between the Wheat Access Facilitation Programme and section 57(c) of the *Canada Grain Act*? In particular, has the Wheat Access Facilitation Programme been established under the authority of section 57(c)? Please provide documentary support.

6. Canada's answer to the Panel's question mis-characterizes the United States' reference to the Wheat Access Facilitation Programme. We have not referred to the WAFP as a separate challenged measure, but, rather, we refer to it to provide a concrete example of the CGC's onerous regulatory requirements. This does not expand the scope of the proceedings.

7. The CGC characterizes the WAFP not as a separate authorization, but as a document that "clarifies the Canadian Grain Commission's (CGC) requirements for Canadian licensed primary elevators handling wheat from the United States (US)."[1] (Emphasis added.) The WAFP also states that primary elevators may receive US wheat "subject to participation in the Wheat Access Facilitation Programme and adherence to the requirements set out in this Memorandum."[2] (Emphasis added.) Moreover, not adhering to the WAFP requirements has serious consequences for the primary elevator. The Memorandum states that "[f]ailure to comply with the requirements in this Memorandum could result in revocation of license, prosecution, or the CGC refusing to give further permission to facilities to receive US wheat."[3] (Emphasis added.) Finally, the Importer's Declaration form, a form required under the WAFP, specifically refers to Section 57(c) of the CGA, indicating that Section 57(c) is indeed the legal authority under which the WAFP operates.[4]

8. In short, the CGA violates GATT Article III:4, and the WAFP is but one clear example of this. This is true regardless of the origin of the WAFP, which is irrelevant to the dispute and does not excuse Canada from maintaining an otherwise WTO-inconsistent measure.

Question 73: With reference to section 57(c) of the *Canada Grain Act*, once the receipt of foreign grain has been authorised, does a CGC employee have to be physically present, in most or all cases, to monitor the flow of the foreign grain into the elevator bins? If so, do CGC employees similarly monitor the flow of Canadian-origin grain into elevator bins?

9. Canada provides no evidence for its assertion that it is "rare" that CGC inspectors are present to monitor receipt of grain into primary and transfer elevators. Indeed, Canada's response is contrary to the requirements of the CGC as clarified by the WAFP, which states that the CGC will not

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[1] Canadian Grain Commission, "Memorandum to the Trade: Canadian Licensed Primary Elevators Handling United States Wheat," (22 Feb. 2001), *available at* www.grainscanada.gc.ca/Views/Tradenotices/uswheat99-e.htm (Exhibit CDA-60).

[2] *Id.*

[3] *Id.*

[4] *See id.*

authorize the entry of US wheat unless there is a CGC employee on site to monitor the flow of US wheat into bins.

Question 76: Canada indicates in its responses to Questions 16(b) and 59(a) that there is no authorisation requirement for the mixing of different grades and classes of foreign grain. Could Canada explain why section 72(2) of the *Canada Grain Act* does not apply in such cases? Furthermore, if there is no requirement for the mixing of different grades and classes of foreign grain, would Canada nevertheless impose a requirement that such mixed foreign grain not be designated as "Canadian" grain, etc. If so, what would be the legal basis for such a designation requirement?

10. Despite statements to the contrary in paragraph 16 of Canada's answer, Section 56(1) of the CGR does explicitly mandate the imposition of mixing restrictions with respect to foreign grain.

Question 78: With reference to section 151 of the *Canada Transportation Act*, please clarify element "E". In particular:

(a)

that railway companies do not take the revenue cap into account, railroad company executives have stated that they see it as their obligation to stay below the rail revenue cap.[7]

Question 80: With respect to Canada's defence of section 57 of the *Canada Grain Act* and section 56(1) of the *Canada Grain Regulations* under GATT Article XX(d), and with reference to the panel report on *European Economic Community - Regulations on Imports of Parts and Components* (BISD 37S/132, paras. 5.14-5.18) which suggests that Article XX(d) covers only measures designed to prevent actions that would be illegal under the laws with which compliance is sought to be secured, please identify for each of the laws referred to (*Canada Grain Act*, etc.), and provide the text of, the obligations with which sections 57 and 56 seek to secure compliance. In addition, please provide details of how sections 56 and 57 are necessary to secure compliance with the relevant provisions of the laws in question.

15. Canada has not met its burden with respect to its Article XX(d) defence. Section 57 and Section 56(1), which are wholesale prohibitions on the entry into grain elevators and mixing of foreign grain, are not necessary to secure compliance with the grading provisions of the CGA and CGR. Canada has not adequately explained how the *per se* prohibition on the entry of foreign grain into grain elevators under Section 57 and the *per se* prohibition on the mixing of foreign grain under Section 56(1) prevent actions that would be illegal or are otherwise designed to secure compliance with Sections 32 (inspection certificates), 61 (grading and inspection procedures on receipt of grain for primary elevators) and 70 (grading and inspection procedures on receipt of grain for transfer and terminal elevators). Canada appears to argue that Sections 57 and 56(1) ensure that inspectors do not make mistakes and assign Canadian-specific grades to foreign grain. Yet Canada provides no evidence that Section 57 and 56(1) are designed to eliminate such errors.

16. Even if Canada had demonstrated that Sections 57 and 56(1) were designed to secure compliance with Sections 32, 61, and 70, the *per se* prohibitions under Sections 57 and 56(1) are not necessary to secure compliance with Sections 32, 61, and 70. The grading provisions of the CGA and CGR themselves, described in Canada's own submissions, along with the enforcement provisions under the CGA and CGR, are adequate to ensure that "that Canadian grades are not inadvertently and inappropriately given to non-Canadian grain."[8] Indeed, as Canada itself points out, Section 32 already distinguishes between grain grown in Canada and grain grown outside Canada. Canada has not shown that proper inspection and grading cannot be accomplished in the absence of Sections 57 and 56(1).

17. Regarding compliance with the CWB Act and the CWB Regulations, Canada has other measures in place to ensure that the CWB only markets western Canadian wheat and barley. There is no reason to establish a prohibition on the entry of all types of foreign grain into all grain elevators throughout Canada under Section 57 in order to secure compliance with the CWB Act and the CWB Regulations. The grading requirements under the CGA are adequate to ensure that foreign wheat and barley are not mistaken for western Canadian wheat and barley and marketed by the CWB. In these proceedings Canada has portrayed the CWB as a sophisticated entity, and it is difficult to see – and Canada does not adequately explain – why a *per se* prohibition on the entry of all foreign grain into all grain elevators is needed in order to secure compliance with the CWB Act and the CWB Regulations. Indeed, Canada has no such *per se* prohibition in place with respect to the entry into grain elevators of eastern Canadian wheat and barley, grains which are also outside of the CWB's mandate under the CWB Act and the CWB Regulations. The CWB can ensure that it is only supplied western Canadian wheat and barley by writing that requirement into its contracts with grain elevator operators, or using the measures that are in place for eastern Canadian wheat and barley. The

and CWB Regulations. Section 56(1) already includes a prohibition on mixing western Canadian grain, and this prohibition alone is sufficient to secure compliance with the CWB Act and CWB Regulations.

18. Finally, regarding compliance with Section 52 of the Competition Act, Canada fails to demonstrate how Sections 57 and 56(1) are necessary to secure compliance with a general misrepresentation statute, especially in light of the fact that there are specific inspection provisions of the CGA that "ensure that foreign grain maintains its identity in the bulk handling system."[9] Furthermore, Canada fails to explain why Canada does not find it necessary to segregate all products according to origin in order to secure compliance with the general prohibitions on misrepresentation contained in Section 52 of the Competition Act.

Question 81: With reference to Canada's reply to Question 63, is there any reason why Canada

companies transporting it. Is such an advantage covered by the provisions of Item 1(a) of the Illustrative List annexed to the TRIMS Agreement?

22. Regarding Canada's reference to the US Department of Commerce countervailing duty investigation, as noted in paragraph 38 of our second written submission, the US Department of Commerce analysis is not relevant to this proceeding.

Question 85: How do the parties define the term "use" in Item 1(a) of the Illustrative List contained in the Annex to the TRIMS Agreement?

23. Canada conveniently refers to only one, narrow concept of the word "use" in its answer. However, the word "use" is not limited to consumption, processing and transformation. Indeed, the

Question 98: With reference to para. 95 of Canada's second written submission, does not, or might not, a condition to keep foreign grain separate from domestic grain entail costs for an elevator operator, including the costs of separate/additional bins, etc.?

27. Contrary to Canada's assertions, Canada's grain segregation requirements do in fact entail costs for elevator operators. Keeping foreign grain separate regardless of commercial demand for such segregation leads to inefficiencies in the grain handling system. For example, it would be more efficient for an elevator operator to store US corn and like Canadian corn in the same bin, since the end user who purchases the corn (*e.g.*, a feed lot) does not care if it is mixed. Instead, an elevator operator may have a bin half full of US corn and be unable to utilize the excess capacity because he only has Canadian corn that needs storage.

28. The grain segregation requirements extend to rail car and truck shipments, which leads to additional inefficiencies. Because US grain and Canadian like products must be kept separate, an elevator operator may find that he has to ship a partially full rail car of US corn, since he is not permitted to add like Canadian corn to the rail car in order to fill it. This results in additional costs for the elevator operator. With costs for handling foreign grain higher than the costs of handling like Canadian grain, foreign grain faces less competitive conditions than like Canadian grain, as elevator operators will be more likely to accept like Canadian grain over foreign grain in order to avoid the additional handling costs associated with foreign grain.

Question 99: Could Canada elaborate upon, including by providing the legislative basis for and the practicalities associated with, the inspection and reporting requirements with respect to Canadian grain referred to in response to Questions 14(c) and 15? Do these requirements apply to foreign grain as well?

29. If, as Canada states, foreign grain is not officially inspected at terminal elevators,[12] it is difficult to understand why CGC inspectors must be present to monitor the flow of foreign grain into terminal elevators.[13] This contradiction highlights the fact that throughout its submissions Canada makes misleading statements about its grain segregation system in an attempt to obscure the legal requirements under the CGA and make it difficult to assess whether Canada's measures are consistent with its WTO obligations.

30. Canada maintains a highly comprehensive reporting system that, as Canada admits, also extends to foreign grain. Canada's statement that "relying on reporting is not sufficient in the case of foreign grain to address potential concerns," is a baseless assertion and is not supported by the extensive documentation listed at www.grainscanada.gc.ca/regulatory/licensees/forms-e.htm.

Question 102: With reference to Canada's replies to Questions 13(b), 13(c) and 15, how does Canada control shipments of foreign grain for GMO and SPS problems where foreign grain is shipped to the end-user directly rather than through the bulk grain handling system?

31. Again, as with Canada's answer to Question 81, Canada misleadingly implies that the provisions of the CGA and CGR at issue in this dispute are SPS measures. This is patently false. As we discuss in our comments on Question 81, phytosanitary issues with respect to grain imports are handled by the Canadian Food Inspection Agency (CFIA). For example, CFIA Directive "Barley, Oat, Rye, Triticale and Wheat -- Phytosanitary Requirements on Import, Transshipped, In-Transit and Domestic Movement," effective November 2000, specifies the plant protection requirements for

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fifty per cent of durum wheat planted in the spring of 2000 was of a Canadian variety.[15] Even so, this wheat is treated as "foreign" and is given less favourable treatment than like Canadian wheat.

<u>Question 109</u>: With reference to Canada's defence under Article XX(d), could Canada please indicate the level of compliance section 56 of the *Canada Grain Act* and section 57 of the *Canada Grain Regulations* seek to secure with the various laws referred to in Question 80? Please provide support for the level indicated.

37. Canada's answer to Question 109 does not satisfy Canada's burden regarding its affirmative defence under Article XX(d). As set forth in our written submissions,[16] Canada must prove that Section 57 of the CGA and Section 56(1) of the CGR are

LIST OF EXHIBITS

US-28	Adrian Ewins, "Railways Below Revenue Cap, But Slightly," The Western Producer (2 Jan. 2003), *available at* www.producer.com/articles/20030102/news/20030102news06.html.
US-29	Canadian Food Inspection Agency, "Barley, Oat, Rye, Triticale and Wheat – Phytosanitary Requirements on Import, Transshipped, In-Transit and Domestic Movement, D-99-01 (1 Nov. 2000), *available at* http://www.inspection.gc.ca/english/plaveg/protect/dir/d-99-01e.pdf.
US-30	Montana Agricultural Statistics Service, Montana Wheat Varieties 2003 (18 July 2003).