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**CANADA/US FREE TRADE AGREEMENT
TRADE IN SERVICES**

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FINANCING AND OTHER ASSISTANCE TO SERVICES EXPORTS

I Export Credits and Insurance

(a) By Canada

INTRODUCTION

The Export Development Corporation provides a variety of financial services to Canadian exporters and foreign buyers in order to facilitate and develop export trade. It does this through a wide range of insurance, guarantee and loan services not normally provided by the private sector. All of these are applicable to services exports.

EXPORT LOANS

EDC has traditionally supported Canadian services exports with export financing on the basis of their association with the sale of large integrated packages of capital goods and services. Since early 1980, the Corporation has been prepared to provide greater direct loan assistance in respect of four specific types of services exports, i.e. (1) engineering and consulting studies; (2) engineering and consulting services; (3) feasibility studies; and (4) management or other consulting services. Previously, these services had been eligible for insurance but were not normally considered for direct loan assistance. (Criticisms of the existing system are appended as Annex C.)

As part of its export financing services, EDC now offers a forfaiting service. This involves the EDC purchase of promissory notes drawn by foreign buyers and made payable to the Canadian exporter. Since June 1981, when this program was introduced, no forfaiting transactions involving services exports per se have been concluded. However, in applying the methodology described in footnote 1 to Table 1 it is estimated that services exports of approximately \$40,000 have been supported by the EDC through forfaiting during the first four months of its availability.

Table 1 (Annex A) sets out the aggregate amount of EDC support to services exports as provided through its direct lending and forfaiting operations since 1977.

EXPORT CREDIT INSURANCE AND GUARANTEES

In addition to its financing facilities, EDC provides a wide range of insurance and guarantee services in support of Canadian exports. Almost any kind of transaction involving the export of goods, services or technology may be insured against a variety of credit and political risks beyond the control of the exporter.

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The scope and degree of credit cover available to exporters is broadly similar in each country, with the basic purpose of facilitating the mobilisation of funds for the extension of credit. Typically, the institution will issue credit insurance to the exporter covering both political and commercial risks of non-payment by the buyer, and will also issue a guarantee to the financial institution providing the required funds. Some countries, however, offer additional insurance facilities in such areas as surety requirements (e.g. performance bonds), foreign exchange risk and cost escalation. (See Table 4, Annex A).

B. Financing

In the few OECD countries such as Switzerland and Germany, official support for the bulk of export credits is restricted to the provision of insurance and guarantees as just described. Intense international competition for the sale of capital goods on credit has resulted, however, in the prevalence of export credit offers at interest rates that are at or near the minimum "Consensus" rates, and that are fixed for the duration of the credit, which may be as much as ten years or more. Such terms cannot be provided by the banking systems in most countries, without official financial support, i.e. some form of subsidy. Most OECD Governments, to keep their exporters competitive, have therefore developed mechanisms to ensure that funds will be available for export credit at competitive terms. In the majority of these countries, official financial support is provided to the banking sector, either direct to individual banks or through a specialised intermediary. In the remaining countries, the bulk of longer term export credits are provided direct by government agencies such as the Export Development Corporation.

The following paragraphs summarize and compare the main features of the medium- and long-term export credit financing systems of some of the major countries.

Those few systems where official support is generally limited to insurance and guarantees are sometimes referred to as "pure cover". In Switzerland, export credits are provided by the individual commercial banks, which raise the funds through the issue of fixed rate notes in the Swiss capital market. In Germany, the banks have formed a consortium, AKA, which refinances at market rates the export credits granted by its member banks. Certain German exports, mainly to developing countries, are eligible for official financial support through KfW, a Government institution that provides official credit at below market rates, or through a special rediscounting facility of AKA with the Central Bank. The volume of such operations is small in comparison with those under the "pure cover" system.

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For instance, Global Comprehensive Insurance is available for export sales made on short credit terms of up to 180 days. Specific Transaction insurance and guarantees are available for export sales on credit terms of up to five years. Performance related insurance and guarantees are available for Canadian exporters who are required to post security which guarantees performance. Finally, Foreign Investment Insurance is obtainable for a term of up to 15 years to cover certain kinds of investments made by Canadians in other countries.

Table 2 (Annex A) outlines EDC support of services exports through its insurance services.

CONCLUSION

Table 3 (Annex A) sets out the aggregate amount of support provided by EDC in support of services exports, in the broader context of Canadian service exports as defined in the Balance of Payments accounts. As can be seen, EDC's support of services exports is relatively small for the years under review. The proportion of total Canadian services exports (including travel, freight and interest and dividends and "other" services) supported by EDC is generally less than 4 percent. The 11.1 percent result in 1978 is the result of large transactions (i.e. - Insurance transaction in Saudi Arabia, nuclear project in Eastern Europe) supported by the Corporation and is considered an anomaly. To put EDC support of services exports in the proper perspective, it must be added that the Corporation's involvement with services is essentially limited to transactions under the Balance of Payments heading of "other" services. Using this narrower definition, it can be seen that EDC support is still relatively small at roughly 10 percent.

(b) By Others

Nearly all OECD Member countries provide some degree of official support to ensure the availability of medium - and long-term export credit as a means of promoting the export of capital goods and services although most countries' programs do not differentiate between goods and services.

A. Insurance Facilities

One feature common to all the systems is the assumption, by or on behalf of the government, of the bulk of the credit risk inherent in extending finance to foreign buyers. Every system has a specialised institution for this purpose, either an official body or one that acts in the state's name. These institutions are members of the Berne Union (International Union of Credit and Investment Insurers), through which they exchange creditworthiness information and seek to harmonize policies and criteria in the field of credit insurance.

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The remaining European countries have developed a variety of preferential refinancing and interest rate support facilities to lower the cost of market-sourced funding for export credits. In most cases, these result in the availability of fixed-rate export credits at or near the Consensus minimum interest rate.

In the UK, the individual banks can provide exports credits at consensus terms, and receive an interest rate subsidy direct from the Government to cover the gap between the credit and the normal bank lending rate. (The availability of refinancing the longer maturities through ECGD was discontinued in 1980.)

Elsewhere in Europe, specialised financial institutions have been established as the conduit for official financial support.

In Italy, the state-owned Mediocredito Centrale uses both public and market funds, with an interest subsidy from the Treasury to discount Consensus rate export credits extended by the commercial banks. Alternatively, it can provide an interest subsidy to those banks without discounting. In the Benelux countries, bank credits can be discounted at or near government bond rates, with the possibility of an interest rate subsidy (to Consensus levels) from the Treasury.

The Central Bank plays a role in reducing credit costs in France and Denmark as well. In France, official financing support is supplied in two forms, and is arranged through the BFCE. Credit duration of up to 7 years is financed by BFCE through a combination of market funds and special-rate borrowing from the Central Bank, in proportions that result in a Consensus-rate blend. Maturities beyond 7 years are financed by BFCE entirely from market funds, with an interest subsidy from the Treasury.

In other countries, government agencies have been established to provide official finance direct to the buyer, or the importer.

In the USA, Eximbank provides fixed-rate long-term credit to buyers, with funds borrowed from the market through the Federal Financing Bank. Its overall cost of funds is reduced by the retained earnings it has accumulated since its original capitalization. Eximbank lends only a portion (typically 45 per cent to 65 per cent) of the funds required for a credit, leaving the rest to be provided by the commercial banks (with official credit insurance) at floating rates. The bank-owned PEFCO, guaranteed by Eximbank, also provides export credits at long-term market rates.

The Eximbank of Japan provides the major portion of officially-insured export credit, both buyers' and suppliers', at fixed rates. The Japanese commercial banks provide the balance, also at a fixed rate. Eximbank borrows its funds from the postal savings system, and charges on its loans a rate that, when blended with other commercial banks' portions, will produce a blend consistent with the Consensus.

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Table 2 indicates the level of export financing support for services for major countries. This is similar for each country.

Although the OECD systems are similar, the USTR has identified the following practises as being subsidies to service exports:

- (a) financing of pre-bid surveys, insurance against cost inflation on construction contracts which enable some domestic concerns to enjoy a competitive advantage over foreign firms bidding for contracts in third countries. (France, Germany, Italy, Korea, Japan, Sweden and the United Kingdom);
- (b) subsidized financing provided to national companies competing in foreign markets through offering official credits or providing guarantees against losses to state owned or foreign nationals (countries not specified);
- (c) government counter guarantee of external and internal private banks financing (countries not specified);
- (d) official export credit agency guaranteeing a percentage of contractors profits if prescribed levels of export content are achieved in the contract (countries not specified);
- (e) subsidies on equipment and materials provided to national companies competing in foreign markets (countries not specified).

Other Forms of Assistance

1. In the United Kingdom the Overseas Project Group (OPG) co-ordinates government assistance by selecting potential projects and by providing special financing support - up to 50% of pre-contractual expenses which must be repaid if the U.K. firm wins the contract. This is comparable to Canada's PEMDA.
2. Japan provides special tax deductions for export transactions of technology transfer, patents, copyrights and consultant fees. In France a tax deferral reserve can be established by companies making industrial investments in certain foreign countries. This reserve can equal a maximum of 50% of the capital invested in the first 5 years of operations.
3. The U.S. provides tax incentives through the provision of the Domestic International Sales Corporation (DISC) legislation which permits U.S. corporations to establish export subsidiaries in order to defer, indefinitely, federal corporate income tax on up to 30% of export net income. To

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1980 Official Loan Support - Other Countries
\$ millions U.S.

| | <u>Total Support</u> | <u>Estimated Support For Services*</u> | <u>% Total Support For Services</u> |
|---------------------------|----------------------|--|---|
| <u>United Kingdom</u> | | | |
| product | 1,192 (69%) | 119 | 10.9 |
| project | 531 (31%) | 69 | |
| | <u>1,723 (100%)</u> | <u>188</u> | |
| <u>United States</u> | | | |
| product | 3,789 (66%) | 378 | 10.9 |
| project | 1,914 (34%) | 248 | |
| | <u>5,703 (100%)</u> | <u>626</u> | |
| <u>Japan</u> | | | |
| product | 1,785 (71%) | 178 | 10.8 |
| project | 718 (29%) | 93 | |
| | <u>2,503 (100%)</u> | <u>271</u> | |

* Estimated on the basis of 10% and 13% of product and project support respectively is for services.

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in April 1981 for 4 years at C\$2 million) provides for Canadian technical assistants to work at the Bank. A Canadian Project Preparation Fund was established at the Inter American Development Bank to provide financing for Canadian services related to IADB project preparation. A total of C\$6 million was contributed. In 1980 it was agreed to terminate contributions because no additional Canadian procurement resulted from the Fund, it was merely an alternate source of funding.

The Inter American Bank also has a fund for technical cooperation, which provides for services and Canada seems to have been relatively successful in procuring under this fund. Its total value was \$57 million in 1978, \$43 million in 1979 and \$32 million in 1980. A large proportion of IADB contracts have been awarded for services. For example, from January 1978 to October 1981, contracts worth US\$4 billion were awarded. Of this amount, US\$2.6 billion (or 65%) was for construction services while US\$126.7 million (or 3%) was for other services. During this period Canada competed for 10 contracts (valued at \$36 million) and won three valued at \$19 million. The World Bank has identified disbursements for consulting services, freight and insurance and training for 1980. Of total disbursements to Canada of US\$68 million, procurement of Canadian consulting services accounted for \$16,197,582, freight and insurance for \$413,276 and training for \$44,283. Total disbursements for all goods in 1980 was US\$5 billion.

Table 5 identifies the value of cumulative loans at the IFIs, excluding the Inter-American Development Bank, and indicates the relation between total technical assistance and projects. Many projects may have services associated with them but these cannot be easily identified according to value or country origin of service. Table 6 identifies Canadian procurement performance at the IFIs according to goods and services. In some cases procurement of services can be distinguished from goods.

Canadian commercial banks finance domestic service activity as well as exports of services but are unable to report separately the amounts directed to each. For example the Royal Bank is only able to indicate that total services loans outstanding as of October 1981, in all currencies (both domestic and foreign) amounted for \$157 million or about 1 percent of total loans of about \$19,400 million.

(b) Cost Recoverable Technical Assistance Program (CRTA)

The CRTA is a federal program implemented in 1979, designed to improve Canada's performance in exporting goods and services by providing government expertise on a cost recoverable basis to Canadian firms and to developing countries. The types of technical assistance made available are generally those which are compatible with Canadian supply capabilities in order to maximize the possibility of developing exports. This is particularly relevant for countries with similar geographic or resource characteristics to Canada.

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Canada's contributions to multilateral organizations are not tied to Canadian exports. Much of the benefits from procurement by these agencies generally goes to those exporters who are most aggressive in international bidding. Canadian performance in this area has not generally been very strong.

The third area of CIDA's involvement with concessional funding is its Industrial Co-operation Program. Given the complex dimensions of the North/South poverty gap, traditional development assistance, while essential, can provide only part of the answer. It would need to be complemented with other elements - for example, the resources and capabilities that already exist in the non-governmental sector. Besides its continuing support for a variety of non-governmental organizations engaged in international development, CIDA recently established the Industrial Co-operation Program to encourage the involvement of the Canadian private sector in the development of Third World countries. Although still relatively modest (\$7 million in 1980/81 - its second full year of operation) the program is flexible enough to respond to the many varied needs and capabilities of the private sector.

Under this program, the Canadian Project Preparation Facility (CPPF) was created in an attempt to overcome the difficulties Canadian firms seem to be having in obtaining contracts from international financial institutions. It is estimated that some \$30 billion in uncommitted sourcing is available from such institutions annually for development projects identified by developing countries. Canadian firms, particularly manufacturing companies, have been notably absent from these bidding processes.

The CPPF program enables Canadian companies/consultants on business development trips who manage to turn up opportunities which are at the conceptual stage in the developing country concerned, and for which there is a reasonable likelihood of financing being available from one of the international financing institutions, to provide project preparation (pre-feasibility) studies to developing countries to accelerate their industrialization and to developing countries to accelerate their industrialization and to facilitate Canadian participation in project implementation. CIDA believes that this gives the Canadian company/consultant a head start against international competition in bidding for the feasibility study for the main contracts. Although having a Canadian consultant on site need not necessarily bias the resulting project in favour of Canadian suppliers, it will at least give them a better competitive edge than when consultants are from other countries.

In addition, realizing that better access to Canadian technology would significantly improve the development capabilities of many of the world's disadvantaged nations, the Industrial Co-operation Program also established recently a Canadian Technology Transfer Facility (CTTF).

This enables Canadian firms to test and adapt their technology in developing countries as a lead-in to co-operation with their developing country counterparts. As with the CPPF, maximum funding for a project under the CTTF is \$250,000.

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The CIDA program is by and large a "response" program - to the expressed development needs of Third World countries, and to the extent our own capabilities and resources permit such action. In this development co-operation relationship, experience has shown that the major portion of CIDA's procurement of Canadian services has been not so much to respond to requests for services per se, but rather to help implement mutually agreed integrated bilateral development projects where services represent a key component.

III International Arrangements at the Intergovernmental Level

The OECD Arrangement on Guidelines for Officially Supported Export Credits regulates the use of export credits (See Annex B for a brief description of its origins and terms). The "Form and Scope of the Arrangement" defines its field of application as being export credits with a repayment term of two years or more. The definition of coverage thus focuses exclusively on medium and long term credits rather than export credits supporting sales relating to specific industrial sectors and economic activities. Paragraph 10 of the Arrangement however explicitly lists industrial sectors (Aircraft, nuclear power plant, military and agricultural products) which are expected from its coverage.

There are, however, references in the Arrangement to services. Both paragraphs 1 and 10 which deal respectively with rules for minimum cash payments and limits on local cost financing refer to exported "goods and services". In export credit jargon this expression is often understood to mean "related" services although in many large construction projects, services account for a very large proportion of the total contract value. Participants have not discussed whether the Arrangement would apply to the export of services alone - (or of goods alone!). As the question of whether services alone are covered will be raised in OECD work on services, it is likely that Participants in the Arrangement will be asked to address the issue.

Although there are various arguments that could be developed to support the thesis of either coverage or non-coverage of services alone, these arrangements would seem less important than what should be the Canadian view. On balance Canadian interest would seem to lie in obtaining clarification. There would seem to be few, if any, reasons for seeking an interpretation in favour of non-coverage which would mean that export credits for services would not be subject to international rules. Such an exclusion would only be useful if it meant, in actual practice, that medium term export credits would not be used to support the sale of services. It should be recalled that many countries felt that the inappropriateness of using medium term credits for military and agricultural products was a valid reason for excluding them from the Arrangement. In actual practice, these products are sometimes sold with medium term or concessional export credits.

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The Export Credits Arrangement is an agreement among OECD countries. Other countries (such as Korea, Israel, Brazil) some of which are major exporters of services, are not bound by its guidelines. Non-OECD countries which have signed the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the GATT have implicitly committed themselves to apply the minimum interest rate provisions of the Arrangement. They are not bound by the other credit term guidelines of the Arrangement. However, the GATT applies exclusively to trade in goods. Services are excluded and thus countries which are not signatories to the Export Credits Arrangement would appear to be exempted from international rules on export credit terms for services, assuming that these are in the purview of the Arrangement.

Berne Union

The International Union of Credit and Investment Insurers, known as the Berne Union, was established in 1934. It is a private association of 26 export credit and investment insurers representing 28 countries. Members of the Union include government agencies which are involved in export credit or foreign investment insurance as well as private companies with such responsibilities. Its purpose is "to work for the international acceptance of sound principles of export credit insurance and the establishment and maintenance of discipline in terms of credit for international trade." Beyond this technical mandate, the Union is involved in the coordination of an exchange of information among members. The Berne Union Secretariate collects and disseminates statistical data on members' country commitment levels, claims activities and other matters of interest, which are reviewed and updated on an ongoing and semi-annual or quarterly.

Berne Union members have, in the implementation of their mandate, agreed to limit their support for credit and insurance on specific commodities with less than 5 years repayment terms. The regulatory functions of the Union are not binding upon members' government. Membership in the Union is, however, considered to be of substantial value in terms of information flows.

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ANNEX A

TABLE I

EDC LOAN SUPPORT FOR SERVICES EXPORTS
1980 - 1981
(\$ Millions)

| | <u>1977</u> | <u>1978</u> | <u>1979</u> | <u>1980</u> | <u>1981</u> |
|--|-------------|-------------|-------------|-------------|-------------|
| "Services Transaction" Loans | -- | -- | -- | 7.7 | 3.8 |
| Other EDC Loans ¹ | | | | | |
| - support for projects | 64.3 | 57.6 | 86.9 | 51.1 | 44.1 |
| - support for products | <u>55.7</u> | <u>49.9</u> | <u>75.3</u> | <u>44.3</u> | <u>38.2</u> |
| TOTAL | 120.0 | 107.5 | 162.2 | 95.4 | 82.3 |
| Forfeiting | <u>--</u> | <u>--</u> | <u>--</u> | <u>--</u> | <u>.04</u> |
| Aggregate Loan Support for Services Exports | 120.0 | 107.5 | 162.2 | 103.1 | 86.14 |

- 1) For the purpose of this study, EDC loans are allocated between "Product" and "Project" transactions on a 60 per cent - 40 per cent basis. The service component is then derived by assuming that 10 per cent of "Product" and 13 per cent of "Project" loans support services exports. Project sales tend to have a larger services component than product transactions because they tend to be specially adapted to specific requirements.
- 2) 1981 statistics as at September 30.
- 3) Excludes all forms of bank participation, as well as EDC bank guarantees.

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ANNEX A

TABLE II

EDC INSURANCE SUPPORT FOR SERVICES EXPORTS
1977 - 1980
(\$ Millions)

| | <u>For Year Ending Dec. 31</u> | | | |
|---|--------------------------------|--------------|--------------|--------------|
| | <u>1977</u> | <u>1978</u> | <u>1979</u> | <u>1980</u> |
| Global Comprehensive Insurance | 2.7 | 15.8 | 27.9 | 22.5 |
| Specific Transaction and Performance-Related Insurance and Guarantees | <u>143.0</u> | <u>955.9</u> | <u>123.7</u> | <u>238.1</u> |
| TOTAL | 145.7 | 971.1 | 151.6 | 260.6 |
| Foreign Investment Insurance Outstanding at Year End ² | 20.9 | 11.1 | 11.0 | 8.3 |

Notes:

- 1) 1981 statistics currently not available.
- 2) Foreign Investment Insurance statistics relate to maximum liability at year end while the Global Comprehensive Insurance and Specific Transaction on Performance Related Insurance and Guarantee statistics relate to the volume of business facilitated during the year. The methodology applied in estimating the services component of EDC's loans activity was not considered appropriate for the insurance activity because the services component is deemed negligible where it is not reported specifically.

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ANNEX A

TABLE III

EDC SUPPORT TO SERVICES EXPORTS
AND CANADIAN SERVICES EXPORTS
1977 - 1980
(\$ Billions)

| | <u>1977</u> | <u>1978</u> | <u>1979</u> | <u>1980</u> |
|--|-------------|--------------|-------------|-------------|
| Canadian Services Exports ¹ | 8.348 | 9.785 | 11.812 | 14.088 |
| - Other Services ¹ | 2.106 | 3.707 | 4.185 | 5.185 |
| Aggregate EDC Support to Services Export | | | | |
| - loans | .120 | .107 | .162 | .103 |
| - insurance ² | .146 | .972 | .152 | .261 |
| - TOTAL | <u>.266</u> | <u>1.079</u> | <u>.314</u> | <u>.364</u> |
| EDC Support as % of Total Canadian Services Exports | 3.2% | 11.0% | 2.7% | 2.6% |
| EDC Support as % of "Other Services" Exports | 12.6% | 29.1% | 7.5% | 7.0% |

Notes:

- 1) Source: Statistics Canada
- 2) Excluding Foreign Investment Insurance

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ANNEX A

TABLE IV

Loans and Technical Assistance

| <u>Bank</u> | <u>Date</u> | <u>Loans</u> | <u>(\$US m.) Fiscal 1981</u> | <u>Technical Assistance 1981</u> | <u>% of Tech. Assistance to Loans</u> |
|------------------|-------------------|-------------------|--------------------------------------|--|---|
| | <u>1981</u> | | | | |
| World Bank | \$ June 30 no. | 68,150.3 2,015 | 8,808.9 | 49.5 | 0.56 |
| IDA | \$ June 30 no. | 24,051.9 1,079 | 3,482.1 n. a. | 81.6 | 2.34 |
| IFC | \$ June 30 no. | - | 810.67 | - | - |
| | <u>1980</u> | | <u>Fiscal 1980</u> | <u>1980</u> | |
| AsDB | \$ Dec. 31 no. | 5,652.7 n. a. | 1,435.72 58 | 8.37 | 0.58 |
| Other Sources | | - | - | - | 1.09 |
| AfDF | \$ Dec. 31 no. | 1,055.3 177 | 720.23 - | n. a. | - |
| AfDB | \$ Dec. 31 no. | 1,355.2 265 | 670.58 63 | 10.01 | 1.49 |
| CDB | \$ Dec. 31 no. | 309.61 - | 40.60 | 2.8 | 6.90 |

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ANNEX A

TABLE V

Canadian Procurement Performance at the IFI's

Asian Development Bank

'000 U.S. DOLLARS

| | <u>1979</u> | <u>1980</u> | <u>Cumulative 1967-80</u> |
|--------------------------|-----------------|---------------|---------------------------|
| Goods & Related Services | 13,485 | 32,431 | 111,000 |
| Services | 4,143.6 | 8,394 | 24,470 |
| TOTAL | <u>17,628.6</u> | <u>40,825</u> | <u>135,470</u> |

Caribbean Development Bank

| <u>\$CDN.</u> | <u>1979</u> | <u>1980</u> | <u>Cumulative 1975-80</u> |
|--------------------------|------------------|----------------|---------------------------|
| Goods & Related Services | 393,800 | 90,000 | 706,800 |
| Services | <u>1,164,000</u> | <u>212,800</u> | <u>2,502,700</u> |
| TOTAL | <u>1,557,800</u> | <u>302,800</u> | <u>3,209,800</u> |

African Development Fund

| <u>\$U.S.</u> | <u>1979</u> | <u>1980</u> | <u>Since Joining</u> |
|------------------------|-------------|-------------|----------------------|
| All goods and services | 1,107,900 | 1 8,600 | 2,321,000 |

IBRD/IDA

Cumulative procurement of all goods and services since joining:
IBRD U.S. \$514,900,00; IDA U.S. \$129,100,000.

Inter-American Development Bank (actual disbursements)

| <u>\$Cdn. '000</u> | <u>1978</u> | <u>1979</u> | <u>1980</u> | <u>1981 Jan-Jun</u> | <u>Cumul. '72-80</u> |
|--------------------------|--------------|---------------|---------------|---------------------|--------------------------|
| Goods & Related Services | 3,646 | 22,325 | 15,451 | 2,580 | |
| Services | <u>1,626</u> | <u>6,135</u> | <u>1,244</u> | <u>221</u> | |
| TOTAL | <u>5,272</u> | <u>28,460</u> | <u>16,695</u> | <u>2,801</u> | <u>82,400</u> |

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TABLE VI

Official Support for Exports of Goods and Services

| Program | | INSURANCE AND GARANTEES | | | | | |
|----------------|-----------------------|-------------------------|-----------------|------|------------------|-----------------|--------------------|
| Country | Agency | Political Risk | Commercial Risk | Bond | Foreign Exchange | Cost Escalation | Foreign Investment |
| Canada | EDC | X | X | X | | | X |
| United States | EXIM FCIA PEFCO | X X | X X | X | | | |
| Japan | EID | X | X | X | X | | |
| Franch | COFACE | X | X | X | X | | |
| United Kingdom | ECGD | X | X | X | | X | X |
| Germany | HERMES | X | X | X | X | | |
| Italy | SACE | X | X | X | X | X | X |

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ANNEX B

OECD EXPORT CREDITS ARRANGEMENT

The "Arrangement on Guidelines for Officially Supported Export Credits" is an informal agreement among most OECD countries which sets guidelines for credit conditions as a way of limiting competition in export credits. The Arrangement originated on July 1st 1976 among the Economic Summit Members (as the "Consensus" or "Gentlemen's Agreement") and by 1978 all other participants had adhered.

The main guidelines of the Arrangement are those setting maximum credit maturities and minimum interest rates. These take account of the state of economic development of recipient countries. Maximum credit maturities are 8½ years for relatively rich and intermediate countries. Relatively poor countries are subject to a maximum credit maturity of 10 years.

Minimum interest rates are as follows:

| Credit Maturity | 2-5 years | 5-8½ years | 8½-10 years |
|------------------|-----------|------------|-------------|
| Country Category | | | |
| Relatively Rich | 11.0 | 11.25 | N/A |
| Intermediate | 10.50 | 11.0 | N/A |
| Relative Poor | 10.0 | 10.0 | 10.0 |

The Arrangement guidelines also set minimum cash payments (15% of contract value), limits on local cost financing, and prescribe how principal and interest payments should be made. The Arrangement requires Participants to follow well defined procedures in cases where they intend to disregard the credit term guidelines. These procedures ensure transparency and give other Participants the opportunity to match, the threat of which is intended to ensure compliance with the guidelines.

This matrix of rates became effective on 16 November 1981 as part of an interim after 18 months of difficult negotiations. The agreement also stipulated that official credits in currencies whose market rate is inferior to the rates set out above would be subject to a uniform minimum rate of 9.25% and called for the negotiation of further increases in minimum rates in the spring of 1982.

Negotiations on further increases in minimum interest rates will open in Paris in March of 1982. Although no proposals have been tabled on a range of new minimum rates, most Participants accepted last November's compromise on the understanding that there would be a presumption of movement towards market interest rates. Negotiations

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will also address the question of how to ensure that Arrangement rates are kept in line with market developments. It is unlikely that it will be possible to establish a system which ensures automatic adjustment in rates, but some form of framework for review and adjustment of rates will have to be considered.

Negotiations are also expected to cover a number of proposals for other changes in the Arrangement and for the extension of its coverage to sectors now excluded. The proposals are as follows:

- increase in minimum cash payments for rich countries from 15 to 20%;
- decrease in the maximum repayment term for rich countries from 8% to 5 years;
- local cost support for intermediate countries would be limited to insurance and guarantees (official i.e., subsidized financing would no longer be permitted) as is now the rule for rich countries;
- reduction of the repayment term for conventional power plant from 12 to 10 years for all country categories;
- inclusion of nuclear power plant under the Arrangement at the same terms as those for conventional power plant;
- inclusion of aircraft at interest rates and maturities which remain to be worked out;
- special rules for agricultural credits.

There is also a possibility that proposals will be made for the reclassification of recipient countries. Negotiations may also touch on the issue of stricter application of guidelines of the Arrangement. If this question arose it would be aimed essentially at the Canadian practice of disregarding the Arrangement maturity guidelines. Canada frequently offers longer term to offset its higher than Arrangement minimum interest rates. Canada, which has been frequently criticized in the past for these practices, could very well be faced with proposals to be more assiduous in the application of the guidelines.

It is difficult to predict at this stage what will be the outcome of the negotiations. Much will depend on the attitude of the EEC. A major hurdle that had to be overcome before reaching last November's interim agreement was the treatment of official credits in currencies whose market rates would be below the minimum rates of the Arrangement. At that time official credits in Japanese yen became a major stumbling block. Similar difficulties could arise in the forthcoming negotiations particularly as there will be more currencies whose market rates would be below higher Arrangement matrix rates.

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ANNEX C

CRITICISMS OF EDC BY SERVICES EXPORTERS

EDC deals with a number of private sector interest groups such as the Canadian Exporters Association and the Canadian Manufacturers Association regarding general export financing and insurance issues. For the purposes of this paper, however, the criticisms made by the Association of Consulting Engineers of Canada (ACEC) will be considered representative of the concerns of the "services" sector in general.

EDC, as indicated in our earlier submission, responded to a major need of the ACEC members when it announced that it is prepared to provide greater direct loan assistance in respect of a variety of services exports. In recent months the ACEC has raised several other issues which it feels should be dealt with in the area of export financing. These are as follows:

- more effective parallel financing with International Lending Agencies;
- broader availability of low cost financing for feasibility studies;
- a more aggressive application of the credit-mixte facility; and,
- establishment of cost escalation and currency fluctuation insurance.

EDC has recently undertaken a number of initiatives in the provision of more effective parallel financing with international lending agencies. EDC continues to offer parallel financing with CIDA, as a preferred approach to credit-mixte financing discussed below, and the two organizations are currently working to further improve coordination in arranging timely lending packages. While the operating criteria of each agency must be satisfied, priority markets and project categories of mutual interest are identified on an ongoing basis. EDC also considers the development of a closer working relationship with multilateral banks to be an area of great potential and has recently established a new group within the Corporation to develop these relationships.

In requesting the broader availability of low cost funds for feasibility studies and a more aggressive application of the recently established credit-mixte facility, the ACEC is effectively seeking greater subsidization in export financing. The Corporation is not in a position to offer the highly subsidized financing which the ACEC is seeking since it must operate within the financial framework established by the government. Essentially, the Corporation is required to provide its service to Canadian exporters in a manner which normally would not require government appropriations. Where credit-

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mixte is concerned, EDC must apply the program criteria which were established by the government. As you know, this program was conceived as a defensive mechanism designed only to match the credit-mixte financing being offered by other countries. It is not as a mechanism to provide low cost financing across the board.

The ACEC has requested that EDC offer insurance coverage for the risks of cost escalation and currency fluctuation. The possibility of establishing these services has been examined in the past. On the basis of the review of a number of related alternatives as well as the experience of foreign export credit agencies such as those of England and France, it was concluded that the costs of insurance programs to cover this risk would be prohibitively large.

No means of sustaining such programs on a commercial basis has been identified to date. Accordingly, they would be expected to require significant government subsidization. For example, during 1979, a cost escalation scheme cost the French Government \$470 million in subsidies and in 1979/80 the British agency lost over £40 million on its currency fluctuation program alone. The subject is complicated somewhat by GATT provisions against the establishment of such programs where premium rates are manifestly inadequate to cover long term operating costs. Canada has urged against subsidies of this nature and has been critical of the French and British schemes of their implicit subsidy element. Nevertheless, EDC intends to undertake further studies to examine feasible means of introducing these services.

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FINANCING FACILITIES SPECIFICALLY AIMED AT SERVICES

| COUNTRY | FACILITY |
|-------------|--|
| BELGIUM | Comprehensive insurance agreements for whatever the duration of the credit (i.e. no maximum or minimum duration) |
| SWITZERLAND | Guarantees to banks for mixed credits for up to 5 years with a grace period of 3 years (more aid than commercial in interest) |
| KOREA | Provides technical service credits in the form of supplier credits. Interest rates are 8-9% annually and often carry a 1-2 year grace period |
| BRAZIL | A Special Export Financing Fund used to support the sale of technical studies and for engineering projects. Credits are extended for a 1-5 year duration with an annual interest rate as low as 7% |
| TAIWAN | Provides guarantees for engineering firms to undertake foreign construction projects |

OILFIELD AND OILFIELD SERVICES

DESCRIPTION OF CANADIAN INDUSTRY

Definition and Types of Services

The Canadian petroleum industry includes over 700 oil exploration and production companies operating on land in Western Canada, in the offshore, and in the Arctic. When an oil company decides to drill a well, this sets in motion the hiring of numerous other companies and individuals whose sole purpose is to drill the well, prepare it to produce, complete and maintain it. These companies make up what is known as the exploration contracting, oilfield service, supply and manufacturing sector of the petroleum industry. This means that the oil companies function like general contractors, with the substantive work being sub-contracted to the so-called "service" companies. The types of services required are identical in each of the industry's geographical regions although special problems such as the environment and other general drilling conditions in the offshore and Arctic necessitate some ingenious and innovative adaptations. The special circumstances of the Arctic and the East coast offshore will be discussed subsequently. However, for ease of presentation, the service companies can be grouped into five major categories, each of which comprises a number of specialized services. These categories are:

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- a) pre-drilling
- b) drilling
- c) well completions
- d) support services
- e) supply houses (and manufacturing)

Pre-drilling encompasses services that are carried out before a well is bored. Included are geophysical contractors, land agents, construction and transportation service companies. Drilling services are those executed at the well bore such as drilling contractor services (which comprise the single most important item in terms of cost of service representing approximately 30 % of the total cost of bringing a well on stream), mud services, cement services, logging services, testing services, coring and fishing services and safety services. The services required to bring a well into production and maintain its flow of oil and gas are called well completion services. The types of specialized services include perforating and stimulating services, as well as the mechanical contractors that install the pumping and gathering equipment. The support category includes all the services that may be called upon at any stage of the operation to supplement or complement existing expertise. These support services include geological and geophysical consultant services, production services, economic and financial consultants, environmental consultants, caterers, data processing consultants and training organization services. Associated with these four categories are the

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general supply houses and equipment manufacturers. The supply houses are oilfield "department stores". Several of the large foreign-controlled supply companies such as National Supply Co. and USS Oilwell Supply Co. are connected with manufacturers of oil and gas equipment, and appear to account for a substantial portion of the \$700 million of annual imports of oilfield equipment.

Size of Canadian Industry

The exploration contracting, oilfield services and supply companies, together with the small domestic manufacturing segment provide employment for over 50,000 people, mostly in Western Canada. The total cash expenditure of the petroleum industry in 1980 was \$14.3 billion of which \$7.9 billion or 55% were spent for services and equipment related to the exploration for and development of oil and gas wells. Every time a typical oil well is drilled about 48 companies are required to bring that well into production; 725 person days of employment are created for at least 175 different people; over \$500,000 is spent on acquiring these goods and services.

The value of the equipment utilized by the 48 companies involved in the drilling and completion of a typical well exceeds \$15 million. Gross sales for service companies for 1981, reported in a recent industry survey, amounted to approximately \$1.3 billion.

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About 85% of the number of companies in the "service" industry are Canadian owned and controlled. However, in the high technology (and high profit) segments such as well logging and stimulation, the dominant firms are subsidiaries of foreign companies. For example, the Canadian well logging market comprises three large companies, of which two are subsidiaries of foreign MNE and the third is U.S. controlled with a 35% Canadian interest. Respective market shares are:

| | | |
|---------------------|-----|-------------------|
| Schlumberger | 65% | U.S. controlled |
| Dresser Titan | 15% | U.S. controlled |
| Computalog Gearhart | 15% | Minority Canadian |
| Other | 5% | Mostly Canadian |

Exports and Major Markets

With the exception of some drilling and consulting companies, very few Canadian oilfield service companies have extended their operations abroad. Examples of Canadian controlled drilling companies that operate outside Canada include: Bow Island Drilling, Canadian Marine Drilling, and Challenger International Services and Westburne Drilling (Canada) Ltd. Some of the major Canadian consulting companies in conventional oil and gas are: Canocean Resources Ltd., Fenco Consultants a Division of Lavalin Inc., and Tri Ocean Engineering Ltd. Typically the key services carried out on major well sites in most of the free world countries are performed by subsidiaries of large

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multinational enterprises such as Dresser Industries, Halliburton, and Schlumberger. These firms have established international reputations and the oil companies tend to use these established firms rather than assume the risks inherent in using what they may regard as unproven and relatively inexperienced contractors. (It is not unusual for an operator to contract for the services of a recognized firm like Schlumberger and accept a premium of up to 30% over the bid of a smaller Canadian firm because of Schlumberger's reputation of reliability, and in order to minimize down time. In the operator's assessment, the potential cost of time lost in drilling with an "unproven" contractor is much greater than the extra cost incurred for hiring the MNE). Moreover, the segmentation of world markets by MNE's has tended to preclude Canadian subsidiaries from bidding and competing worldwide against their affiliates.

Most of the Canadian service firms, especially in the high technology segments, lack the financial resources, experience and scale of operations to service Canadian offshore or Arctic operations, let alone export to the international market. There have been a few exceptions in the last two years arising from the downturn in Canadian activity and oil price deregulation in the U.S. A few firms such as Canadian Fracmaster, and Canadian Perforators have established subsidiary companies in the U.S. in response to the strong demand for services. Based on a limited survey of leading companies actual gross revenues for oilfield services exported to the U.S., are quite modest,

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totalling less than \$10 million in 1981. There has been some export of services to other countries, such as Australia, but in most instances the Canadian firms have set up foreign subsidiaries, and thus their revenues are not regarded as the export of services. If as expected the lower level of oil exploration in North America persists, it does not seem that the export of Canadian services is likely to grow substantially in the near to medium term.

Imports

Very little information is available concerning imports of oilfield services on land-based conventional producing areas, although industry sources indicate that they are relatively low. Imports for offshore and Arctic operation, by comparison are relatively high. Included are the services provided by drilling platforms, dredge ships used in building artificial islands and some supply vessels. (It is interesting to note that in most circumstances, foreign owned drilling vessels imported for use in Canada are equipped with service equipment belonging to the large international service companies like Schlumberger. Because this equipment is built to meet their specific standard operating procedures, no other firms can provide the service unless they replace the specialized equipment). We estimate that the total value of service for these imports in 1981 amounted to approximately \$160 million. (Of greater significance, of course, is the direct import of oilfield equipment, which is running in the order of \$700 million annually).

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CANADIAN REGULATIONS, POLICIES AND LEGISLATION

The principal regulations and policies governing the oilfield service sector are:

(a) FEDERAL LEGISLATION

Exploration contracting and related services may be subject to review under the Foreign Investment Review Act, or to provisions of the Canadian Oil and Gas Act, the latter inspired by objectives set out in the National Energy Program. Specifically:

Foreign Investment Review Act

In the energy sector, any acquisitions by foreign interests of service companies, or the establishment of new energy-related service companies by foreign interests are subject to Government review under terms of the Foreign Investment Review Act, which first came into force in 1974. The compatibility of such proposals with national energy policies is included in one of the five factors considered by Government in determining whether or not the investment is of significant benefit to Canada. The National Energy Program (NEP) stated the objective of increased Canadian participation in the oilfield service sector, so that regardless of which companies undertake the work, Canadians have an opportunity to derive increased benefits associated with such activity.

Canada Oil and Gas Act

Under sections 10 and 76 of the Canada Oil and Gas Act, the Canada Oil and Gas Lands Administration is (COGLA) responsible for reviewing proposals by oil companies seeking exploration and production rights in Canada Lands. An applicant's contracting and procurement plans are scrutinized for industrial, employment, and general economic benefit contribution. Initial negotiations are supplemented by annual reviews.

Canadian Tariffs and Excise Tax

Over 75% of all imports of equipment used by the oil and gas sector are duty free. This is particularly true in the offshore where goods are free of duty when "of a class or kind not made in Canada" is applicable. In Canada, rigs, platforms and vessels are deemed to be "made" in Canada and therefore are dutiable, while most other equipment fall in the duty free category. However, rigs, platforms and vessels may enter Canada on a temporary basis (up to one year) if no such Canadian equipment is available. Payment of 1/120th of the total duty for each month of operation within Canadian waters is assessed. Current tariffs on rigs, platforms, vessels and associated equipment are 10% under MFN, 5% under BP or GP. Drill pipe is accorded duty free entry while well casings are dutiable at 9.5% MFN or 5% BP or GP.

Other Federal Regulations

In addition to the specific legislation described above, Canada has blanket legislation that monitors and controls immigration and temporary work permits through the Canadian Immigration Act. COGLA and the Department of Employment and Immigration have signed a memorandum of understanding to permit Canadian manpower objectives to be reflected in agreements with respect to Canada Lands.

(b) PROVINCIAL LEGISLATION

At least two provinces have enacted legislation regarding the oilfield service sector. Newfoundland's Petroleum and Natural Gas Act of 1977 spells out specific regulations concerning disclosures of well information, along with education, training, research and development provisions, preference in the hiring of local labour and the procurement of local goods and services. For example, in order to obtain a permit or lease, a company must give preference in relation to the provisions of goods and services to firms owned or controlled by residents of the province and to firms incorporated in the province at least 51% of the shares of which are held and beneficially owned by Newfoundlanders; if this does not yield a bid that is "competitive in terms of fair market price", exploration companies must alternatively, seek bids from service and supply firms that conduct and manage their operations from a permanent establishment in the province, and in which

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the majority of employees engaged in the business are resident in the province. Moreover, each company must present to the Government a complete listing of total expenditures made in relation to its petroleum activities within six months of the issuance of a permit or lease. The Government of Nova Scotia has passed similar legislation under its Petroleum Resources Act, although not quite as restrictive as the Newfoundland law.

IMPEDIMENTS TO CANADIAN EXPORTS

Only limited information is available concerning the policies, legislation, and administrative practices of other countries as these affect the ability of Canadian oilfield service firms to export their services. The information that is available concerning the policies of other OECD energy producing countries indicates that, with some significant exceptions, formal legislation to govern the import of services has not been enacted.. Rather, they have employed informal but highly effective arrangements to maximize procurement of domestic goods and services.

The United Kingdom in 1975 established an Offshore Supplies Office (OSO) within its Department of Energy to promote and develop domestic sources of oilfield equipment and services. In that year, the OSO reached an agreement with the Offshore Operators Association (OOA) in the form of a Memorandum of Understanding and an Associated Code of

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Practice. The Memorandum contains a comprehensive description of how purchases should be carried out and provides for the direct involvement of the OSO in procurement process. Members of the Offshore Operators Association have undertaken to provide U.K. manufacturers, consultants, contractors and service companies with "a full and fair opportunity to participate in the supply of goods and services required for U.K. offshore hydrocarbon activity". Prior notification to the OSO is required regarding any intent to purchase materials and manufactured goods valued over 100,000 from non-U.K. sources, or regarding the placing of contracts for construction and services over 500,000 with non-U.K. contractors. We understand that there have been few, if any, instances in which a private operator has elected to source outside the U.K. against the advice of the OSO.

The United States has a number of legislative measures in place which strongly support domestic sourcing for major projects where government fundings is involved. These include, notably, the Buy America Act of 1933, which requires that: 1) federal government agencies purchase only domestic products unless U.S. supplies are unavailable in sufficient quantities or satisfactory quality or 2) the purchase of domestic supplies would be "inconsistent with the public interest", or their cost would be unreasonable. Private procurement practices are affected by the Merchant Marine Act (i.e. the "Jones Act"), which provides that coastal and fresh water shipping either directly or indirectly between points in the U.S. must be carried out

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in vessels built and registered in the U.S. and owned by U.S. citizens. This Act also prevents the use of foreign built supply vessels and tankers in offshore hydrocarbon exploration and development activities.

In 1975, Norway instituted legislation concerning oil and gas operations on its continental shelf, which stipulated that the "licencee shall use Norwegian goods and services in the activity as far as they are competitive with regard to quality, service, schedule of delivery and price". Oil companies are required to send to the responsible Minister all bidding lists on contracts over \$200,000, and the Minister may add names to the lists. While the final procurement decision still rests with the private operator, the Norwegian Government compiles statistics indicating the percentage of domestic goods and services used by each company, and these statistics are used in considering the issuance of new exploration and production licences. The percentage of Norwegian goods and services used in offshore oil and gas activity reportedly increased from 28% in 1975 and 62% in 1978.

Notwithstanding the existence of legislative and administrative impediments in other countries, the largest current constraint on the export of Canadian oilfield services seems to be the relatively small size of the Canadian companies. This is due in certain sub-sectors, like logging and stimulation, to the dominant position in the Canadian market held by MNE companies, and the dominant position that the same MNE companies hold in foreign markets. This illustrates the inter-relationship between investment and trade issues affecting oilfield services.

POLICY CONSIDERATIONS

Over the next decade and perhaps longer, the focus of exploration and development activity in Canada may tend to shift from conventional oil and gas producing areas in Western Canada to frontier areas in the offshore east and west coasts and in the Arctic. This shift in focus will be impelled both by more promising geologic potential in frontier areas and by the design of federal fiscal incentives, which are directed at increasing frontier exploration. The frontier regions offer a new and more challenging environment for exploration activity, and require the use of equipment and services which, it now appears, will be more costly, specialized and technically advanced than those used to date in conventional areas. Indeed, the geography and climate of Canada's North appears to offer Canadian service firms a unique opportunity to develop new generations of equipment and related services, and to market this equipment and services in other parts of the world.

Canada has not yet articulated a comprehensive policy vis-à-vis the development of the oilfield service sector. The National Energy Program stated the Government's intention to ensure that a high level of Canadian goods and services is employed in oil and gas activities, especially in the tar sands and in Canada Lands. The passage of the Canada Oil and Gas Act has provided the legislative authority to give effect to part of this objective through the negotiation of exploration

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agreements and the issuance of permits. Other legislative measures are under consideration. Future policy options will include taking measures to increase the demand for Canadian oilfield goods and services and taking measures to increase the supply of such goods and services through direct and indirect assistance (e.g. support for increased domestic research development, demonstration and commercialization). Further policy, of course, must reconcile the competing objectives of stimulating the growth of the domestic services sector and maintaining access to foreign-based technology. It seems reasonable to expect that foreign-based firms and their subsidiaries in Canada will continue to play a major role in the oilfield service sector, but that Government policy, particularly at the federal level, will seek to encourage the growth of Canadian owned firms, particularly in new technology areas.

SUITABILITY FOR INTERGOVERNMENTAL NEGOTIATIONS

Accordingly, Canadian objectives in any future multilateral negotiations would appear to be the following:

- a) to promote greater acknowledgement of the inter-relationship between investment and trade issues;
- b) to preserve the right of national governments to take appropriate measures to promote the growth of domestic service industries;
- c) to demonstrate that Canadian policies, as manifested in FIRA and

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COGLA, simply offer "full and fair opportunity" to Canadian suppliers on a competitive basis, without discriminating against foreign interests;

- d) to seek to negotiate greater acceptance of MNE subsidiaries' ability to act freely in all trade matters, possibly on the basis of specializing in particular services on a global level i.e. a type of "product mandate" in services.

AIR TRANSPORT

I. Description of the Canadian Air Transport Sector

The Canadian Air Transport Industry consists of three categories of air carriers: national, regional and local. In 1980, the industry generated nearly \$4 billion in operating revenues and employed 47,000 people.

Canada's national carriers are the publicly owned Air Canada and the privately owned CP Air. The two carriers in 1980 generated 48% (\$1.9 billion) and 17% (\$680 million) of the industry's revenues and employed one half and one fifth of the total labour force respectively.

Air Canada and CP Air both operate scheduled services between principal centres in Canada. Internationally, Air Canada provides scheduled services to points in the United States, the Caribbean, United Kingdom, France, West Germany and Switzerland, while CP Air operates scheduled services to points in the United States, (including Hawaii), Peru, Chile, Argentina, Japan, Hong Kong, Fiji, Australia, Holland, Italy and Portugal. However, the nationals are not serving the following countries to which they are permitted to operate: Austria, Czechoslovakia, Belgium, China, Denmark, Finland, Ireland, Israel, Mexico, Morocco, Norway, Pakistan, Panama, Poland, Spain, Sweden, and the USSR. Both carriers are involved in charter operations and maintain sales offices in several other countries around the world.

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The regional air carrier category consists of four airlines: Eastern Provincial Airways (EPA) with operations in the Maritimes; Quebecair, mostly in Quebec; Nordair in Ontario, Quebec and the eastern Arctic; and Pacific Western Airlines (PWA) in the four western provinces, the Yukon and western and central Arctic. Two of the Regionals are privately-owned; Nordair is a subsidiary of Air Canada and PWA is owned by the Alberta government. In addition to their scheduled domestic services, the Regionals operated extensive charter services to holiday destinations. The four carriers in 1980 generated 12% (\$496 million) of the industry's revenues, and employed 14% (6,403) of the total labour force collectively.

In a category virtually by itself is Wardair, a private charter operator with a fleet of large widebody aircraft, with regular domestic transborder and transatlantic services.

The rest of the Canadian air carrier industry, the local service air carriers, consist of roughly 800 companies of various sizes operating in all parts of the country. The locals are an essential component of the total system, performing a variety of services, such as feeder type operations, charters, exploration and northern supply functions. In 1980, this segment of the industry generated 23% (\$904 million) of total revenues and employed 18% (8,656) of the labour force collectively.

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Results of recent studies dealing with the performance of the air carrier industry indicate that Canadian airlines as a group have recorded rates of return comparable to or slightly higher than those of the Civil Aeronautics Board (CAB) certificated carriers in the United States and lower rates of return than the other industrial sectors.

II Foreign Activities in Canada

In 1978, the total volume of Canadian international air origin and destination (O/D) traffic (carried on both scheduled and charter services) was estimated to be 12.6 million passenger trips*. Traffic to and from certain countries/regions was much greater than to others. For example, in 1978 Canada-U.S. O/D traffic accounted for over half of this volume. Together the U.S., Europe and Caribbean markets accounted for over 90% of the total traffic. Traffic volumes to the Middle and Far East regions, although growing strongly, have relatively small traffic bases; the implication is that their relative size will improve but not so much as to significantly alter the general traffic distribution profile as it exists today.

* Defined as a one-way passenger journey. For example, a passenger travelling from Montreal to Paris and return is shown as two distinct passenger trips.

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It has been estimated that the gross revenue value of Canadian international O/D passenger traffic was over \$2 billion in 1979. The relative distribution of gross revenue is slightly different than that reflected by the regional distribution of passenger volume mentioned above, primarily because the longer the trip, the larger the average dollar value and different average yields (average revenue per mile). As a result, the gross revenue attributable to the traffic from Canada to the Middle and Far East will be greater relative to that to the U.S. and that reflected by the size of the passenger market.

There are, at present, four Canadian and 38 foreign airlines authorized to operate scheduled air services to and from Canada, and 5 additional Canadian and 77 additional foreign airlines authorized to operate international charters, although most of these do not in fact regularly participate in the charter market.

Canadian carriers have had mixed results in competing in the international air transport market. In charter services, Canadian carriers have generally fared extensively well, carrying, in almost all cases, the vast majority of the traffic. This has been attributed to the fact that a large proportion of the traffic is of Canadian origin and to Canadian regulations relating to charter operations.

While Canadian carrier performance in competitive scheduled service markets* has not matched that achieved in the charter service,

* Markets which have service by both a Canadian and foreign carrier.

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with the exception of U.S. market, Canadian carriers have fared quite well. In the Canada-U.S. scheduled market Canadian carriers carried only about 40% of the traffic and accrued a comparable share of the revenue derived from this traffic. A recent study has concluded that this imbalance did not arise from any inherent inability of Canadian carriers to compete effectively in the market-place, all things being equal, but rather that the imbalance arose from the structural advantages of airline networks, and demographic and geographic factors beyond the control of either Canadian carriers or bilateral agreement. Furthermore, the agreement on southbound preclearance, which is of tremendous benefit to the Canadian and U.S. travelling publics alike, allows the U.S. carriers to better capitalize on certain geographic and demographic advantages, such as the greater number and higher density of markets behind U.S. gateways compared to markets behind Canadian gateways.

The extent to which Canadian air carriers are able to compete effectively in the international market-place has certain implications to the airfare account* of Canada's international balance of payments. The latest figures (for 1977) although incomplete, show a B.O.P. deficit of \$319 million, i.e. \$299 million for passenger operations alone, on receipts of \$302 million, and a deficit of \$20-million for non-passenger services, from receipts of \$39 million. This is a

* Defined as the revenue derived by Canadian airlines from foreign residents less the revenue derived by foreign airlines from Canadian residents.

function of the Canadian carriers' share of the market and of the distribution of the traffic between Canadian and foreign residents. In general, because the majority of traffic is Canadian in origin, the balance of the airfare account is not in Canada's favour. In certain cases, this imbalance is exacerbated by demographic factors. The largest deficits in this account are probably evident in the Canada-U.S. and Canada-Italy markets.

The prospects with respect to the effects of foreign airline activities in Canada are mixed. Firstly, greater access for foreign airlines to Western Canada is quite probable over the next decade, reflecting the faster growth in these markets over those from Eastern Canada. As such, Canadian carriers can expect lower returns from Western Canada as former monopoly markets will have to be shared (implying a greater proportion of higher cost, multiple-stop services). However, new improved services to the United States, the Far East, and possibly the Middle East and South America, are feasible over the next decade. The impact of these new services on volume and value would depend on the detailed routes and rights that will be exchanged in bilateral air agreements and the method of implementation of these new routes by Canadian and foreign carriers. Presumably, the impact on the balance of the airfare account will, in general, be in Canada's favour as the many passengers presently carried via indirect foreign carrier routes will be increasingly carried on Canadian carrier direct services.

III (a) Canadian Legislation, Regulations and Policies

There are two main statutes through which the federal government exercises constitutional jurisdiction over aeronautics, assigned to it by the British North America Act, as interpreted by the courts: the National Transportation Act (NTA) and the Aeronautics Act. The NTA established the Canadian Transportation Commission (CTC) as an independent regulatory body. The Aeronautics Act, in Part I, makes the Minister of Transportation responsible for carrying out, inter alia, the duty to secure Canada's rights in international air traffic. Part II of the statute gives the CTC extensive powers with respect to the economic regulation of commercial civil aviation, enabling it to control the right to provide commercial air services and generally to regulate airline traffics, routes, terms and conditions of service, as well as airline mergers and acquisitions.

In exercising the licensing powers of the CTC, the Air Transport Committee is required to satisfy itself that the proposed service "is and will be required by the present and future public convenience and necessity". In respect of scheduled international air services, the Committee would regard the formal conclusion of a bilateral agreement between Canada and the country concerned as evidence that the proposed services have satisfied the requirement in question, and issue a license to the foreign carrier designated by its government through diplomatic channels, provided that the carrier has obtained a valid operating certificate from the Department of Transport.

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Except for the constraints of certain international agreements or understandings, the CTC has been free to regulate international non-scheduled or charter air transport services, in accordance with its own interpretation of "public convenience and necessity" and subject to government policy tempered by an assessment of what other countries might reasonably be expected to accept.

Canadian policies reflect the government's goal of developing air transport services as an economic and social tool as well as a commercial activity. In the international field, government policies reflect also elements of Canada's strategy in terms of what Canadian authorities perceive to be the air policy goals and tactical objectives of other countries.

In an earlier era, Canadian air policy appeared to have been based on the proposition that private industry should not be allowed to "restrict the Government's freedom of development (in air transport) within Canada and with other countries beyond". Competition between air services over the same route was not permitted, and Canadian international air policy had been one of controlled market development with other countries.

Post-war developments saw a lessening of the importance placed on air transport as an instrument of national policy, in favour of its commercialization, but without a diminution of the policy and

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regulatory roles of the Government. With the emergence of CP Air and Air Canada as Canada's two international carriers, the approach to airline regulation by federal authorities over time has been a blend of intervention and reliance on market forces.

Underlying this pragmatism and flexibility was a change in the Government's perception of international civil aviation, from an earlier belief in the merits of a uniform world air transport system to a recognition of the advantages of reasonable competition, coupled with the desire for economic viability and profitability of Canadian international airline services. Consistent with this approach has been the absence of any doctrinal constraints in dealing with such matters as inter-airline cooperation, discussion, capacity-sharing or the regulation of capacity and frequency through intercarrier agreement and government approval. There is, nonetheless, the abiding belief that some measure of Government intervention is necessary in respect of trade in scheduled and charter air transport services in order to ensure, for Canada and for Canadian airlines, a fair share of the traffic originating in or destined for Canada.

In the scheduled field, the Minister of Transport indicated in a 1965 policy statement that the "Government has undertaken to regard Air Canada and Canadian Pacific Airlines as its chosen instruments ..." and pursuant to the wishes of both carriers for a clear division of overseas markets "so that outside Canada, neither airline would serve

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any point served by the other," he defined the world areas to be allocated to each of the two carriers.

In 1973, the Government adopted a comprehensive set of policies governing international civil aviation with the broad objectives of providing efficient and convenient air services to meet the travelling and shipping needs of Canadians, of contributing to the economic and social well-being of Canada, and of ensuring Canadian airlines a favourable climate and reasonably balanced opportunities for developing viable air services. The 1973 policy statement also provided a revised division of world routes between Air Canada and CP Air.

One of the issues that emerged from the 1973 policy was the principle that the Canadian gateways offered to foreign countries would depend on an assessment as to which would best serve the Canadian travelling public, the value to Canada of the rights accorded in exchange for these facilities, and the best interests of Canada as a whole. This represented a departure from the longstanding Canadian position that Montreal alone would be designated as the gateway in eastern Canada, and Vancouver the gateway in western Canada.

Given that a number of transatlantic air carriers had already secured access to Toronto (BOAC, Alitalia and Lufthansa), the 1973 policy reflected the results of past negotiations and led to the entry into Toronto of additional European carriers: KLM (1974), Swissair

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(1975) and Air France (1976). Air France's entry corresponded with the government announcement of a moratorium on further foreign airline access owing to congestion at the Toronto International Airport and the uncertainty of additional facilities becoming available in the Toronto area. The first service by a major European carrier to western Canada began in April 1981, following re-negotiation of the Canada-United Kingdom Air Services Agreement, which opened the way for direct access by British Airways to Vancouver, Calgary and Edmonton. The right of access to western Canada has also been given to Lufthansa on the basis of a revised agreement concluded with the Federal Republic of Germany in January 1982.

It has been an unwritten Canadian policy (except in our agreements with the U.S., Mexico and the U.K.) to allow our own carriers to operate from any Canadian point to destinations abroad while limiting foreign carrier entry to specific points in Canada. Notwithstanding the division of world routes between Air Canada and CP Air, Canadian authorities have, where appropriate and possible, sought the privilege of naming more than one Canadian airline at bilateral negotiations, although we have never availed ourselves of the opportunities thus obtained. In the Canada-U.S. transborder market, where the points to be served on both sides are specified in the route schedule, so far only two routes have been accorded double airline designation, and Canada has not in any case named two carriers to serve the same route despite the freedom to do so.

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While bilateral agreements normally provide for reciprocal services by the airlines of both countries, recent Canadian practice has permitted single-track operation by the airline of the other party where the Canadian carrier involved is not prepared to begin service of its own. Thus, under our agreements with Morocco (1975), Poland (1976) and Finland (1977), Royal Air Maroc, LOT and Finnair alone operate services to Montreal, the latter two on the basis of a commercial arrangement with Air Canada. Sabena, CSA, Aeroflot, Iberia, El Al, and Cubana also operate single-track services to Canada as a result of Air Canada and CP Air suspending operations to Brussels, Prague, Moscow, Madrid, Tel Aviv and Havana. On the other hand, CP Air has over the years served Fiji, Hong Kong, Peru, Chile and, until recently, Argentina on a single-track basis. Our agreement with Haiti (1978) provides for Air Canada alone operating a scheduled service between the two countries for an agreed period. Air Canada also operates single track routes to Barbados, the Bahamas and Antigua.

Regarding frequency and capacity regulation, free commercial choice has generally been Canada's objective and has been applied in respect of our most important international markets, the U.S.A., the U.K., the F.R.G., Holland and others, as well as in several other major markets. In other situations, Canada has accepted capacity controls, such as mandatory intercarrier agreements, and has tolerated restrictive foreign regulatory practices in many markets. Canadian practice has been to adopt a flexible approach by adhering to the Bermuda capacity formula while accepting some form of capacity limitation or control where circumstances require.

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Capacity on international non-scheduled air transport services is generally free of control, or is regulated unilaterally (or bilaterally in the Canada-U.S. and Canada-Cuba agreements) in ways that provide varying degrees of protection for scheduled operations. As between Canadian and foreign charter carriers, the Canadian regulatory objective has been to maximize the share of the Canadian-originating charter traffic carried by Canadian airlines. There are at present few internationally agreed controls respecting market entry of non-scheduled services. Canadian regulations do not limit or control the points of origin or destination of charter flights. Foreign carriers are allowed free access to any point(s) for which there is sufficient demand.

The CTC maintains an "eligible list" of foreign carriers entitled to operate charters out of Canada. It has generally protected Canadian operators from foreign competition by:

- (1) requiring that Advance Booking Charters contracted for in Canada by foreign carriers be priced no lower than the lowest price available from a Canadian carrier for a comparable charter (the so-called "floor price");
- (2) limiting the charter capacity of foreign carriers to roughly the number of foreign-originating charter passengers each carrier has brought into Canada during the same period (the so-called "uplift ratio");

- (3) allowing only Canadian carriers and carriers of the destination country to operate Advance Booking and Inclusive Tour Charters; and,
- (4) giving Canadian carriers the primary right or opportunity to operate Entity and Common Purpose Pro Rata Group Charters in considering the applications for foreign carriers that do not have their home in the destination country.

b) The International Framework

In international air transport, each State has the right to impose, in addition to safety regulations, conditions of entry and other constraints regarding foreign air carrier access to its territory. Given this environment, trade in air transport services has been made possible principally through two forms of interaction between States, one multilateral and the other bilateral.

1) Multilateral

Since 1945, international air transportation has developed within the general framework established by the Convention on International Civil Aviation (open for signature on December 7, 1944, at the close of the Chicago Conference). The Convention recognizes that every State has complete and exclusive sovereignty over its airspace. It provides

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that scheduled international air service may be operated to and from a State only in accordance with the terms of a special permission granted by that State. For commercial charter flights, a State has the right to impose any regulations, conditions or limitations it may consider desirable. Thus, the legal or institutional climate for international air transport is such that each State may determine both the timing and the conditions of market entry by the airline(s) of any other State regarding the carriage of commercial air traffic between their territories, either directly or via a third State.

The Chicago Conference succeeded in setting up a comprehensive plan for the development of world-wide technical standards in air navigation and safety, but failed to adopt a common framework for the exchange of commercial rights in international air transport to facilitate the establishment of air services. It agreed to draw up a multilateral instrument known as the International Air Transport Agreement which provided a uniform basis for one State to grant to any other State party to it, the rights of entry and to make traffic stops in its territory. However, this Agreement has received little support.

Also drawn up at Chicago was an instrument of more limited scope. The International Air Services Transit Agreement provided the basis for a multilateral exchange of the rights to overfly and to make technical or non-traffic stops in each other's territory. This Agreement has been accepted by more than 90 ICAO member States.

ii) Bilateral

Having failed to achieve a multilateral solution to the exchange of commercial rights in international air transport, States have taken the bilateral course in securing airline access to foreign markets. Bilateral air agreements generally provide for the reciprocal granting of transit as well as commercial traffic rights and set out principles governing capacity to be offered, routes to be operated by the airlines of both parties, the management of regulatory review of rates to be charged by carriers and other requirements of a technical and administrative nature.

A key postwar bilateral settlement was the agreement negotiated between the United Kingdom and the United States at Bermuda in 1946. Under this agreement, the carriers of both parties are permitted to freely adjust the level of frequency and capacity of their services to traffic on demand on each route, subject to certain agreed guidelines and to ex post facto review. Bilateral agreements other than the Bermuda type generally provide for some form of control on capacity. These agreements either predetermine the capacity, i.e., frequency in relation to aircraft type, to be operated by the carriers of both parties, or stipulate that the capacity to be offered shall be agreed or discussed between the two sides before scheduled air services are introduced.

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In direct opposition to the concept of capacity controls is the market-oriented approach to capacity regulation adopted by the U.S. following its policy of deregulating the airline industry since about 1975. Coupled with the principle of free or multiple airline access to the market place, the so-called "free-determination" method of capacity regulation is to allow airline management independently to set its own capacity on any route in accordance with its assessment of market demand. In the past few years, the U.S. has achieved some measure of success in this approach with a number of its bilateral partners.

The bilateral approach is mainly applicable to trade in scheduled air transport services. Commercial non-scheduled or charter operations are to a large extent governed in practice by the rules of the country of origin of the traffic but these rules are often tempered by what other countries are prepared to accept.

c) Civil Aviation and the Application of MFN and National Treatment Principles

In the network of bilateral agreements which, along with the Chicago Convention and the work of ICAO, govern the international environment of air transport services, the granting of traffic rights can be differentiated from the application, to the airlines which exploit those rights, of national regulations and laws relating to taxation, employment, corporate operations and so on.

1) Traffic Rights

The exchange of traffic rights is entirely a function of bilateral exchange, with countries treating the airline or airlines of any given trading partner in a manner perceived to be commensurate with the way their own carrier (or carriers) is treated by that partner. The ideals of an "equitable exchange of economic benefits" and "fair and equal opportunity" are incorporated into the preambles of many agreements, and a notable imbalance in benefit (usually but not always measured primarily in airline revenues) is often cited as just cause for seeking the renegotiation of the basic terms of an agreement. In the exchange of traffic rights, certain conditions of geography, demography, basic economic wealth or airline industry structure can often mean that the direct exchange of third and fourth freedom traffic rights does not represent a reasonable balance of either opportunity or potential benefit, and which can be corrected by the addition of fifth freedom traffic rights, the right to designate more than one carrier on any given route, or other rights or advantages commonly sought by one country or another. Depending on the bilateral relationship, some countries have agreements with some of their partners that are little more than a restricted exchange of third and fourth freedom traffic rights, and agreements with others that are more open exchanges with each side enjoying extensive fifth freedom traffic rights. Whatever the exchange is, it is always limited to a specific bilateral relationship, and "most favoured nation" or "national treatment" provisions are not used in bilateral agreements to assure access to new

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routes or rights which might be enjoyed by third country airlines or by the airlines of the granting state.

ii) Operational Environment

On the other hand, incorporated into the fabric of international civil aviation, through the Chicago Convention, through many ICAO resolutions and recommended practices, and through the "technical" articles of bilateral agreements, is the principle that airlines engaged in operating the services permitted by bilateral accord should be treated no less favourably than either the airlines of the other partner (national treatment) or any other airline operating services to the country concerned (MFN treatment). The national treatment principle is generally applied explicitly to provisions affecting tax and duty exemption, as is the MFN principle, which is also applied to the rights to establish local offices with expatriate personnel, to remit revenues to the country of nationality, and to import technical and operational goods and material. Albeit not quite so widely, the MFN principle is also applied to the right to carry out in-house ground handling and servicing of aircraft and in fewer cases still to the right to contract with third country carriers for local handling and marketing operations.

111) Canadian Practices

Although the early bilateral air services agreements Canada entered into tended to be less comprehensive and explicit on the granting of reciprocal exemption for duties and taxation and of reciprocal treatment in operational matters than more modern agreements, Canadian policy has been to treat all foreign carriers equally, unless there is a specifically identified lack of reciprocity for a Canadian carrier in the other country concerned. Subject to reciprocal advantages being granted by an aviation partner, Canada has been permissive in allowing foreign carriers to establish local operations, to use expatriate managerial personnel, to be exempt from all national sales and excise taxes, customs, duties and other charges (neither foreign or Canadian carriers are exempt from provincial taxes, however), to conduct their own ground handling, servicing and marketing, and to remit freely operational revenues to corporate headquarters.

IV Impediments to Canadian Airline Operations Abroad

Although the following is undoubtedly not exhaustive, it does cover most of the kinds of impediments which are or have been faced by Canadian airlines in their operational environments abroad. It should be kept in mind that the right to operate international air services is a function of bilateral agreements, and the right to engage in domestic services has always been limited, except in the rarest of cases, to domestic carriers.

a) Rights of Establishment and Access to Markets

Once assured of the right to establish operations by a bilateral agreement, Canadian carriers have not faced impediments preventing the introduction of services, or for the most part, inhibiting the establishment of local offices.

Obtaining full and fair market access has proven difficult only in a few cases, where local practices have effectively precluded the Canadian carrier from selling its services to the entire local market (in the Soviet Union, for example, Soviet citizens were "encouraged" through exist visa controls, to fly with Aeroflot), to portions of that market (many countries insist that government personnel, for example, use their own national carriers), or where integrated national travel marketing systems have favoured national carriers. There have also been impediments to cargo market access by national regulations and practices effectively assuring that all cargo in whole or in part financed by the government is reserved for the national carrier.

On the whole, however, Canadian carriers have not been active in markets where this form of cargo reservation has been exercised, and have generally had little difficulty in gaining fair access to passenger markets.

b) Government Economic Policy and Regulation

Given the very large proportion of Canada's aviation partners which have government-owned national carriers, it is very difficult to assess equality of treatment in taxation matters or in access to equity financing and credit. However, given that in most theatres of air service operation there are collaborative rate-setting mechanisms in place (either through IATA or by the two carriers concerned), the market effect of these advantages has not been serious. While there are undoubtedly many international airlines which would have long since gone out of business without significant government support, the institutionalized control (through, in the Canadian example, the CTC's authority over tariffs) against non-compensatory rates has prevented severe market disruption to the disadvantage of our airlines.

With many of Canada's aviation partners, bilateral agreements on the avoidance of double taxation are in place, and with certain others, specific provisions in the bilateral air agreements similarly apply. With others, however, (notably some of the South American countries and Hong Kong) Canadian carriers are subject to double taxation on profits, and while efforts are being pursued to resolve these problems bilaterally, these efforts have produced little success.

One of the problems Canadian carriers have faced in a number of countries without freely convertible currencies is the inability to

remit at prevailing market rates, and at the time desired by the carrier, the revenues gained in the marketing of passenger and cargo services. In most cases, we have been able to rectify such problems through bilateral negotiations, and it should be noted that this has not arisen with any major aviation partner.

Given the extensive international cooperation and coordination on the establishment of technical standards and on operational practices that have marked the development of international civil aviation, there are very few technical and operational impediments affecting adversely the activities of foreign airlines in ICAO member states. While problems unquestionably arise from time to time, these are generally resolved through bilateral or coordinated international efforts.

c) Direct Government Intervention

Civil aviation is almost everywhere an economic sector particularly prone to direct government intervention. Not only are governments responsible for the management and safety of the airways and to provision of airport facilities, but air services are often considered to be a key element of economic development. In many countries, maintenance of a national carrier is a political priority that is virtually unrelated to the economic costs of doing so, and the advantages of government assumption of carrier debt, low cost credit or credit guarantees for equipment purchases and other vehicles of financial support are practically impossible to estimate.

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As part of the support given national carriers, many countries insist that foreign airlines use a national carrier for any ground handling, servicing or marketing that the foreign airlines are unwilling or unable to carry out themselves. Others insist that such services be provided by domestic corporations specifically established for such purposes, possibly as subsidiaries or affiliates of the national carrier. However, where this is a local policy, there is generally no discrimination among foreign carriers, and where there is, MFN treatment can usually be negotiated bilaterally.

There has been only one case where restrictions on the employment of expatriate staff have impeded the efficient operation of a local office in a foreign city by a Canadian carrier, and that particular situation was addressed by applying a similar restriction on the employment of staff from the country concerned by its carrier here in Canada. For the most part, Canadian carriers try, in any case, to limit to as few as possible the Canadians employed in their offices abroad, given the extremely high costs of maintaining expatriate staff in most parts of the world.

V. Suitability for Multilateral Negotiations

As was mentioned earlier, bilateral agreements are the most important mechanism regulating international air transport. Problems outlined to the Task Force by air carriers in the areas of ground

handling and taxation, for example, are of a minor nature and are usually resolved bilaterally or through coordinated international efforts. In this respect, there is little scope for multilateral negotiations.

However, if broader, horizontal, issues such as government procurement or subsidies do arise in multilateral negotiations, there might be matter for consideration in respect to air transport; but since in many countries, the possession of a national airline remains a matter of national policy and pride rather than a viable undertaking, the prospectives for success in liberalizing this sector may not be great.

MARITIME TRANSPORT

MARITIME

I History of Canadian Deep-Sea Shipping

Shipping has always played an important role in Canadian economic life. During the nineteenth century, Canada was active in both shipbuilding and ocean transport. The advent of steamships and the lack of a strong steel industry placed Canada's marine industry at a disadvantage, which was reflected in the reduction of the deep-sea fleet to a position of minor significance. During and immediately after the First World War, Canadian shipyards built a number of steel freighters, some of which the government decided to operate through a Crown Corporation, the Canadian Government Merchant Marine Limited. Canadian deep-sea shipping remained, however, largely an adjunct to British shipping enterprises. In 1936, after years of precarious financial existence brought about by declining post-war freight rates, the government owned company disposed of the last remnants of this fleet.

The Great Lakes fleet had thrived during the period between the wars and by 1939 this fleet numbered over 300 ships. This fleet had sustained the Canadian shipbuilding industry and contributed to the wartime merchant fleet that was later to develop. Many Great Lakes ships saw wartime service overseas.

A fleet of 11 ships belonging to another government owned company, Canadian National (West Indies) Steamship Company, together with 10 Imperial Oil tankers and a few Canadian Pacific liners, in effect constituted the Canadian deep-sea fleet on the eve of the Second World War. Canadian shipyards soon responded to wartime demands for both naval and merchant ships, however. In 1942, the Park Steamship Company was formed to administer merchant ships constructed for Canadian registry. By 1945, the Park fleet consisted of 176 vessels.

By 1948 the Canadian fleet comprised 215 dry-cargo vessels totalling two million deadweight tons (dwt). The post-war shortage of shipping services and high ocean freight rates allowed Canadian vessels to operate in the deep-sea trades despite the fact that Canadian flag operating costs were the second highest in the world. By the end of the decade, however, growing competition from foreign fleets a drop in world freight rates, labour problems and changing technology began to tell upon Canada's merchant marine.

The Canadian Maritime Commission, after a substantive review of the international shipping situation in 1948-49, concluded that:

"Having regard to cost of construction and operation and taking trade balances into consideration, it is inadvisable as well as uneconomic for Canada to consider the construction and operation of a Canadian flag ocean-going merchant marine of sufficient dimensions to accommodate all her export trade or any fixed percentage thereof".

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The Commission recommended that Canada maintain the shipping and shipbuilding industries as a nucleus capable of rapid expansion in an emergency. The government, however, conscious of the difficulties faced by the Park Steamship Co. decided to rely instead on market forces and approved a phased liquidation of its Park fleet. Owners were given seven years in which to use the proceeds of the sale of war built ships for the acquisition of new or reconditioned ships, preferably ones built in Canadian shipyards. Because owners were reluctant to build deep-sea tonnage, a large portion of the sale proceeds were ultimately diverted into lake and coastal shipping. This process was stimulated by the construction of the St. Lawrence Seaway which held great promise for Canadian operators.

As a result of these decisions, Canada today maintains an open-door policy with respect to international shipping. Ships from many nations carry Canadian imports and exports. Canada's shipping policy to date rests on the belief that in the long run a freely competitive shipping environment will prove more beneficial to her interests than measures to develop and/or subsidize a national deep-sea fleet. Such restrictions on foreign shipping as do exist in Canadian law, stem mainly from concerns about marine safety and pollution prevention. Canadian public expenditures on marine transportation have been directed toward the provision of the support facilities and service necessary to ensure safety of navigation and to facilitate cargo handling. Given that Canada's trade was being carried at reasonable rates, successive governments were not prepared to introduce measures that would make deep-sea shipping under Canadian registry competitive with that under foreign flags.

Canada's Great Lakes fleet, however, has benefited greatly from Government support over the past three decades, due largely to its importance to Western Canada's export grain trade. The presence of a laker fleet was also ensured by a low cost, Great Lakes-St. Lawrence water route capable of handling large lakercs as well as ocean going vessels, the provision of extensive terminal facilities and other related infrastructure. The government has also provided assistance to shipbuilding programs for lake vessels.

- Present Situation

It should be noted that, while Canada is not normally considered to have a merchant marine, in 1978 some 3.4 million deadweight tons (dwt) of Canadian-registered vessels operated in the domestic and transborder trades, mostly on the Great Lakes, and some 7.3 million dwt flying foreign flags can be identified as being Canadian-owned.

During 1978, the volume of cargo transported to and from Canadian ports in coastal, deep-sea and transborder movements amounted to 239 million metric tonnes and is accounted for as follows:

| <u>COASTAL</u> | <u>DEEP-SEA</u> | <u>TRANSBORDER</u> | <u>TOTAL</u> |
|----------------|-----------------|--------------------|--------------|
| 60.7 | 104.6 | 73.7 | 239.0 |
| 25.4% | 43.8% | 30.8% | 100% |

II Description of Canada's Maritime Trade

a) Coasting Trade

The coasting Trade is defined as including the carriage by water of goods and passengers from one port or place in Canada to another, whether directly or by way of a foreign port. Most of the coasting trade is carried in Canadian ships.

Domestic cargo movements have risen about 19% in the last decade to some 60.7 million metric tonnes in 1978. This increase was most evident on the St. Lawrence-Great Lakes system, but offset somewhat by declining activity on the Pacific Coast.

The following records the tonnage (60.7 million metric tonnes) of seven important commodities transported in coastwise trade.

| <u>GRAIN</u> | <u>FUEL OIL</u> | <u>IRON ORE</u> | <u>PULP- WOOD</u> | <u>COAL</u> | <u>GYPSUM</u> | <u>NEWS- PRINT</u> | <u>OTHERS</u> |
|--------------|---------------------|---------------------|-----------------------|-------------|---------------|------------------------|---------------|
| 12.7 | 10.7 | 8.6 | 1.8 | 1.4 | .7 | .5 | 24.3 |
| 20.9% | 17.6% | 14.2% | 3.0% | 2.3% | 1.2% | 0.8% | 40.0% |

Domestic traffic falls into three main categories: East Coast; St. Lawrence-Great Lakes and West Coast. Arctic and intercostal movements are included in the statistics only as totals.

| <u>EAST COAST</u> | <u>ST. LAWRENCE- GREAT LAKES</u> | <u>WEST COAST</u> | <u>TOTAL</u> |
|-----------------------|--------------------------------------|-----------------------|--------------|
| 12.0 | 32.3 | 16.4 | 60.7 |
| 19.8% | 53.2% | 27.0% | 100% |

1) East Coast

East Coast traffic consists mainly of fuel product Newfoundland shipments, local pulpwood movements, and general cargo to and along the Newfoundland-Labrador coasts. This traffic which amounted to 12.0 million metric tonnes in 1978 is carried in a variety of vessel types, ranging from small general cargo coasters, to tugs and barges, to specialized roll-on/roll-off vessels, and small to medium sized tankers. Many of these vessels are ice-reinforced for year-round navigation in the Gulf of St. Lawrence area.

ii) St. Lawrence-Great Lakes

The St. Lawrence-Great Lakes system is the most important coastal trade, accounting for some 32.3 million metric tonnes in 1978. Shipments consist mainly of grains from the Lakehead to St. Lawrence River ports; iron ore from the Lower St. Lawrence River ports to the Lakes; petroleum products from the refining centres on the Lakes and in Quebec to local destinations, and miscellaneous bulk shipments such as salt, limestone, sand and gravel.

The main vessel type for dry bulk cargoes is the specialized Great Lakes bulk carrier designed to maximize carrying capacity through the Seaway locks, but for structural reasons they are generally restricted to operations west of Anticosti Island. Petroleum products are mainly shipped in small coastal tankers, with the newer units ice-reinforced and capable of navigating outside the Great Lakes system during the winter months.

iii) West Coast

The tug and barge industry on the Canadian West Coast has been growing since World War II, helped by a surplus of military equipment which became available for commercial use and because sheltered waterways made this wide-scale use possible. Where it is technically feasible to operate tug and barge units, they generally have a competitive advantage over conventional ships; therefore, tugs and barges are carrying most of the traffic on the Canadian West Coast. In these areas, the carriers provide two kinds of service: regular services from Vancouver to a large number of small communities which have no other means of communications; and transport of natural resources from points of extraction to manufacturing centres. The main products carried are logs and pulpwood, sand and gravel, fuel oil, lumber and timber. However, the traffic has decreased sharply since 1966 because of changes in the handling and sorting of logs and pulpwood. In 1978, loadings were in the order of 16.4 million metric tonnes in coastal shipping. Although there is a very large number of tug and barge operators on the West Coast, a small number of companies dominate the industry, with many smaller companies having been amalgamated during the last ten years.

iv) Intercoastal Trade

This route is principally between the West Coast and the Atlantic Coast, and between the West Coast and Great Lakes/St. Lawrence area via the Panama Canal. However, it also includes the route from the West Coast to Portland, Maine, which was used in 1973-74 for the carriage of eastbound petroleum cargoes ultimately destined for Montreal via the Portland-Montreal pipeline. Most traffic on this route flows from west to east, and is mainly bulk cargo, the principal commodities being coal and petroleum and forest products.

During 1975-1978, the number of annual movements has varied from one to eleven, in tonnage terms from 26,300 to 338,380 metric tonnes. Intercoastal movements are not produced or identified as a separate statistic but they are included in the total for coastwise trade. From the total number of movements made - 31 - only two were made by Canadian vessels, one of which was a tug and barge movement, and 29 by foreign flag vessels. This indicates that in spite of the trade being reserved for British, Commonwealth and Canadian vessels, the provisions of the waiver system ensure that non-availability of these ships does not hinder trade along the route (for further information see section of the Canada Shipping Act, page 14).

v) New Coasting Trade Policy

For some years it has been the intention of the government to revise existing coasting trade law. As a result of extensive consultations with the provinces and the marine industry, new policy proposals are now under review to reserve all coasting trade and coastal marine activities taking place upon submerged Canada Lands (except fishing) to Canadian ships, with provision to use foreign ships when no suitable Canadian ships are available. Any ship not built in Canada will be subject to customs duty upon temporary or permanent importation.

b) Arctic Movements

Although marine activities in the Canadian Arctic are very diversified, total marine traffic is small compared to the volumes moved in the Great Lakes/St. Lawrence River area and along the Pacific Coast; in 1978, the total Arctic traffic amounted to about 1.2 million metric tonnes of which approximately 0.6 million metric tonnes was a coasting trade movement and approximately 0.6 million metric tonnes was a deep-sea movement.

The deep-sea movements consisted of grain traffic from Churchill and minerals from the Eastern Arctic. These movements are included in the statistical totals for deep-sea movements but they are not identified separately (see page 3). Coasting Trade movements consisted of Eastern Arctic community resupply, Mackenzie River system resupply and Western Arctic community resupply. Resupply operations are generally carried out in Canadian flag coastal vessels, and in the case of the Mackenzie and Western Hudson Bay, by Canadian flag tug and barge operators. The existing Coasting privileges are mainly responsible for this dominant position held by Canadian flag vessels. Grain from Churchill is moved for the most part in foreign flag vessels in common with similar operations in other Canadian ports. Mineral shipments from the Eastern Arctic to foreign destinations are made largely in foreign flag vessels, except for the use of the M.V. Arctic.

Federal government objectives for northern Canada seek to encourage its economic development, the maintenance of Canadian sovereignty and security in the North and the protection of the northern environment. The use of Canadian flag vessels is encouraged in the Arctic.

c) Transborder Shipping

Shipments between Canadian and U.S. ports totalled 73.7 million metric tonnes in 1978, some two-thirds (49.1 million metric tonnes) of which was carried in Canadian flag vessels. Iron ore, coal, wheat and petroleum products are the most significant commodities in transborder shipping.

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| EAST COAST (Including St. Lawrence) to US EAST COAST (Including Gulf Coast) | GREAT LAKES (Including St. Lawrence) to US GREAT LAKES | WEST COAST to US WEST COAST | WEST COAST to US EAST COAST (Including Gulf Coast) | TOTAL |
|---|--|--------------------------------------|---|--------------|
| 17.7 24.0% | 48.3 65.5% | 6.6 9.0% | 1.1 1.5% | 73.7 100% |

The Canadian flag is particularly dominant in the important Great Lakes/St. Lawrence River trade with U.S. Great Lakes ports, where Canadian vessels, mostly Great Lakes bulk carriers, handled some 84.3% of the 48.3 million metric tonnes moved in 1978. The shipment of iron ore to U.S. (as well as Canadian) Great Lakes ports has long served as a backhaul for grain movements from Thunder Bay to St. Lawrence River ports, and this, among other factors, has helped Canadian operators maintain an edge over their U.S. competitors. Because of the coasting opportunities enjoyed particularly by Canadian lake fleets, foreign, non-U.S. flag operations play a minimal but growing role in this segment of transborder trades.

For the trade between the St. Lawrence and Canadian East Coast ports and the U.S. East Coast and Gulf Coast ports, however, foreign flag fleets dominated, carrying some 91.8% of the 17.7 million metric tonnes shipped in 1978. U.S. flag vessels play a minimal role in this trade, which consists largely of minerals, petroleum products, and forest products.

Transborder traffic between B.C. Ports and Alaska and U.S. Pacific Coast ports has been increasing reaching some 6.6 million metric tonnes in 1978, mostly forest products. Canadian-flag vessels handle some 66% of this trade, which is attributable to the Canadian Coasting Trade Legislation. A modest volume of cargo (some 1.1 million metric tonnes in 1978) was also shipped from B.C. ports to U.S. Atlantic and Gulf areas, and this traffic is entirely carried by foreign, non-U.S. flag, deep-sea vessels.

d) Canadian Deep-Sea Trade

(in million metric tonnes and billion Canadian dollars)

| EXPORTS | IMPORTS | TOTAL |
|------------------------------|------------------------------|-----------------|
| 75.5 (72.2%) \$15.3 (52%) | 29.1 (27.8%) \$14.5 (48%) | 104.6 \$29.8 |
| LINER | NON-LINER | TOTAL |
| 14.9 (14%) \$20.0 (67%) | 89.7 (86%) 9.8 (33%) | 104.6 \$29.8 |

In 1978, Canadian deep-sea (non-U.S.) waterborne trade was estimated to be approximately \$29.8 billion, with exports being valued at \$15.3 billion and imports at \$14.5 billion. In tonnage terms, the total Canadian deep-sea trade for 1978 was 104.6 million metric tonnes of which exports accounted for 75.5 million metric tonnes and imports accounted for 29.1 million metric tonnes. This trade is split between liner and non liner traffic, with the liner traffic accounting for only 14.9 million metric tonnes while the non liner traffic accounted for 89.7 million metric tonnes or 86% of the total tonnage. In terms of value however liner traffic accounted for \$20 billions or 67% of the total traffic while non-liner traffic accounted for 33% or \$9.8 billion.

Four commodities (grain, iron ore, coal and forest products) accounted for 73.8% of the total commodity tonnage exported deep-sea in 1978. Container movements accounted for 4.7%. Four imports, petroleum, alumina and bauxite, fuel oil and sugar accounted for 74.2% of the total commodity tonnage imported deep-sea for 1978. Container movements accounted for 11.0%.

EXPORTS

| <u>GRAINS</u> | <u>IRON ORE</u> | <u>COAL</u> | <u>FOREST PROD.</u> | <u>CONT.</u> | <u>OTHERS</u> | <u>TOTAL</u> |
|---------------|-----------------|-------------|---------------------|--------------|---------------|--------------|
| 22.9 | 13.7 | 11.1 | 8.1 | 3.5 | 16.2 | 75.5 |
| 30.3% | 18.1% | 14.7% | 10.7% | 4.7% | 21.5% | 100% |

IMPORTS

| <u>PETROLEUM</u> | <u>ALUM. & BAUXITE</u> | <u>CONT.</u> | <u>FUEL OIL</u> | <u>SUGAR</u> | <u>OTHERS</u> | <u>TOTAL</u> |
|------------------|--------------------------------|--------------|-----------------|--------------|---------------|--------------|
| 15.8 | 3.5 | 3.2 | 1.5 | .8 | 4.3 | 29.1 |
| 54.3% | 12.0% | 11.0% | 5.2% | 2.7% | 14.8% | 100% |

Our main trading partners are Japan, the United Kingdom and other Western European countries.

1) Liner Trades

Liner trades are those commodities that are carried in vessels operating on fixed routes according to published schedules. Service is provided to the general public within the limits of his equipment and ports of call. Liner operators can be divided into conference and non-conference operators. A conference is an association of ocean carriers that has the purpose of regulating rates, charges and conditions for the transportation by those carriers of goods by water.

Since the late sixties, containerization of the Canadian liner trades with other developed countries has been growing very rapidly. The large investment needed to operate a container service has

encouraged the formation of consortia and made it more difficult for newcomers to enter the trade. It should be noted, however, that in Canada, CAST has penetrated the trade by using innovative shipping techniques and by combining containerization with dry bulk.

Even if most of the liner traffic with our developed trading partners is carried by conference lines, they have to compete with a certain number of well-established non-conference liner companies as well as with non-liner vessels, especially for certain commodities like asbestos and paper products. Another effect of containerization has been the concentration of liner traffic in a smaller number of ports. Halifax, Saint John, Montreal and Vancouver are the only ports which handle a significant volume of containerized traffic.

In the trades with developing countries, containerization is much less important, even though some development in this direction has taken place in recent years. While the trades with Europe and Japan are almost in balance, the liner traffic destined to less developed countries is usually of greater magnitude than traffic originating there. Some of these trades are also served only by conferences dominated by the national lines of our trading partners; this is the case in our trades with Argentina, Brazil and India.

Canadian liner trades are served mainly by European flags, especially from the United Kingdom, Norway, Japan and West Germany. Furthermore, European flag carriers are involved in our trades with Latin America, Australasia and Africa. Flags of other areas are doing much less cross-trading and operate mainly between Canada and their countries.

The flags of state trading countries do not carry a high proportion of the Canadian liner trade, their share being only around 10%. Flags of convenience are of less importance in the Canadian liner trades.

ii) Non Liner Trades

Non liner trades in this document refers essentially to those commodities that are carried in bulk such as grain, iron ore, and crude oil.

In 1978, around 89.7 million metric tonnes of Canadian deep-sea cargoes were carried by non-liner vessels. This accounted for only about one third of the dollar value of the Canadian deep-sea trade in terms of volume. This means that the bulk commodities we are importing are much more valuable than the ones that we are exporting. The main bulk commodities loaded in Canadian ports for deep-sea shipping are wheat, iron ore, coal and barley while imports are crude oil, petroleum products and alumina/bauxite. Of the imports 90% of our deep-sea bulk trade originates in developing countries: crude oil from the Middle East and Latin American countries and bauxite coming from Guyana, Brazil, Guinea, Surinam and U.S. Virgin Islands. On the other hand, 70% of our export deep-sea traffic is bound for developed countries, mainly Japan, the United Kingdom and the Netherlands; this trade is made up mainly of coal and iron ore and to a lesser extent, wheat.

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There is an export/import imbalance in the Canadian bulk trades, since Canadian dry bulk exports do not move to the major sources of crude oil imports. Use of combination carriers for crude oil imports and dry bulk exports involves complex routing and/or cross-trading, and is rarely achieved in practice.

Flag of convenience vessels carry half of the petroleum products imported into Canada but only around 20% of the dry bulk trade moved deep-sea to and from Canada. The balance is carried by European flags, with Japanese ships carrying most of the Canadian coal exported to Japan. Flags of state-trading countries and those of the lesser developed countries do not play an important role in the transportation of Canadian bulk traffic, the former carrying mainly Canadian grain to their own countries or to other state-trading countries.

Another group of products carried either by liner or non liner vessels are neo-bulk commodities*. While Canada's containerized cargo is concentrated on the East Coast, neo-bulk trade tends to be concentrated on the West Coast. The main Canadian neo-bulk exports consist of forest products, pig iron, asbestos and aluminum and neo-bulk imports consist almost entirely of finished steel products and automobiles. The main areas of origin and destination of Canadian neo-bulk trade are Western Europe and Japan.

Backhauls are difficult to secure in these trades due to incompatibilities in handling techniques for forest products and automobiles. Indeed, specialized "open-hatch" carriers dominate the forest products export trade, whereas specialized car carriers handle the automobile import trade.

In summary, the diverse nature of the Canadian bulk trades renders two-way hauls uncommon.

e) Passenger and Cruise Boat Industry in Canada

i) Domestic Passenger Volume

Both east and west coasts, as well as the lower St. Lawrence are served by extensive ferry operations. On the east coast, passenger volume on major routes amounted to over 2.8 million in 1978, an increase of 65% over 1970. On the lower St. Lawrence, passenger volume on government operated or assisted services exceeded 4.1 million

* Neo-bulk commodities are those which are usually packaged in some uniform manner and which tend to move in large parcel lots. For these commodities operators have found it convenient to utilize small to medium carriers with the vessels and/or handling gear tailored to commodity stowage requirements.

passengers in 1970, but declined to about 3.3 million by 1978. Major west coast ferry services recorded passenger volumes of over 6.1 million in 1970, increasing by 73% to 10.6 million in 1978. In addition to this traffic, a significant, though undetermined number of passengers are carried by local coastal services, as well as aboard ferries operated at numerous inland river and lake crossings throughout the country. Examples of relatively large inland ferry operations include the Toronto Island ferry service and the service to Manitoulin Island in Lake Huron.

Other important components of domestic passenger carriage are cruises and sightseeing excursions which have grown in popularity in recent years. A number of cruises are offered on the St. Lawrence, the Great Lakes and coastal waters which are generally a few days in duration. Most domestic cruises, however, especially those further inland, are exclusively sightseeing excursions lasting no more than a few hours. The total number of passenger fares for domestic traffic in 1975 was over 22 million, increasing by about 30% to 29 million in 1978.

11) International Passenger Volume

International ferry services carried almost 1.6 million passengers to and from Canada in 1978. In the Maritimes, services linking Nova Scotia with the State of Maine carried 243,319 passengers in that year. An additional east coast international services is provided between Newfoundland, and St. Pierre and Miquelon. While total traffic on this route is not known, at least 19,000 Canadian residents were carried in 1978. Further inland, a ferry service between Detroit, Michigan and Bob-Lo Island, Ontario carried 362,253 passengers in 1978, down from a high of 501,385 passengers in 1973. On the west coast, three ferry services linking British Columbia with the State of Washington carried 948,953 passengers in 1978, a 25% increase over 1970.

International cruises which embark passengers at Canadian ports, as well as those which originate in foreign ports but enter Canadian waters, are relatively small, though an increasingly important component of passenger traffic. In eastern Canada, most itineraries involved either the Caribbean or St. Pierre and Miquelon. The peak of cruise activity here occurred between 1970 and 1972 with about 20 sailings per season, the majority of which were made by Soviet vessels. Since that time, however, the Canadian east coast cruise trade has become more limited with the Soviets, at least temporarily, utilizing their vessels elsewhere. Available data indicates that, over the 1970-78 period, cruise traffic declined by over 57% to less than 5,800 passengers. In addition to cruises which originate in eastern Canada, there are also a small number sailing from the U.S. east coast which call at Canadian ports but do not embark passengers. No statistics are available concerning the number of passengers taking such cruises.

On the west coast, cruise traffic has experienced remarkable growth, increasing from about 40 sailings and over 26,000 passengers in 1970, to over 100 sailings and approximately 55,000 passengers in 1977 and 1978. The majority of these cruises involve Alaskan itineraries. It should be noted, however, that these figures include passengers embarking on cruises in California, which call at, but do not embark passengers, at Canadian ports of call.

In addition to ocean cruises, many cruises are operated on the Great Lakes and the upper St. Lawrence River. While the actual volume of such traffic is not known, available data suggests that in 1978, as many as 365,000 Canadian returned to Canada from short duration excursion cruises on the Great Lakes and the St. Lawrence. While this figure may not be representative of actual international cruises traffic in this region, it may perhaps be regarded as a minimum estimate of such traffic in Canadian waters because there are conceivably a significant number of non-Canadian residents taking such excursions, as well as passengers embarking on cruises in the U.S. which enter Canadian waters. With the inclusion of this inland component, international cruise traffic within Canadian waters in 1978 is estimated to have been in excess of 426,000 person-trips.

Between 1975-78, passenger volume increased by about 28% to over 31 million in 1978, with domestic traffic accounting for approximately 93.5% of this volume. Ferry services made up over three-quarters of the international component.

f) The Canadian Merchant Fleet

1) The Foreign Registered Fleet

In addition to the domestic fleet, while Canada has an insignificant Canadian-flag deep-sea capability, it does have a substantial fleet under foreign registry. In 1980, the identifiable deep-sea merchant fleet, which appeared to have substantial Canadian ownership, was estimated to be in the order of 118 ships totalling some 7.3 million dwt. These are comprised of:

| | <u>No. of Vessels</u> | <u>Carrying Capacity (000dwt)</u> |
|--|---------------------------|---|
| <u>Foreign Registered Canadian Fleet</u> | | |
| Cargo | 5 | 42.2 |
| Bulk | 56 | 2305.0 |
| Container | 4 | 55.0 |
| Roll-On/Roll-Off (RO/RO) | 2 | 23.0 |
| Ore/Bulk/Oil (OBO) | 13 | 1688.8 |
| Ore/Oil (OO) | 5 | 435.6 |
| Tanker | 33 | 2722.9 |
| Total | 118 | 7272.5 |

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ii) The Canadian Registered Fleet

At the end of 1980, the self-propelled ships of 1,000 gross tons and over on Canadian registry consisted of 261 vessels with a carrying capacity of 3.4 million deadweight (dwt) tons. The following table summarizes the composition and distribution of the Canadian registered fleet.

THE CANADIAN REGISTERED FLEET
(SELF-PROPELLED VESSELS OF 1,000 GROSS TONS AND OVER)
1980

| | <u>No. of Vessels</u> | <u>Carrying Capacity (000dwt)</u> | <u>Total No. of Vessels</u> | <u>Total Carrying Capacity (000dwt)</u> |
|--|---------------------------|---|-------------------------------------|---|
| <u>Canadian Registered Deep-sea Fleet</u> | | | | |
| Dry-bulk carrier | 1 | 28.7 | | |
| General cargo | 7 | 46.2 | | |
| Tankers | 2 | 76.5 | | |
| Ore/oil carriers | 2 | 63.5 | 12 | 214.9 |
| <u>Domestic Fleet</u> (usually engaged in the following areas) | | | | |
| <u>Atlantic Coast</u> | | | | |
| Tankers | 30 | 248.0 | | |
| General cargo | 14 | 58.7 | | |
| Dry-bulk carriers | 18 | 318.9 | | |
| Combined passenger/ general cargo | 6 | 7.3 | | |
| Ferries | 16 | 26.3 | 84 | 659.2 |
| <u>Pacific Coast(1)</u> | | | | |
| Ferries | 27 | 36.2 | | |
| Passenger | 1 | 1.1 | | |
| General cargo | 1 | 1.2 | | |
| Dry-bulk carrier | 2 | 22.8 | | |
| Tankers | 1 | 5.0 | 32 | 66.3 |
| <u>Inland Waters</u> | | | | |
| Dry-bulk carriers | 108 | 2418.3 | | |
| Tankers | 6 | 30.1 | | |
| General cargo | 6 | 44.8 | | |
| Ferries | 11 | 10.0 | | |
| Passenger | 2 | .8 | 133 | 2504.0 |
| TOTAL CANADIAN MERCHANT FLEET | | | 261 | 3444.4 |

(1) There are also 350 barges with a carrying capacity of about 3000 thousand dwt each.

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g) Ownership

Under the "Canada Shipping Act", a shipowner is defined as meaning:

- a) the actual owner in the case of an unregistered vessel and the registered owner in the case of a registered ship, and
- b) when used in relation to goods, every person who is, for the time being, entitled either as owner or agent for the owner to the possession of the goods, subject to any liens.

Owner also includes, for the purposes of legislation on pollution, the lessee or charterer of any vessel who is responsible for the navigation thereof and includes beneficial owner for purposes of liability. Under the Canada Shipping Act only a British subject within the meaning of the British Nationality Act 1948, as amended from time to time or a body corporate incorporated under the law of a Commonwealth country and having its principal place of business in that country is entitled to own a vessel registered in Canada. For the purposes of this paper a Canadian company refers to any company incorporated in Canada under federal legislation or under the legislation of one of the provinces.

In Canada, there are different types of shipping companies and, therefore, defining the concept of ownership is problematic. Canadian Westfal-Larsen, for example is a Canadian registered company, involved in deep-sea shipping and operates foreign registered vessels. Major decisions and principal control originate from a parent company in Norway.

There are also companies such as Federal Commerce and Navigation Co. Ltd., that are totally owned and managed by Canadians but their fleet consist of foreign flag vessels.

Papachristidis Maritime Inc. is a Canadian owned company but it is managed from London, England where the owner resides. His fleet is registered under flags of various countries, and chartered to a number of ship operators.

In yet another example, the majority of shares (61%) of the CAST group are held by a Canadian Citizen living in Switzerland. The remaining shares are held by two major partners (Helix Investments Ltd. and Canadian National). The fleet is jointly owned by two companies registered in Bermuda and Switzerland and operated by a marketing firm incorporated in Canada. The vessels are registered under various flags.

III Canadian Governments' Legislation, Regulations and Policies

a) Federal

Deep-sea shipping falls under federal jurisdiction in the "British North America Act" which specifically grants inter alia to the Federal Parliament responsibility for:

- The Regulation of Trade and Commerce
- Beacons, Buoys, Lighthouses, and Sable Island
- Navigation and Shipping
- Sea Coast and Inland Fisheries
- Ferries between a Province and any British or Foreign Country or between two provinces

In addition, Federal legislation exists governing the registry of vessels, shipping conferences and the coasting trade. Also, provisions in customs regulations provide special tariffs for goods imported from the United Kingdom under direct shipping provisions.

The most important statute governing shipping in Canada is the "Canada Shipping Act", which is primarily concerned with the construction, operation, registration and manning of ships. In effect, it regulates shipping from the point of view of operations and safety. Furthermore, under the Act, ships eligible for registration in Canada must be either Canadian built or, if foreign built, with permission from the Minister of Transport. The name and residence of persons as registered owners of shares in a ship are entered into the Register, as well as the name and address of persons to whom the management of a ship is entrusted.

Part XV of the Canada Shipping Act governs the coasting trade of Canada, reserving it for Canadian ships in the Great Lakes/St. Lawrence area, and for British (i.e., Commonwealth built and registered) ships in all other areas. More than 97% of coasting trade is carried in Canadian ships.

The legislation further reserves coasting trade within the area west of Anticosti Island to Canadian registered vessels. The Coasting Trade laws provide for a waiver system for both of the above-mentioned regimes permitting foreign flag vessels to be used when no suitable Canadian vessel is available.

The original provisions of the coasting trade legislation enabling commonwealth ships to engage in the coasting trade became law in 1934 and have as their basis the British Commonwealth Merchant Shipping Agreement entered into in 1931 which required that all signatories grant equal treatment to ships of Commonwealth countries. Since the original signing of the agreement there has been a significant change in the make up and membership of the Commonwealth and in the size, structure and operating circumstances of their merchant marines. As a result in 1977 it was agreed that signatories to the 1931 Commonwealth Shipping Agreement should severally withdraw their accession to that agreement.

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Revision to the coasting trade legislation is being considered to take these changes into account and to consider other marine activities, such as dredging, salvage, drilling, seismic surveying and cable laying.

The "Carriage of Goods by Water Act" in effect applies the Hague Shipping Rules to the transportation of goods between points in Canada, and between Canada and any foreign port. The general purport of these rules is to regulate the legal position vis-à-vis the ocean carrier and the shipper or consignee of the goods.

A limited degree of economic regulation of shipping is imposed by four other federal statutes, the "Inland Water Freight Rates Act", the "Pilotage Act", the "Transport Act" and the "Shipping Conferences Exemption Act 1979".

The "Inland Water Freight Rates Act" applies to the transportation of grain from Thunder Bay to any port in Canada or the United States and it empowers the Canadian Grain Commission, in certain circumstances, to fix maximum rates for the carriage of grain.

The "Pilotage Act" also influences shipping in Canada by creating Pilotage Authorities who, in turn, are responsible for the establishment of compulsory pilotage areas and for the regulation and administrative aspects of these areas as prescribed by the Act.

The "Transport Act" empowers the Canadian Transport Commission to regulate the entry of persons into the business of transporting goods or passengers by water from any one point to any other point in Canada. The Act applies in respect of an inland water or sea only when so proclaimed; the only areas in Canada to which Part II of the Act is applicable are the St. Lawrence west of Quebec City, the Great Lakes, and the MacKenzie River system in the Territories.

The "Shipping Conferences Exemption Act 1979" exempts certain shipping conferences practices from the provisions of the Combines Investigation Act in order to allow them to exist on a legal basis. The underlying intention is to ensure the provision of satisfactory shipping services to Canadians who are the direct or indirect users of ocean transport rather than to provide the conferences with certain legal privileges.

The Act allows conferences to operated freely in Canadian trades subject to certain requirements design to protect the public interest. Those requirements include the filing of contracts, agreements and tariffs with the Canadian Transport Commission, the provision of copies of the tariffs for inspection at its principal offices and at the agencies of the member lines, attending meetings with designated shippers' groups and the provision of information sufficient for the satisfactory conduct of the meeting. The first Act came into force on April 1, 1971 and was amended on March 1, 1979. An interdepartmental committee has been formed to assess the effectiveness of the Act and to report to Cabinet by August 1983.

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Under the Canadian Customs Tariff, the "British Preferential Tariff" (BPT) applies to goods shipped from most British Commonwealth countries, colonies, properties or territories under British trusteeship when conveyed without trans-shipment from a port of any British Commonwealth country to a port in Canada. A program exists to phase out the British Preferential Tariff by 1987.

The direct shipment requirement of goods originating from New Zealand and Australia, as well as for many commodities from Commonwealth least developed countries which are eligible, is no longer in force and will only be re-instated if it is shown that the national interest has been hurt by this action.

Because of decisions in the late 1940s and early 1950s to rely on the international shipping market for the supply of essential shipping services, Canada does not today possess extensive legislative or regulatory mechanisms capable of dealing with the kinds of policy issues now emerging.

In a 1974 report on shipping policy issues, Howard Darling noted that Canadian legislation relating to deep-sea shipping, for the most part, lacks any significant policy stipulations.* The "Carriage of Goods by Water Act", he noted, deals only with the commercial aspects of shipping by providing a framework for the settlement of disputes within Canadian law in accordance with international conventions. The "Shipping Conferences Exemption Act", while it prohibits certain cartel practices and imposes certain obligations on shipping conferences as to tariffs, procedures and the filing of conference agreements and tariffs for public inspection, it does not confer significant powers with reference to rates and services.

Darling expressed some concern that machinery for dealing with problems and trends in international shipping potentially harmful to Canada was in his view either non-existent, or so cumbersome as to be ineffective.

The "National Transportation Act" provides the CTC with powers to investigate, but its powers to issue directives with respect to marine matters are severely limited.

The Foreign Investment Review Act (FIRA), established in 1974, requires that reviewable foreign investment proposals be assessed by the Governor in Council by reference to criteria as set out in the Act. In relation to investment proposals in the shipping sector, FIRA has reviewed a number of cases but its decisions have not inhibited developments.

* "The Elements of an International Shipping Policy for Canada", Ottawa, 1974.

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b) Provincial

In November 1978, the Newfoundland and Labrador Provincial Government issued the "Newfoundland and Labrador Petroleum Regulations, 1977" (pursuant to section 9 of the "Petroleum and Natural Gas Act, 1970"). One of the most important goals of these regulations is to ensure that preference be given to local labour on foreign flag vessels engaged in offshore activities off the coast of Newfoundland.

In October 1979, Norway issued a formal complaint to the Federal Government which stated that the Newfoundland and Labrador crewing requirements were contrary to international practice within the shipping industry as well as Norwegian Law. At the time, a Norwegian shipping company had chartered two supply ships to Eastcan Exploration to be used off the coast of Newfoundland.

The case made by Norway was examined by the Constitutional Law Section of the Federal Department of Justice. It was concluded that the Newfoundland Regulations were legal within the context of Canadian law. It is also understood that the provinces of Nova Scotia and Prince Edward Island are developing similar legislation.

IV Impediments to Canadian Exports

a) Tax and Fiscal Incentives

The industry considers that the greatest impediments to the Canadian export of shipping services are the tax and fiscal advantages provided by other governments compared to the regime available to the shipping industry in Canada. Some of these differences were addressed by the UNCTAD InterGovernmental Preparatory Group on Ship Registry, convened in Geneva, April 13-30, 1982. This action will undoubtedly spark a similar discussion in the OECD Maritime Transport Committee or one of its subsidiary bodies. It should be noted however that an attempt was made to harmonize conditions of registry in 1957 without success.

Canada's tax system in contrast to most other countries does not recognize the international nature of the industry and does not afford special concessions to shipowners, in which shipowners' effective tax rate can normally be reduced to zero. Shipowners have argued that the Canadian Government should adopt a number of fiscal incentives to encourage the gradual development of a deep-sea fleet, in particular free depreciation as used in the UK, the establishment of tax free funds for vessel acquisition, freedom of recapture on vessel sales if funds are used for the acquisition of a new vessel within a set number of years; and EDC*-type financing for domestic shipowners. Canadian shippers, particularly the BC forest industry have opposed any incentives on the grounds that they will lead to further government support and eventually to cargo sharing in support of Canadian shipowners.

* Export Development Corporation.

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b) Transportation Fuel Compensation Recovery Charge (TFCRC)

Since the oil crisis of 1973 and the tremendous price increases for foreign oil, the Canadian government has established a lower price for oil products sold in Canada. This is made possible by our considerable amounts of domestic supplies which must be supplemented however by foreign oil imports. In order to maintain the same oil prices throughout the country, the government subsidizes the importers of foreign oil to compensate them for the difference between the international and domestic prices.

Whenever domestic marine fuel is supplied to foreign or Canadian vessels for use in international transportation, there is necessarily less domestic oil available to meet Canadian needs. As a result, oil import requirements rise and the federal government's import compensation expenditures increase correspondingly.

To prevent such outlays of government funds, a Transportation Fuel Compensation Recovery Charge (TFCRC) was introduced in the 1980 Budget and implemented by the National Energy Board on May 1, 1981. The TFCRC therefore ensures recovery of import compensation payments made by the government. This charge applies to all marine bunkers supplied in Canada for international maritime transport regardless of whether it is domestic or international in origin. The charge takes into account marine fuel prices within U.S. competitive areas and is not applicable to Canada - U.S. trips in ballast.

c) Effects of U.S. Legislation

i) Biaggi Bill (HR 3637)

In 1981, United States Representative M. Biaggi, (D-NY), Chairman of the House Merchant Marine Subcommittee, introduced Bill HR 3637, which provides for jurisdiction over common carriers by water engaged in foreign commerce to and from the United States utilizing ports in nations contiguous to the United States. Bill HR 3637 would redefine common carrier by water in the foreign commerce of the United States to include carriers engaged in the transportation of property originating in or destined to United States points by way of ports in nations contiguous to the United States. The U.S. Federal Maritime Commission (FMC) would then exercise its authority over common carriers so defined and would therefore be in a position to control freight rates and subsequent traffic flows through Canadian ports.

Canada has formally and informally expressed concern over the various U.S. efforts to have the Bill adopted, arguing that this would constitute an attempt to exercise extraterritorial jurisdiction which would be incompatible with established trading practices. We have also pointed out that on the West Coast a significant number of containers of Canadian origin and destination are carried through U.S. ports.

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In spite of strong opposition, Bill HR 3637 has passed the Committee stage and it is waiting for a calendar date to go before the House of Representatives. There is still however opposition to the Bill in the House and thus enactment is not probable.

ii) U.S. Coasting Trade Legislation (Jones Acts)

The U.S. Coasting Trade legislation governs the U.S. coastwise trade and has mandatory requirements that all U.S. cabotage has to be in "vessels built in and documented under the laws of the U.S. and owned by persons who are citizens of the U.S." It is also required that all officers of U.S. vessels engaged in coasting trade be in all cases American citizens.

d) Flag Discrimination Measures

The discriminatory trade practices of a number of countries, particularly developing countries are impediments to vessels operating to those ports. These practices are designed to give a form of preference to national flag lines. At the present time the most pressing problems are with the following countries:

Algeria

The Algerian government requires a 50% cargo clause in export contracts for both oil and LNG giving preference to Algerian flag vessels.

A law enacted in 1978, stated that no contract for goods and supplies of services can be concluded with foreign enterprises except by the state, local authorities or state organization. The Government seeks to have as much of its bulk cargo imports and exports carried by national flag ships as possible.

Algeria also has ten known bilateral shipping agreements which divide cargo on a 50-50 or a 40-40-20 basis.

Brazil

Brazil has several laws governing its waterborne imports and exports. For example a 1969 law secures 100% national flag carriage for government goods, covering imports and exports by Federal/State/Municipal/Public administration departments as well as public enterprises and mixed economy firms and for goods enjoying tariff concessions, national finance or international loans. A waiver of cargo preference is also provided under this law.

Among other discriminatory practices, we find that:

- 1) Brazil has advantageous rates of exchange for shipping costs on national lines;

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- 2) Foreign shipping companies cannot operate from Brazil unless they are a member of a conference of which a Brazilian company is a member also;
- 3) Brazil regulates conferences in which it participates to assure an increased carriage of cargo for its own flag;
- 4) In 1981 the Brazilian government owned and controlled 74% of its merchant marine (gross registered tons);
- 5) Lloyd Brasileiro is compensated by the government for residual operating losses in pioneering trade routes.

Brazil has also signed 15 known bilateral shipping agreements which divide cargo on a 50-50 basis or in pooling arrangements.

Chile

Chile has introduced tax provisions requiring non-Chilian flag vessels to pay a tax of 5% on marine freight. Exemption from this tax is granted on a reciprocal basis.

Ecuador

The 1981 Ecuadorian Resolution Number 2/81 calls for 100% of general import cargoes from Brazil and Argentina to be carried in vessels belonging to Ecuadorian shipping companies.

Under this Resolution, the Ecuadorian Merchant Marine Board is empowered to verify that the freight tariffs to be applied by the national companies are not higher than those applied by the shipping companies operating in the same traffic and with the same classification or than those presently in force in the international freight market.

France

It has been reported recently that the French government has decided to embark on a substantial programme of regulatory and financial measures designed to increase their national fleet's share of trade to 50% of cargoes moving to and from French ports.

Peru

Peru requires cargoes to be carried in their vessels or those of their trading partners.

South Korea

The Korean Shipping Promotion Law makes it mandatory for exporters and importers to use Korean flag ships exclusively for all shipments. A waiver is allowed only when there is no suitable Korean vessel

available. The Port of Portland, Oregon has received such a waiver for all carriers sailing to or from that port to participate in the carriage of Korean cargoes. The Port of Vancouver has asked that the Canadian Government obtain a waiver exempting Vancouver from the provision of Korean law.

Korea demands that all container cargo move in national flag vessels. Again a waiver may be granted to a foreign flag vessel, if no suitable Korean flag vessel is available to move cargo in three days.

The intention of the 1976 Transportation Ministry Decree is that imports of crude oil, iron ore, lumber, grain and fertilizer will be carried in national flag ships when available.

Korea encourages the use of national flag ships by awarding government procurement contracts on a FOB basis rather than on a CIF basis. Also, a preferential interest rate for importing raw material for export production is extended to cover freight costs when imports are carried on Korean flag vessels.

V Suitability for Intergovernmental Negotiations*

a) Cargo Sharing

On the multilateral side, cargo sharing, particularly in the bulk trades could be detrimental to the Canadian interest. Canada has had a long-standing policy of reliance on the principle of "free and fair competition" which, it has been argued, has maintained the costs of shipping services at a relatively low level. Since cargo sharing would reduce competition, it is important to assess the precise implications for Canadian trades and shipping.

While such actions could assist shipowners, this would only be true as long as shipping costs remained low enough to allow exporters to compete on world markets. It is generally accepted that without the freedom of securing backhaul and cross trade cargoes in all parts of the world, shipping costs will increase dramatically. However, specialized carriers, such as very large crude carriers (VLCC's,) operate well without this advantage.

The current oversupply of shipping services would make it difficult to enter the shipping market at the present time. Selective entry where Canadians have specific technical expertise, such as self-unloaders, of course would be possible. This situation is aggravated by the growth of eastern bloc fleets that do not compete on the same basis as the fleets of market economy countries.

*A list of relevant multilateral agreements to which Canada is a party is annexed to this paper.

b) Organization for Economic Co-operation and Development (OECD)

The OECD Maritime Transport Committee is discussing a shipping policy to be applied among OECD countries and a tentative agreement has been reached among most OECD countries for a shipping policy to be applied to OECD member countries' relationships with third countries.

Shipping policies within OECD countries are fairly liberal at the present time as most OECD countries apply in varying degrees the Code of Liberalization of Current Invisible Operations. The current efforts to further liberalize shipping under an intra-OECD Shipping Policy tends to benefit the major shipowning nations that are looking for additional employment for their vessels. The following issues are being discussed under this exercise:

- (a) Cabotage (may be deleted)
- (b) Possible liberalization of offshore supply
- (c) Subsidies and fiscal benefits
- (d) Exchange controls and other financial matters
- (e) State trading joint agencies and companies
- (f) Technical and customs restrictions
- (g) Conference trades and practices and competition policy
- (h) Cargo reservation
- (i) Right of establishment
- (j) Differential port dues, fees, etc.

c) United Nations Conference on Trade and Development (UNCTAD)

The objectives of UNCTAD's work on maritime transport are twofold: first to increase the efficiency of maritime transport in its function as the major carrier of international trade, including the trade of developing countries, and secondly to increase the participation of developing countries in the international shipping industry.

The UNCTAD Trade and Development Board has set up a Committee on Shipping, which has adopted a comprehensive work programme on shipping and ports, and which in turn established a Working Group on International Shipping Legislation to review economic and commercial aspects of international shipping legislation and practices, and identify areas where modifications may be required.

Harmonization of policies of Governments in the field of shipping, ports and multimodal transport is carried out in UNCTAD through the adoption of recommendations to the States Members of UNCTAD and the elaboration of rules and new international conventions. Among the latter should be mentioned the Convention on a Code of Conduct for Liner Conferences and the Convention on International Multimodal Transport of Goods.

The following issues are also currently being discussed at UNCTAD:

- (a) Open-registry fleets
- (b) Port problems
- (c) Protection of shipper interests
- (d) Technical assistance and training
- (e) Carriage of bulk cargoes

Due to the broad political and geographical differences between the Canadian federal and provincial governments, it has often been difficult to obtain a general consensus on various issues (mostly financial incentives for a deep-sea fleet) aimed at reaching a common Canadian policy on shipping. It therefore would be difficult for Canada to support the inclusion of shipping issues, which might have provincial implications, in the trade in services exercise.

It would be particularly difficult for Canada to agree to include matters, such as cabotage and offshore marine related activities, in this exercise as this policy has been under review since 1970 in Canada when the Darling report was published. While it appears that agreement on a new policy is within reach, the new policy will still include restrictions. Over the past two years, Canada has expressed a strong opposition to the consideration of cabotage and offshore marine related activities in the Phase IV policy discussions at the OECD Maritime Transport Committee. Canada feels that these matters are national issues and, therefore, should not be part of international consideration. Because numerous shipping related issues are already being discussed by international organizations, such as OECD, UNCTAD, IMO, UNCLOS, the usefulness of having another international Committee undertake work in this area is questioned.

The majority of Canada's deep-sea trade is with OECD countries, and without a significant deep-sea fleet Canada has more to lose than gain in these trades as Canada would lose some of its advantage in the important trade with the United States in the Great Lakes and St. Lawrence River.

Unlike other OECD countries, Canada does not provide a special fiscal regime for the Canadian shipping industry. Canadian shipowners have made the point that until this situation is rectified and they are allowed to compete on an equitable basis, the elimination of other discriminatory measures will have little effect on their ability to export a shipping service.

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There are a few Canadian shipowning/operating companies that do export a shipping service particularly to developing countries. While a potential exists for expanding shipping services to developing countries, many of these countries practice discriminatory measures that limit or prohibit Canadian or other foreign flag participation in the trade. These measures also restrict the freedom of choice available to Canadian shippers and lessens competition. The United Nations Code of Conduct for Liner Conferences with its cargo sharing provisions will come into force in 1983 and will have the effect of reducing competition. Discussion of these practices under the Trade-in-Services project would be advantageous to Canada if these practices could be reduced or eliminated. Other options available to Canada would be bilateral diplomatic negotiations leading to bilateral agreements or retaliatory actions. Work under the Trade in Services project that increases competition is beneficial from a Canadian shipper's point of view.

ANNEX

NAVIGATION

Multilateral Agreements to which Canada is a party

- 1965, April 9 Convention on Facilitation of International Maritime
London Traffic
In force for Canada: Sept 16, 1967
- 1967, May 3 Convention on the International Hydrographic
Monaco Organization
In force for Canada: Sept 22, 1970
- 1969, June 23 International Convention on Tonnage Measurement of
London Ships, 1969
Signed by Canada June 23, 1969
Not yet in force
- 1969, Dec. 15 Amendments to the Annex to the Convention on the
London Facilitation of International Maritime Traffic, 1965
In force for Canada: August 12, 1971
- 1973, Nov. 19 Amended Text of Article VII of the Convention on
London Facilitation of International Maritime Traffic, 1965
Acceptance by Canada: Dec. 19, 1974
Not yet in force

Pollution

- 1954, May 12 International Convention for the Prevention of
London Pollution of the Sea by Oil, 1954
In force for Canada July 26, 1958
- 1962, April 11 Amendments to the International Convention for the
London Prevention of Pollution of the Sea by Oil, 1954
In force for Canada June 28, 1967
- 1969, Oct. 21 Amendments to the International Convention for the
London Prevention of Pollution of the Sea by Oil Done at
London in 1954 and amended in 1962
In force for Canada January 20, 1978
- 1971, Oct. 12 Amendments to the International Convention for the
London Pollution of the Sea by Oil, 1954, as amended,
concerning the Protection of the Great Barrier Reef
Acceptance by Canada: August 14, 1974
Not yet in force

ANNEX

1971, Oct. 15 Amendments to the International Convention for the
London Prevention of Pollution of the Sea by Oil, 1954, as
 amended, concerning Tank arrangements and Limitation of
 Tank Size
 Acceptance by Canada: August 14, 1974
 Not yet in force

1972, Dec. 29 Convention on the Prevention of Marine Pollution by
 Dumping of Wastes and Other Matter at Sea
 In force for Canada December 13, 1975

1978, Oct. 12 Amendments to Articles XI, XIV(4) and XV(1)(a) and
London addition of an Appendix to the Convention on the
 Prevention of Marine Pollution by Dumping of Wastes and
 Other Matters, 1972
 Acceptance by Canada: February 27, 1979
 Not yet in force

Luggage

1967, May 27 International Convention for the Unification of Certain
Brussels Rules relating to the Carriage of Passenger Luggage by
 Sea
 Signed by Canada: May 27, 1967
 Not yet in force

Liability

1957, Oct. 10 International Convention and Protocol relating to the
Brussels Limitation of the Liability of Owners of Sea-Going
 Ships
 Signed by Canada: Oct. 11, 1957
 In force May 31, 1968 - For Canada - not yet

Load Lines

1930, July 5 International Load Line Convention
London In force for Canada: Jan.1, 1933

1966, April 5 International Convention on Load Lines
London In force for Canada: April 14, 1970

1971, Oct. 12 Amendments to the International Convention on Load
London Lines, 1966
 Acceptance by Canada: Aug. 14, 1974
 Not yet in force

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1975, Nov. 12 Amendment to the International Convention on Load
London Lines, 1966
 Acceptance by Canada: October 14, 1976
 Not yet in force

Bills of Lading

1968, Feb. 23 Protocol to Amend the International Convention for the
Brussels Unification of Certain Rules of Law relating to Bills
 of Lading signed at Brussels on August 25, 1924
 Signed by Canada: February 23, 1968
 In force June 23, 1977 - For Canada - Not yet

Containers

1972, Dec. 2 International Convention for Safe Containers (CSC)
Geneva Signed by Canada: December 5, 1972
 In force Sept. 6, 1977 - For Canada - Not yet

Ice Patrol

1956, Jan. 4 Agreement regarding Financial Support of the North
Washington Atlantic Ice Patrol

 In force for Canada: July 5, 1956

Safety

1910, Sept. 23 Convention for the Unification of Certain Rules of Law
Belgium respecting Collisions between Vessels
 In force for Canada: October 28, 1914

1910, Sept. 23 Convention establishing Certain Uniform Rules with
Belgium respect to Assistance and Salvage at Sea
 In force for Canada: October 28, 1914

1960, June 17 International Convention for the Safety of Life At Sea,
London 1960
 In force for Canada: May 26, 1965

1966, Nov. 30 Amendments to Chapter II of the International
London Convention for the Safety of Life at Sea
 Acceptance by Canada: April 23, 1968
 Not yet in force

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ANNEX

| | |
|-------------------------|--|
| 1967, May 27 Belgium | Protocol to Amend the Convention for the Unification of Certain Rules of Law relating to Assistance and Salvage at Sea In force for Canada: August 15, 1977 |
| 1967, Oct. 25 IMCO | Amendments (1967) to the International Convention for the Safety of Life at Sea, 1960, Adopted at the Fifth Regular Assembly of IMCO Acceptance by Canada: June 2, 1969 Not yet in force |
| 1968, Nov. 26 London | Amendments to Chapter V of the International Convention for the Safety of Life at Sea, 1960 Acceptance by Canada: August 14, 1974 Not yet in force |
| 1969, Oct. 21 London | Amendments of the Regulations annexed to the International Convention for the Safety of Life at Sea 1960 (SOLAS) Acceptance in Canada: August 14, 1974 Not yet in force |
| 1971, Oct. 12 London | Amendment to International Convention for the Safety of Life at Sea (SOLAS) Acceptance by Canada: August 14, 1974 Not yet in force |
| 1972, Oct. 20 | Convention on the International Regulations for Preventing Collisions at sea, 1972 In force in Canada: July 15, 1977 |
| 1973, Nov. 20 London | Amendments to Chapters II, III, IV and V of the International Convention for the Safety of Life at Sea, 1960 Acceptance by Canada: Oct. 7, 1975 Not yet in force |
| 1974, Nov. 1 London | International Convention for the Safety of Life at Sea, 1974 In force May 25, 1980 |

ANNEX

LIST OF IMCO CONVENTIONS TO WHICH CANADA IS A PARTY

| <u>Agreement</u> | <u>Date</u> |
|--|---|
| Convention on the Intergovernmental Maritime Consultative Organization | 1948, March 6 In force Mar. 17, 1958 |
| Amendments to Articles 17 & 18 of the IMCO Convention, 1948 | 1964, Sept. 15 In force Oct. 6, 1967 |
| Amendments to Article 28 of the IMCO Convention, 1948 | 1965, Sept. 28 In force Nov. 3, 1968 |
| Amendments to Articles 10, 16, 17, 18, 20, 28, 31 & 32 of the IMCO Convention, 1948 | 1974, Oct. 17 In force April 1, 1978 |
| Amendments to the Convention on the Inter-Governmental Maritime Consultative Organization (Res. A. 400 X) | 1977, Nov. 17 Accepted by Canada Nov. 5, 1979 Not yet in force |
| Amendments Nos. 17, 18, 20 & 51 to the Convention on the Inter-Governmental Maritime Consultative Organization (Res. 450 XI) | 1979, Nov. 15 Accepted by Canada May 12, 1980 Not yet in force |
| Amendments to the title and substantive provisions of the IMCO Convention. Adopted by the Assembly of the IMCO by its resolutions A.358 (IX) of Nov. 15, 1975, and A.371 (X) of Nov. 9, 1977 (rectification of Res. A.358 (IX)). | 1977, Nov. 9 Accepted by Canada April 6, 1979 Not yet in force |

9. Cultural Services

INTRODUCTION

The Cultural sector covers a wide range of services, many of which are not considered as intangibles at all but rather as goods, depending on the circumstances. Films, video and sound recordings, newspapers, books and art are all goods in themselves, but the services involved in their creation, production, distribution, exhibition and consumption outweigh their tangible quality.

This paper considers only part of the spectrum, and examines four subsectors: broadcasting, film, sound recording and advertising, the latter included first because it has an obvious link with most other cultural media, second because it is also a factor that shapes the culture of a nation.

Canada is fortunate to have a cultural diversity but this diversity fragments the size of the market. In order to strengthen both Canadian national cultures against erosion, the Canadian government has, over the last twenty years, taken policy measures which may become the subject of multilateral negotiations.

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I DESCRIPTION OF THE CANADIAN CULTURAL SECTOR

The cultural industries examined by the Task Force represented revenues of about \$3 billion in 1980. Broadcasting alone accounted for \$1.7 billion (including CBC's budget) for the 674 originating broadcasting stations. The film industry had revenues of about \$760 million including \$386 million of box office receipts, \$248 million from distribution and \$124 million from private film and video production; the recording industry, with its 175 or so establishments, counted for about \$350 million while the approximately 300 advertising agencies posted revenues in the \$200 million range. In addition, gross advertising expenditures in Canada amounted to more than \$3.4 billion in 1979.

The industries examined above are, on the whole, Canadian owned and controlled (except in the film distribution sector and in sound recording) while in advertising, foreign controlled firms command a sizable proportion of billings. Broadcasting is Canadian-owned by virtue of an Order-in-Council limiting foreign ownership to 20%, but in the distribution sector of the film industry, Canadian-controlled firms, while accounting for 60% of the employment in 1978, earned only 1/3 of gross revenues and only 20% of profits earned in the sector. Foreign controlled firms account for 3/4 of all releases and earned 92% of sales revenues in the sound recording field in 1979.

Approximately 70,000 people work for these industries either on a regular or freelance, full or part-time basis. Broadcasting is relatively fairly distributed across the country, coinciding on the whole with the population distribution. However, since the largest production centers are located in Toronto and Montreal, most people involved in broadcast production are also located in these metropolitan areas. The film industry, as well as the sound recording and advertising agencies are also heavily concentrated in Toronto and Montreal.

Exports

In 1979, exports of Canadian broadcasting programming totalled \$8.1 million, mostly outside the U.S.; in addition, American advertisers purchase time on Canadian stations to the tune of a few million dollars.

The export market for Canadian theatrical films was small in the latest data (1979): only 16% of revenue was derived outside the Canadian market, while for television programs, 19% of revenues were earned outside the country; finally, non theatrical films earned 14% of their distribution revenues outside Canada, mostly in the United States. It is believed that export prospects of Canadian films will increase as more films are being produced specifically to suit the demand of American distributors, as was the case with a few of the

recent productions done under the auspices of the Canadian Film Development Corporation (CFDC), but this raises problems of real Canadian content and cultural identity.

Exports of sound recording have experienced tremendous increases between 1976 and 1980 (over 1,200% to \$25 million), half of the sales going to the EEC and 30% of the remainder to the U.S.; however this is more related to the devaluation of the Canadian dollar. It is believed to be made up mostly of American music reproduced in Canada for export. Nevertheless in 1979, there were \$2.3 million in royalties from the leasing of masters to foreign companies, and the use of recording studios in Canada by foreign artists was also a significant source of revenue.

As to the export of advertising services, the 1977 balance of payments showed exports of \$28 million and in the case of printed advertisement, virtually all exports in that year were directed to the U.S.; it can be presumed that this also applies to other segments of advertising.

Innovativeness

Innovation is not really an issue in most of the cultural industries; the market for development of new technology is quite small in Canada, Canadian controlled companies themselves are too small to

engage in research and development, while foreign controlled firms rely on their parent organizations for R&D, especially the sound recording industry. Innovations are, however, already having a tremendous effect on broadcasting, through the use of satellites and scrambling technology.

Profitability

Private broadcasting in Canada is fairly profitable, since net earnings in 1980 for radio and television were 11% and 18% of total revenue, respectively.

In the film industry, the private film and video producing sector in 1978 was not particularly profitable, averaging 7.5% of total revenue; the situation in 1981 is believed to have been worse. Sponsored and educational films (usually made for private industry and government departments) are quite profitable and represent an increasing share of Canadian producers' revenues, accounting for 40% of the \$20 million market in Canada.

The recording industry is a highly risky field since only one album out of 15 recovers its costs. In 1979, 22 of 41 companies in the industry ran deficits: 74% of small firms, 44% of medium-sized firms and 8% of the large firms were in deficit; however, the small firms are the biggest producers (proportionally) of Canadian content releases.

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The advertising agencies sector is seen as a profitable business, with profit ratios on gross billings of 1.5% and 1% for large and smaller firms respectively. Agencies reported net profits before taxes of \$14.4 million in 1977. It is believed that in the three years since then, the profit position of the industry has been good and that the largest 10 agencies have increased their gross billings to well over \$800 million in 1981.

II IMPORTS

Imports of broadcasting programs in 1979 totalled \$55.5 million, mostly from the U.S., which resulted in a trade deficit of \$47.4 million in this area. Furthermore, there have traditionally been deficits for Canada in the advertising broadcast trade, although it has been considerably reduced since modifications to the Income Tax Act in 1976.

The film distribution industry paid out \$117 million in 1978 to foreign producers for distribution of their production in Canada. In the Canadian sponsored and educational film market, 60% of the current estimated demand of \$20 million is imported from the U.S., the remaining \$8 million being supplied by Canadian producers.

Imports of sound recordings grew 84% between 1977 and 1980, to a level of \$29.4 million; the U.S. share of these imports has varied

between 68% and 82% during those years. In addition, the industry paid \$45 million in 1979 as royalty payments for the use of foreign master recordings and tapes, and the vast majority of this sum went to U.S. record companies.

In advertising, figures from the service account of the balance of payments show a deficit of \$61.4 million for Canada on imports of \$86.4 million in 1977. More recent figures are not available.

Statistics Canada's figures for printed advertisement showed an increase in imports of 24% over the period 1977-1980 to \$41 million, the U.S. share of which is 76.5%. Other statistics available are for filmed advertisement, and these showed imports of \$600,000 in 1980, virtually all from the United States. It is understood that the majority of this material was produced for MNE's for use in their domestic market and is exported to Canada by their subsidiaries.

Foreign-owned or controlled firms have a tendency to favour imported output. In film, for example, in 1980, it is believed that only 1% of the revenues of these firms are derived from the distribution of Canadian films, while Canadian controlled firms derive about 20% of their revenues from domestic production; this probably holds true for sound recordings; in addition, foreign subsidiaries generally leave the development of export markets for Canadian music to the parent organization.

III CANADIAN GOVERNMENTS' LEGISLATION, REGULATIONS AND POLICIES*

A. Federal

One of the basic pieces of legislation in the cultural sector is the Broadcasting Act (1968) which makes of Canadian broadcasting an instrument of national policy, and according to which policy the broadcasting system should strengthen the cultural, social, political and economic fabric of Canada. The Act empowers the Canadian Radio-television and Telecommunications Commission (CRTC) to issue regulations and affix particular conditions to licenses. The CRTC regulates broadcasting and imposes Canadian content regulations on television and radio, and also limits the amount of time devoted to advertising on these medias (12 minutes per hour of broadcasting). In addition, several classes of products are prohibited from advertisements. The CRTC may also order changes to advertising copy deemed "objectionable", and requires adherence to the CAB Code of Advertising to Children.

Other sources of authority in broadcasting include Cabinet directives, and powers of political and judicial review. The Governor-in-Council can, under the Act, issue directives to the CRTC regarding

* This section contains a non-exhaustive list of government undertakings in the cultural field.

the maximum number of channels, the frequencies for broadcast use, the reservation of channels or frequencies, the classes of applicants to whom broadcasting licences may not be issued, and programs of urgent importance to be broadcast to Canadians. The Governor-in-Council may also refer back to the CRTC for reconsideration or set aside, within certain time limits, a licensing decision of the Commission. If the CRTC confirms the decision, the Governor-in-Council may set it aside within 60 days of the confirmation. In the past, orders-in-council have been issued regarding foreign ownership, reservation of cable channels for education purposes, and educational broadcasting by provincially-owned institutions.

The CRTC's Cable Television Regulations (sec. 19) state that cable operators must substitute the Canadian signal on the cable channel of the American station whenever the two stations are broadcasting identical programs (if the Canadian station requests it). The result is that the advertising of the Canadian station is seen whether one tunes into either channel. Section 6 of the Regulations require that Canadian signals be accommodated on basic service before any foreign signals are authorized. This is seen as an impediment in the U.S. since Canadian viewers must purchase or rent a cable channel converter to view American signals. In addition, the CRTC doesn't permit the carriage of more than three commercial and one non-commercial foreign signal on any cable system, where distant reception of foreign signals is used (microwave, satellite, etc).

In addition to the Broadcasting Act and the CRTC Act (1975), the other basic legislation is the Radio Act which empowers the Department of Communications to regulate and control the technical aspects of the planning, construction and operation of broadcasting and takings.

The Combines Investigation Act has been strengthened and broadened since 1976 to deal with misleading advertising.

The Income Tax Act (sec. 19 (1)) is used to discourage Canadian advertisers from using foreign media, and the Foreign Investment Review Agency (FIRA) has disallowed two proposals involving the sound recording industry in the past; in addition, in 1918, it disallowed one proposal by a U.S. firm to acquire a Canadian advertising agency.

The Copyright Act protects a wide variety of works many of which are of a cultural nature, e.g. books, films and sound recordings. The Act grants national treatment to works created by nationals of our treaty partners. Virtually all industrialized countries belong to at least one of the Universal Copyright Convention or the Berne Convention.* Committees of those treaties meet on a regular basis and provide an appropriate forum for the discussion of multilateral copyright issues.

*A list of pertinent multilateral agreements is annexed to this paper.

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Some interests, both foreign and domestic, have complained because cable T.V. companies in Canada may simultaneously retransmit broadcasts without compensating the copyright owners. That may be done regardless of whether the broadcast originates in Canada or another country, e.g. a U.S. border station or satellite. That immunity from payment is the result of a 1954 court decision which has never been appealed. The U.S. courts gave a similar interpretation to the previous U.S. Copyright Act. The U.S. Act was amended, effective 1978, imposing copyright liability on cable companies for the first time. It applies to signals originating in the U.S., Canada or Mexico.

Recording companies in Canada may exercise a compulsory licence against music in recordings legitimately made in Canada or elsewhere. That enables them to produce their own recorded versions of the music on payment of a statutory royalty. Several other countries, such as the U.S. and the U.K., have similar compulsory licences though with a higher statutory royalty. Some copyright owners see the existence of the licence or the low level of the statutory royalty as being an unfair appropriation of their works and as creating unfair competition in international markets. It is likely that the Canadian rate will be increased in the revised Copyright Act.

The Copyright Act allows copyright owners to engage in market segregation by restricting the importation of copies of their works produced in foreign countries. This is a purely private right which is

exercised at the discretion of the individual copyright owner. The right exists in the copyright legislation of many other countries and a similar right is found in patent, trademark and design legislation in many countries. Recently, legitimately produced Canadian records were barred from entry into the U.K. by the owner of the copyright in the U.K. It would be in Canada's interests for other countries to eliminate this right of market segregation regardless of whether we do so ourselves. At the same time we could not reasonably argue for such a policy unless we changed our own Act.

Proposals for a comprehensive revision of our Copyright Act are being presented to Cabinet in July 1982 by the Department of Consumer and Corporate Affairs and the Department of Communications.

The Customs Tariffs Act places a duty equivalent to 1.3¢ per linear foot on film and 15% on the value of videotape for British and most favoured nations; however news footage enters free of all duties, as well as master recordings, tapes, and films to be dubbed or printed in Canada. This is considered as a loophole by the film industry, since many film goods enter Canada free of duty.

The National Film Board helps the development and production of films of social, cultural and technical value and the Canadian Broadcasting Corporation is the largest producer of film and video products in Canada.

The CFDC promotes the development of a feature film industry in Canada and administers the co-production treaties on behalf of the government. It loans funds for the development of projects or to provide interim financing ("bridge" financing).

The Department of Communications, in addition to regulating the technical aspects of broadcasting, administers the 100% Capital Cost Allowance and provides assistance for participation in film festivals, as well as financial aid for performing and visual arts, writing and publications etc.

The Department of Industry, Trade and Commerce provides export promotion and industry development services for the film and sound recording industries and assists the latter in trade fair participation.

The Canada Council provides financial assistance and special services to individuals and organizations in the arts (theatre, music, dance, visual arts - including film, video and photography - creative writing and publishing. Help to the film industry is budgeted at \$1.4 million for 1981/82.

The Department of External Affairs encourages and sponsors tours by Canadian artists, performers, writers and playwrights around the world.

The Department of Employment and Immigration monitors and controls the entry of foreign personnel (artists, technicians, directors) and the lack of enforcement in this area is seen as having a negative effect on the Canadian film industry.

B. PROVINCIAL

The Broadcasting sector is almost totally regulated by the federal government. However, the provinces do get involved in regulation of advertising broadcast, for example, the Quebec Consumer Protection Act forbids advertising directed to children under the age of 13.

The provincial governments are more involved in film and video production, having recognized the importance of media in social affairs. In addition, the provinces have the responsibility of licensing all theaters and drive-ins, and classify all motion pictures exhibited within their borders.

Ontario

The Ontario Educational Communications Authority, (the province's educational broadcasting agency), spent approximately \$10 million of its \$23 million budget in 1976/77 on programming Canadian content material. The Ministry of Culture and Recreation provides assistance to the film industry as well as to the operation and activities of the

Canadian Independent Record Product Association. The Ministry of Industry and Trade is establishing an office of film, video and software, and is now getting involved in support for the foreign distribution of Ontario-made films and television programs. The Ontario Film Council provides grants to filmmakers, script writers, and provides funds for various activities related to the development of original creative works.

Québec

Radio-Québec, the provincial educational broadcasting agency, spends about two thirds of its budget on programming. The Direction générale du cinéma et de l'audio-visuel coordinates the production of government sponsored film and audio-visual materials. The Cinémathèque nationale acquires and conserves copies of all works produced in the provinces. L'Institut québécois du cinéma (with a \$4 million budget in 1978) invests, loans and subsidizes the production, distribution and exhibition of Québec films and high quality foreign feature films. The Société de développement des industries de la culture et des communications (SODIC which will soon double its capital to \$20 million), is lending risk capital at low interest rates and underwrites projects of cultural expertise export, among other things.

Alberta

The Department of Business Development and Tourism provides assistance to filmmakers wishing to shoot films in Alberta, and also supplies small grants to film organisations; Alberta Culture also provides grants for script writing and training in film production. The provincial educational resources corporation, ACCESS is involved in the development, production, distribution and utilization of educational media resources in the province; 57% of its \$8.7 million budget in 1976/77 was allocated to programming.

British Columbia

The Department of Culture and Youth provides some opportunities for residents to participate in cultural activities; the province's Educational Communications Corporation is authorized to produce, acquire, sell, lease, distribute, exhibit or otherwise deal in programs and materials of an educational nature, and the Saskatchewan Development Corporation has invested as much as \$300,000 in a feature film in the past.

Other provinces are only beginning to be involved in film but they can be expected to increase their role in the future.

IV IMPEDIMENTS TO CANADIAN EXPORTS

Broadcasting content regulations exist in other English speaking nations, notably the United Kingdom (where 86% of all programming must be produced domestically or within the EEC) and in Australia, where there is a point system as well as quotas on specific categories of programming (e.g., children's programming). In non-English speaking countries, it seems that language is a sufficient barrier and there are few if any quotas. Many countries have measures destined to protect employment in broadcast-related industries, e.g., in France all dubbing to French must be done in the country.

Regulations regarding the nature and amount of advertising broadcasts are in effect in most countries, notably the U.K., Japan, Australia, Italy, Holland. In the United States the industry regulates itself through the code of the National Association of Broadcasters. Limits on advertising time range from 6 minutes per hour in the U.K. to 18 minutes in the U.S.

In cable television, the only English-speaking countries with significant links are the United States and Canada. In the United States, there are FCC priority carriage rules which guarantee local broadcasters carriage on U.S. Cable systems; however there are few other restrictions (for example, no equivalent simultaneous substitution regulations).

In the film sector, the main impediments in our most important

market, the U.S., relate to the vertical intergration of the market structure in that country; moreover, the transnational aspect of vertical integration by major American distributors has a significant influence in the marketing of Canadian film products in many other countries. No major obstacle to trade for Canadian production is reported in other countries, but it is likely that the same obstacles reported by American industry in OECD document TlR(82)1 will inhibit the export of Canadian films. Immigration policies are presently an obstacle to the movement of Canadian personnel in the United States, where regulations in this respect are more stringent than in Canada.

The United States does impose serious obstacles in the ownership of broadcasting undertakings: the Communications Act of 1934 prohibits issuance or renewal of licenses to corporations where more than 25% of the capital stock is controlled by foreign interests. In Australia, 85% of the capital must be owned by residents of the country while in many other countries, the broadcasting system is controlled 100% by the State.

In sound recording, the United States and France offer the greatest potential for Canadian content products (both English and French) yet many of the most important producers/distributors in Canada are foreign-controlled, and these firms usually leave the development of foreign markets to their parent organizations, who may not be interested or even aware of the potential. Consequently, under the present industry structure it may be difficult for Canadian music to break into those markets although the traditional barriers are low.

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In advertising, the world market is dominated by the United States (50% of world advertising expenses), and in Canada, American firms control a sizable portion of billings/revenues. Tariffs and non-tariff barriers are low or inexistant, and the U.S. market offers the greatest potential for Canadian firms. The performance of these firms will be determined by their competitiveness and resourcefulness.

V. SUITABILITY FOR INTERGOVERNMENTAL NEGOTIATIONS

It is understood that the United States will try to use the motion picture sector to link trade in services with the GATT. It has already published a substantial list of impediment to its worldwide exports of films (in OECD Doc. TIR(82)1); this includes import and screen-time quotas, subsidies, tie-in arrangements, dubbing taxes, local work requirements, monopoly controls discriminatory taxes, restrictions on remittances, piracy etc. The United States Trade Representative has also published, in an OECD Supplemental Report, a list of impediments by country which includes, in addition to the above, in the case of Canada, several other items in the field of advertising.

The following is a partial list of Canadian policy actions which can or could be identified as barriers by other countries in sectors covered by the Task Force:

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- CRTC Regulations on Canadian content, advertising and services offered by cable television companies;
- CRTC Regulations affecting the character and timing of advertising;
- Quebec's Consumer Protection Act forbidding advertising to children under the age of 13;
- Sections of the Income Tax Act discouraging the use of non-Canadian media for advertising;
- FIRA decisions and criteria;
- Cable T.V. immunity from copyright liability;
- The Canadian Film Development Corporation (CFDC);
- The Capital Cost Allowance for the Canadian film industry.
- Exceptions to the Customs Act which provide for the customs evaluation of audio tapes and discs used in radio broadcasting libraries at fair market value rather than tangible cost.

These may seem numerous, but against the background of Canada being historically an importer of culture, they are a "drop in the bucket", considering that only 28% of books sold in Canada in 1978 were written and/or published in Canada, that only 3% of films shown in the country are Canadian, and that over 80% of sound recordings sold in

Canada are of foreign origin. However, such measures will probably be fought.

It appears that there are more serious obstacles in Canada to trade in cultural services than there are abroad. This imbalance may be a natural reflection of Canada's position in relation to the dominant cultural position of the U.S.A., and to a lesser extent, Western Europe. In this sector, trade flows tend to be relatively skewed towards imports from the cultural metropolises, particularly the

United States, and in this context any relaxation of barriers would accentuate this anomaly. Since Canadian cultural material is heavy in "Canadian content", it may not be much in demand abroad and therefore has limited opportunities in other countries, unless, as mentioned earlier, production is specifically made to suit export markets. All these factors will make it difficult for Canada to negotiate without significantly reducing the measures which have been inscribed throughout government policies in the last twenty years.

Canadian restrictions, particularly on imports of advertisements are defensible, to a degree, on grounds of preserving the Canadian character of a major cultural factor, and ensuring that the limited potential sources of revenue for Canadian publications and media are not devoted to underwriting further foreign cultural penetration. It would not cause excessive difficulties for Canada if other countries were to adopt similar measures, as is demonstrated by the accommodating Canadian attitude to American mirror legislation on border broadcasting.

In conclusion, it seems that if Canadian measures were relaxed, the increase in imports, especially from the U.S., would greatly outweigh any projected benefits from increased exports of cultural services. In these circumstances, since the situation between Canada and the United States is different from that vis-à-vis other countries, the optimal posture might be to retain the status quo with the U.S. and work towards liberalising trade in cultural services with the rest of the world. This is probably not attainable, since it could be considered as discriminatory, but could be kept in mind, since it would be the course best suited to Canadian interests.

ANNEX

Multilateral Cultural Agreements

In force for Canada

Constitution of the United Nations Educational, Scientific and Cultural
Organization (UNESCO)

In force for Canada Nov 4, 1946

Agreement for Facilitating the International Circulation of Visual and
Auditory Materials of an Educational, Scientific and Cultural Character
with Protocol of Signature (Beirut Agreement)

In force for Canada Aug 12, 1954

Statutes of the International Centre for the Study of the Preservation
and Restoration of Cultural Property

In force for Canada: Nov. 7, 1978

Convention on the Means of Prohibiting and Preventing the Illicit
Import, Export and Transfer of Ownership of Cultural Property

In force for Canada: June 28, 1978

Convention concerning the Protection of the World Cultural and Natural
Heritage

In force for Canada: Oct. 23, 1976

Statutes of the International Centre for the Registration of Serial
Publications (Annex 1 to the Agreement between UNESCO and France on the
Establishment for the Registration of Serial Publications

In force for Canada: March 28, 1978

Copyright (Protection of Literary and Artistic Works and Cultural Property).

I. Principal Multilateral Agreements

Canada is a party to:

- (a) The Universal Copyright Convention done at Geneva on September 6, 1952. The reference in the Canadian Delegation's Final Report on the CSCE negotiations to "the Geneva Convention on authors' rights" must mean the Universal Copyright Convention.

Canada ratified the Universal Copyright Convention on May 10, 1962, and it entered into force for Canada on August 10, 1962.

The Universal Copyright Convention has three protocols, namely, "Protocol I Concerning the Application of the Convention to the Works of Stateless Persons and Refugees", "Protocol II Concerning the Application of the Convention to the Works of Certain International Organizations", and Protocol III Concerning the Effective Date of Instruments of Ratification or Acceptance or Accession of the Convention". Although Canada signed all three of these Protocols on September 6, 1952, it has ratified only Protocol III (in force for Canada since May 10, 1962), and therefore is not bound by Protocols I and II.

Canada is not a party to the revised Universal Copyright Convention, done at Paris on July 24, 1971.

- (b) The Berne Convention, as revised. In relation to the Berne Convention (Convention for the Creation of an International Union for the Protection of Literary and Artistic Works, done at Berne on September 9, 1886) the Canadian position is as follows. The Berne Convention has been revised at Paris (1896), Berlin (1908), Berne (1914), Rome (1928), Brussels (1948), Stockholm (1967) and Paris (1971). It has two main sets of provisions: substantive ones and administrative ones. States can be bound at one level for the substantive provisions and at another level for the administrative provisions. Canada is currently bound, as regards the substantive provisions of the Convention, at the Rome level (Revised Convention for the Creation of an International Union for the Protection of Literary and Artistic Works, done at Rome on June 2, 1928). The Rome Convention entered into force for Canada on August 1, 1931. As regards the administrative provisions of the Berne Convention, as revised, Canada is at present bound at the Stockholm level (International Convention further revising the Berne Convention for the Protection of Literary and Artistic Works, with Protocol regarding Developing Countries, done at Stockholm on July 14, 1967). Canada acceded to the Stockholm Act on March 26, 1970, and it entered into force for Canada on July 7, 1970.

Canada is not a party to the Brussels revision of 1948 or the Paris revision of 1971.

- (c) The Beirut Agreement (Agreement for Facilitating the International Circulation of Visual and Auditory Materials of an Educational, Scientific and Cultural Character, done at Lake Success on July 15, 1949).

Canada is not a party to the Florence Agreement (Agreement on the Importation of Educational, Scientific and Cultural Materials) done on November 12, 1950, approved by the UNESCO General Conference later held at Florence.

II. Related Multilateral Agreements

Canada is a party to:

- (a) The Customs Convention on the Temporary Importation of Scientific Equipment, done at Brussels on June 11, 1968.
- (b) The Convention respecting the Agency for Cultural and Technical Co-operation, done at Niamey on March 20, 1970. (Please note that although ratified by Canada this Convention is not yet in force).
- (c) The Convention concerning the Protection of the World Cultural and Natural Heritage, done at Paris on November 16, 1972.

Industrial Property (Protection of patents, industrial designs, trade marks, service marks, trade names, etc.)

Canada is a party to the Convention of the Union of Paris, as revised (Convention for the Creation of an International Union for the Protection of Industrial Property, done at Paris on March 20, 1883). The Paris Convention has been revised at Brussels (1900), Washington (1911), the Hague (1925), London (1934), Lisbon (1958) and Stockholm (1967).

As in the case of the Berne Convention, States can be bound at one level for the substantive provisions and at another level for the administrative provisions. Canada is currently bound, as regards the substantive provisions of the Paris Convention, at the London level (Revised Convention for the Creation of an International Union for the Protection of Industrial Property, done at London on June 2, 1934). The London Convention entered into force for Canada on July 30, 1951. As regards the administrative provisions of the Paris Convention, Canada is at present bound at the Stockholm level (International Convention further revising the Paris Convention for the Protection of Industrial Property, done at Stockholm on July 14, 1967). Canada acceded to the Stockholm Convention on March 26, 1970, and it entered into force for Canada on July 7, 1970.

Intellectual Property

The term "intellectual property" includes rights relating to:

- literary, artistic and scientific works,
- performances of performing artists, phonograms and broadcasts,
- inventions in all fields of human endeavour,
- scientific discoveries,
- industrial designs,
- trade marks, service marks and commercial names and designations,
- protection against unfair competition, and all other rights resulting from intellectual activity in the industrial, scientific, literary or artistic fields. It thus covers both the protection of industrial property and the protection of literary and artistic works.

There is one multilateral agreement, the Convention establishing the World Intellectual Property Organization (WIPO), done at Stockholm on July 14, 1967. Canada acceded to this Convention on March 26, 1970, and it entered into force for Canada on June 26, 1970. The objectives of WIPO are to promote the protection of intellectual property and to ensure administrative co-operation between the Berne and Paris Unions.

EDUCATIONAL SERVICES

INTRODUCTION

Preliminary figures showing educational service trade indicate that the provision of education is a major component of trade figures.* The nature of this service can be broken into several categories:

- i) public institution education in Canada, e.g. foreign students,
- ii) private education, again foreign students, and
- iii) educators or goods/services located abroad, which is inclusive of a wide range of factors.

One has to clearly distinguish the trade component of educational services from the aid component. This paper deals with commercial trade, although it is clearly recognized that, in terms of demand in developing countries, most of the demand, if met, will be through the aid channel.

The costs and benefits derived from such trade have not been well defined because costs are often subject to institution/provincial/

* This paper was written from material presented by the Department of External Affairs, Secretary of State, DRIE and educational organizations.

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federal conflicts of interest as to what real costs are. The same is true for benefits; while many contribute directly or indirectly to a positive trade balance, others are in dollar values. Therefore, the following presents the macro-dimensions of the international exchange but does not attempt to formulate cost/benefit ratios which would be of major importance when assessing trade policy development for trade in services. Components of this question are currently being addressed by the institutions themselves (e.g. the Commission on Foreign Student Policy established in 1981) or the Council of Ministers of Education. The latter organization, in conjunction with the federal government is currently grappling with an overall agreement which will establish a mechanism for state-to-state agreements in the educational field. This would be inclusive of foreign student education in Canada (where they go and under what conditions and costs) and educational expertise going abroad.

PUBLIC INSTITUTION EDUCATION

Education in Canada is primarily a provincial concern and all provincial governments have placed primary responsibility in the public institutional mode. It becomes a matter of governmental cost, with the majority of the "market" being outside of trade considerations. Given this however, foreign participation and transfer of benefit does occur and is both a balance of payments contributor and has aspects which strengthen trade links with our trading partners.

Preliminary enrollment data shows a renewed rapid growth pattern of students coming into Canada for educational purposes (Table I).* Figures for all levels of education show an increase of approximately 13,000 students 1980-81/1981-82 to a total of 66,399. Ontario receives just over half the students entering the country. While the number appears large, only 5% of Canadian university enrollment is foreign, with this fluctuating from between 1% and 10% by institution. This compares with Germany, for example, where 8% of the university body is foreign, with this figure being established by law as the maximum.

The source of funding is an important trade question, as a foreign student needs a considerable amount of money to live and pay educational costs. Prior to entry into Canada, Canadian regulations require that students must present proof that funding is available. Table II shows that the majority of students do come from high income countries (60%), with another 36% coming from middle income countries where it is a relatively safe bet that the students are from the upper levels of society. Only 3% are from the poorest countries of the world where there may be aid implications to the source of funding.

Table III uses 1976 data and it is estimated that the 1981- 1982 figures would be roughly double. Trends are the same however, 73.8% of total expenditures in Canada were from sources abroad and of the funding from within Canada, most was paid for value received. An

* Statistical information was supplied by the Bureau for International Education, based on Statistics Canada and CEIC data.

extrapolation for all student levels is very difficult, but each student would spend \$5-10,000. per year. This makes education one of the larger contributors to the trade in services balance of payments. Canadian students abroad is approximately half the number mentioned above and they have roughly the same level of expenditure. The surplus on BOP is thus substantial.

Students come to Canada for a variety of reasons. Canada has a very positive reputation abroad for both its cultural and education system in both languages. A basic premise is that there is relative ease of access to high quality education as the financial burden is not as high as in the U.S. or several of the European countries. The basic choice remains personal, influenced strongly by family and friends. To a large extent, the "marketing" of educational services is self-perpetuating.

The following observations can be made on the pro side of having foreign students educated in Canada. Many are altruistic and extremely difficult to measure in economic terms, but benefits thus derived do go far beyond the BOP argument stated above.

- 1) There is a long and continuing history of Canadian dependency on foreign country educational systems; Canada is now able to provide similar service to students of other countries who cannot obtain a suitable education at home.

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- 2) Global inequalities can be ameliorated and stimulation of economic development can be advanced through providing training and research experience.
- 3) The development of skills, transmissions of knowledge and advancement of research are international in scope where benefits are continuously being derived due to interchanges amongst the international intellectual community.
- 4) The education of foreign students is a means of fostering good relations in terms of contacts in a number of areas such as tourism, goods sales, and other service sales such as consulting.
- 5) Foreign students are a resource for the Canadian education system in that they interchange their experience with Canadian students, and, at the graduate level, provide skilled manpower and international connections to research projects.

This is not to say that problems do not exist as they do. The interaction at both a personal and cultural level between the foreign student and Canadians can be difficult. The cultural leavening which occurs is used as a major con argument by many Canadians who view the tax dollars spent on foreign education as a non-viable expenditure.

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Provincial interest in providing educational services to foreigners are varied. The declining numbers of students in Canada (although there are conflicting reports on this) is a direct cause of a surplus of teachers and equipment. By coming to Canada, foreign students can consequently help turn the investments already authorized to account and strengthen the present cycle. In some disciplines, however, competition for space between foreign students and Canadians is a problem. If, for example, the projections on shortages of engineers is right, then foreign students can be a source of needed manpower for Canadian firms.

The question of costs is a hotly debated item. Two major viewpoints hold sway, (i) cost per student is in direct proportion to overall costs per institution, and (ii) costs per foreign student are assessed as marginal costs because the facilities would need to be there in any case to serve the Canadian public. Because of this difference in accounting principles, no overall value of cost/benefit can be determined. All provinces except Newfoundland, Manitoba, Saskatchewan and British Columbia now require foreign students to pay a higher tuition fee than Canadians. Even so, tuition fees comprise only a certain percentage of total educational costs. It is generally conceded that higher fees have not significantly altered the flow of foreign students to Canada and are therefore not trade discretionary.

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Contractual Agreements

Universities and governments have identified, and are willing to commit resources to, the possibilities of selling educational services. Increasingly, there are agreements between the government, a government or non-government agency, or a firm from a foreign country on the one hand, and the federal government, a provincial government, a government or non-government agency, or an educational institution on the other, who are sending a group of students to Canada, or a group of educational exports abroad for education or training purposes. These agreements ensure that the cost incurred by such agreements are repaid in full or in part by the buyer of those services. It does not include the movement of students and teachers sponsored by CIDA or arising out of individual initiatives.

In the summer of 1978, a cost recovery technical aid program was established, one aspect of which was to offer places in Canadian colleges, technical institutions, and universities to interested foreign countries. In August 1978, an initial agreement was concluded with Nigeria. A request for provincial ministerial involvement was recognized as legitimate by the federal government in 1979. When consideration was given to concluding an agreement with China on the sale of educational services, the provinces through the Council of Ministers for Education were completely involved in the planning, negotiation and implementation stages of the agreement.

Since then, the growing interests shown by many countries in concluding this type of agreement with Canada has resulted in many federal/provincial meetings (at the ministerial level and at the level of government officials) between the provincial authorities responsible for education and their External Affairs department and Secretary of State counterparts. Purpose of those meetings was to agree on the possible instituting of a mechanism for federal/provincial cooperation which would enable Canada to act in its own interests when a foreign country reveals its intention in buying educational services from abroad. Considerable headway has now been made in negotiations in that connection, and the federal/provincial task force on international activities related to education agreed, on February 1, 1982, to create a sub-committee consisting of representatives from the Department of External Affairs and the Secretary of State and the provinces to re-examine those matters. A mechanism should be in place soon to enable Canada to sign state-to-state agreements with other countries.

Sales of educational services are, however, not always the outcome of concluding agreements between governments. Actually, such agreements have hitherto been the exception rather than the rule. The non-government sector (non-profit organizations) and even the private sector have been, and still are, active in this field. For example, the Association of Universities and Colleges in Canada entered into a contract with the Fundacion Gran Mariscal de Ayacucho of Venezuela which, as of the first year, brought about 500 Venezuelan university

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students to Canada. Recently, the Canadian Bureau for International Education signed a contract with a Libyan oil company to place 100 Libyan students in colleges in Canada. The total number of students now under contractual arrangement is expected to be 250. To a lesser extent, other organizations such as the Association of Community Colleges of Canada and the World University Mutual Aid are also active in the field. Many of the community colleges and universities have also had highly profitable specialized courses oriented towards a specific market. Laurentian University, for example, brings Japanese students over to teach them English, etc., during the summer; Concordia does much the same thing.

In the case of such arrangements, the buyer agrees to pay (1) tuition fees, those fees may constitute either the tuition fees applicable to foreign students in the host province or an amount decided upon by the host government representing the total cost of the services offered; (2) various allowances for each student's expenses (food, accommodation, insurance, etc.); and (3) the administrative costs of the organization which places the students and administers the contracts.

Public institutional training is not restricted to universities or colleges, which has been the thrust of the preceding discussion. Many provincial bodies orientated to technical skills development are also active, for example, the Northern and Southern Alberta Institutes of

Technology. Where there is a demand for specialized skills in either high technology areas such as data processing, or the more traditional skills such as electrical or welding, foreign governments are placing contracts with public institutions to train their citizens.

Governments become directly involved with training. The Ministries of Transport and Defense run cost recoverable training programs for foreign governments, as do such diverse agencies as the RCMP and the Coast Guard. While not large in number, they do make a valuable contribution to foreign exchange earnings and establish contacts for further training, goods and/or service sales and for the tourism potential.

The above avenues of exports, e.g. bringing students to Canada, in actuality fit into an institutional mode which is not designed to capture all the ancillary benefits to be derived. There is no strong link developed as a matter of policy between foreign students and people or institutions able to serve Canada's export interest. The goal is education in the discipline, not information transfer between, say an engineer and sources of Canadian suppliers in his area of speciality which would tend to capture goods exports. Nor is that student deliberately informed of Canadian engineering consulting

expertise which would be useful for service sales when the student returns to wherever and becomes a decision maker in his own country.

Various European countries do have deliberate policies in this regard. Germany, for example, restricts the disciplines a foreign student can get an entry visa for, a dominant one being engineering. During his education, the student is constantly exposed to German companies and German material, and becomes thoroughly familiar with the strengths of both. While not an impediment to trade, or something which can be negotiated, this linkage does significantly influence trade and the contacts established can become invaluable further down the road.

PRIVATE EDUCATION

The private education system is not faced with the arguments of what is cost and/or benefits as all costs are paid by the foreign student and profits are made to keep the school or training program operating. Figures on total market are included in total student figures given earlier, but it is estimated that approximately six thousand are placed in the private post-secondary educational industry. Each student brings an estimated \$10,000 per annum which he spends on tuition, room and board, clothing, etc., for a total balance of payments earning of \$60 million per annum.

The market potential to train accountants, secretaries, technicians of all types, business professionals, etc. is virtually unlimited. The potential is found particularly in developing countries amongst individuals who want a vocation or enhanced career or by governments who have identified a skill shortage which is impeding development.

The market currently is captured in a manner similar to other forms of private enterprise; by agents, publicity and advertising, by establishment and maintenance of professional standards which allows word-of-mouth business, etc. The private business college sector has a unique feature; a national external examination system which has operated across Canada since 1898. Another Canadian advantage is the ability to train in both French and English.

While the majority of the private education is Canadian owned, there is a growing foreign presence. Estimates are that within five years, up to 20% of the industry will be foreign controlled. For example, in the computer training field which had until recently required a large capital investment, the field is now dominated by such companies as Control Data, Bell and Howell, and Honeywell.

The other aspect of the market is to take Canadian education systems (people, systems, etc.) and establish them abroad. This ranges from establishment of specialized schools, which can start small and

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grow with the market, to the area of sophisticated educational packages depending on computer and video technology. This market, if properly sold, may prove to be the most lucrative in the future.

The private enterprise system is not as constrained in the institutional mode. The nature of the business means a closer link with supplies and/or business establishments. For example, an electronic technician, trained at Radio College in Canada, receives supply manuals and will often order from those on his return. Certified General Accountants would be familiar with textbooks, manuals, supplies obtained from C.G.A. headquarters in Toronto.

PERSONNEL/SERVICES LOCATED ABROAD

All educational institutions are orientated to the foreign environment to some degree. Given the primary purpose of enhancement and dissemination of knowledge, there is a constant desire to establish links with people of similar interests in other countries. This can be as little as exchange of knowledge through international journals, conferences, etc. The increasing amounts of research and development by governments and private enterprise has added to the burgeoning flow of international interchange. No values can be placed on monetary balances, but Canada as a country clearly benefits.

This interchange has often meant that Canadians visit and work abroad in an educational or expert capacity. There are many different mechanisms available for Canadians to work abroad. CIDA regularly has an educational component to aid projects, and the IDRC's main role is to stimulate and conduct research abroad. Professional groups such as medical educators have exchange programs.

Universities and colleges, to varying degrees, have a growing involvement in the export of their own academics for consulting and professional services. To a certain extent, this is reflective of the institutes' reputation by discipline, but tends to focus on those disciplines related to developmental problems of the third world. Universities and academics can market themselves directly or can go through such institutions as the Social Sciences and Humanities Research Council, the Canada Council, or the international aid agencies.

In 1981, the Ontario government set up the Ontario Educational Services Corporation. Corporation activities, however, different from non-government or private organization activities of the kind described earlier. Its aims are to facilitate the concluding of international contracts as, for example, contracts for building schools or colleges, by adding another element to contracts which take the form of a teacher training program, the preparation of teaching programs or the supplying of teaching and non-teaching professional personnel. Other provinces

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have already shown interest in this initiative and it is possible that this model may be copied by one or more of them soon. Alberta and Quebec, in particular, have already concluded agreements in the field of education with foreign trading or political partners.

In terms of hard contracts, Canada has probably identified the greatest opportunities for tradeable sales in the education field. Developing countries, especially the NIC's have created a demand for educational facilities and systems which cannot be met by internal resources. Therefore, schools have to be built, equipment and teaching supplies bought, educational systems devised and/or modified, etc. This area of activity has become big business, hotly contested by most of the OECD countries. The British have a large number of trade commissioners (estimated at 85) with primary responsibility to sell educational related goods and services. A major problem is the subsidization of educational services by governments to "get their foot in the door" in order to sell goods or to orientate future decision makers towards the subsidizing country. This particular problem is similar to the discussion of subsidization found in relation to consulting engineers.

No assessment can be made as to whether or not this academic cum consulting trade flow is positive in terms of trade balances. A great deal is funded by Canadian sources and is therefore neutral or negative; this is of course counterbalanced by earnings obtained under

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profitable contractual arrangements. It is a rapidly increasing mechanism of international co-operation however, and does enhance Canada's reputation as a source of knowledge, technology and expertise.

IMPEDIMENTS TO TRADE

This service sector has not been seen as an area where national governments have enacted policy specifically orientated to trade. Only in the last year or so has the sector been brought into trade discussions, and then only insofar as it facilitates goods and/or other service sales. There are, consequently, impediments in existence but not established specifically for this sector.

Developing countries have minimal impediments. Some countries have currency restrictions or exit requirements which would make it more difficult for their citizens to obtain an education abroad. These restrictions are firmly based in cultural or monetary policy and have not been seen as a trade item. There is a possibility of negotiation on these restrictions to the extent they can be related specifically to the sector and related to tourism which has the same problems.

Most of the impediments are found within Canadian policy or Canadian attitudes. Foreign student entry is hotly debated in terms of the costs incurred and the impact, potential or actual, they have on

community life. This issue is only beginning to be defined by provincial education ministers. At the federal level, incoming visas sometimes are a problem, but any rejections are firmly rooted in areas of health, financial ability, or risks of illegal immigration potential. Again, these are not particularly trade issues.

NEGOTIATING POSITION

Without doubt, there is increasing emphasis on education as an item for international interaction. Countries with well developed education systems, such as Canada, are becoming vigorous in their attempts to sell to those countries, such as Saudi Arabia, Mexico, Malaysia, which can pay a market value for educational services. Such sales not only help the balance of payments, but situates Canadian education as a sector which influences Canada's reputation as a trading partner. In intergovernmental relationships with most developing countries, there is a large aid component to the monetary flows from developed to developing countries. This has not been accounted for here.

Negotiations can establish some ground rules in this market. Unfair competitive practices wherein educational services are offered as a loss leader under a subsidized contract, for the sale of goods or to establish political influence, should always be treated as an untied aid situation rather than having trade implications. When a country can pay for educational services, pure market conditions should be negotiated, such negotiations directed at both developed and a group of recipient countries.

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Transfer of knowledge, either in Canada to foreign students or in the host country by providing training packages or people is as much judged on altruistic moral grounds as it is economic. Canada's current educational industry has the capacity and reputation to meet demand, but up to now, little specific policy direction has been given to the question of exporting educational services. Perhaps such policy development can go hand in hand with overall trade negotiations so a "beggar thy neighbour" environment can be kept out of trade in educational services.

The potential for benefit delivered by this sector lies partly exogenous to the sector itself. The potential is in contacts with future decision makers in all types and at all levels of a country's development and international interaction. This gets translated into goods sales from Canadian suppliers, consulting and other service contracts, and geopolitical influence. Negotiations could work towards a situation where such trade was "clean" and transparent. Developed countries in their exchange of students in effect already have this situation; it should be extended to developing countries as well.

Benefits are fundamentally derived from a free flow and interchange of knowledge. Because developed countries have a sound network of information and idea transfer and are willing to share this with developing countries, advances in humanities, sciences, medicine,

etc., are now being made throughout the world. At the same time, Canadian citizens have the opportunity to develop a world viewpoint by being in contact with, either in Canada or abroad, foreign students and educators.

Canada's negotiating position should be to keep trade in this area as open as possible and ensuring that no restrictions are put in place. In most cases, trade is between governments so this will remove trade impediments which might exist. For facility construction, problems identified for consulting engineers have been identified; both education and health would be excellent targets to immediately remove the problems of subsidy, goods and people transfer, etc., within the consulting engineering negotiations. Educators, students, and educational related material can easily be identified and could be negotiated as having free and easy transit across international boundaries.

The assumption is that the Canadian public institutions for the educational system will remain in place and will not be subject to the vicissitudes of private enterprise competition. For those components which are private enterprise, Canada can play the game of export support to the same degree as other OECD countries, or such support can be negotiated to a harmonized level. Given the humanitarian nature of the transfer of education, perhaps such harmonization should be at a relatively high level of export support and be clearly identified as an aid situation.

TABLE 1

Foreign Students by Intended Type of Education and by Region,
1980-81 and 1981-82

| REGION | PRIMARY & SECONDARY | | | POST-SECONDARY NON-UNIVERSITY | | | UNIVERSITY | | | TOTAL | | |
|-----------------------|---------------------|-------------------|----------------------|----------------------------------|------------------|----------------------|-------------------|-------------------|----------------------|-------------------|-------------------|----------------------|
| | 1980-81 | 1981-82 | Percentage Change | 1980-81 | 1981-82 | Percentage Change | 1980-81 | 1981-82 | Percentage Change | 1980-81 | 1981-82 | Percentage Change |
| Atlantic Provinces | 323 (2.2) | 417 (2.0) | 29.1 | 239 (3.5) | 262 (3.6) | 9.6 | 2,295 (8.0) | 2,682 (7.9) | 16.9 | 2,967 (5.5) | 3,475 (5.3) | 17.5 |
| Quebec | 908 (6.1) | 1,240 (5.9) | 36.6 (14.4) | 963 (16.4) | 1,195 | 24.1 (22.8) | 6,584 (22.3) | 7,574 | 15.0 (17.4) | 9,242 (16.7) | 11,066 | 19.2 |
| Ontario | 10,023 (67.2) | 15,095 (71.2) | 50.6 | 3,280 (49.8) | 3,709 (50.8) | 13.1 | 12,979 (45.0) | 16,166 (47.6) | 24.6 | 27,437 (51.6) | 36,575 (55.4) | 32.8 |
| Prairie Provinces | 1,716 (11.5) | 2,349 (11.1) | 36.9 | 1,422 (21.2) | 1,325 (18.2) | -6.8 | 4,335 (15.0) | 4,479 (13.2) | 3.3 | 7,765 (14.6) | 8,531 (12.9) | 9.0 |
| British Columbia | 1,948 (13.0) | 2,085 (9.8) | 7.0 | 806 (12.0) | 802 (11.0) | -0.5 | 2,657 (9.2) | 3,039 (9.0) | 14.4 | 5,794 (10.9) | 6,430 (9.7) | 10.8 |
| Total | 14,918 (100.0) | 21,186 (100.0) | 42.0 | 6,725 (100.0) | 7,309 (100.0) | 8.7 | 28,923 (100.0) | 33,995 (100.0) | 17.6 | 53,365 (100.0) | 66,399 (100.0) | 23.7 |

Percentage in brackets shows the distribution by region.

Source: Employment and Immigration, unpublished monthly data for January to September of each year (See Appendix B).

* This total includes also the "other" category involving 2,510 students in 1980-81 and 3,214 in 1981-82, mostly in hospitals, in religious institutions and language schools.

TABLE 2
Foreign Student Enrollment in Secondary and Post-Secondary Institutions by
Geographic Origin Classified by Levels of Income¹

| | Secondary | % of column total | Post- Secondary | % of column total | Sub-Group total | % of column total |
|--|-----------|-------------------------|--------------------|-------------------------|--------------------|-------------------------|
| High Income countries (50) ² (GNP per capita over US \$2,500) | | | | | | |
| Hong Kong | 4,100 | (38%) | 7,660 | (23%) | | |
| U.S.A. | 853 | (7.9%) | 4,168 | (12.5%) | | |
| OPEC [6] | - 36 | (3%) | 250 | (8%) | | |
| Others | 1,508 | (14%) | 5,940 | (17.9%) | | |
| | 6,497 | (60.2%) | 18,018 | (54.2%) | 24,515 | (55.7%) |
| Middle Income countries [84] (GNP per capita between US \$400 and \$2,500) | | | | | | |
| Malaysia | 2,451 | (22.7%) | 3,599 | (10.8%) | | |
| OPEC [6] | 411 | (3.8%) | 3,499 | (10.5%) | | |
| Others | 1,094 | (10.2%) | 4,690 | (14.1%) | | |
| | 3,955 | (36.7%) | 11,767 | (35.4%) | 15,723 | (35.7%) |
| Poorest countries [40] (GNP per capita below US \$400) | | | | | | |
| OPEC [1] | 60 | (6%) | 534 | (1.6%) | | |
| Others | 275 | (2.5%) | 2,920 | (8.8%) | | |
| | 335 | (3.1%) | 3,454 | (10.4%) | 3,789 | (8.6%) |
| GRAND TOTAL [174] | 10,788 | (100%) | 33,239 | (100%) | 44,027 | (100%) |

Source: Special tabulation, Employment and Immigration Canada, March 5, 1981 of Student Authorizations valid December 31, 1980.

Note 1: Classification of income levels derived from **In the Canadian Interest? Third World Development in the 1980's**. The North-South Institute. Ottawa: 1980.

Note 2: Numbers in brackets indicate the number of countries in each group.

TABLE 3
Estimated Total Contribution of 13 Sources of Support
for 23,450 Post-Secondary Foreign Students

| Source of Support | Total Support* | Percent of Grand Total |
|--|-------------------|---------------------------|
| OUTSIDE CANADA: | | |
| 1. Family or friend <u>at home</u> | \$ 43,193 | 50.9 |
| 2. Self (e.g. personal savings) | 8,941 | 10.5 |
| 3. Scholarships from abroad | 3,264 | 3.8 |
| 4. Home government agency | 2,461 | 2.9 |
| 5. Family or friend in another foreign country | 1,431 | 1.7 |
| 6. Employer in home country | 607 | .7 |
| 7. Other | 2,692 | 3.2 |
| INSIDE CANADA: | | |
| 1. Teaching or Research Assistantship | 6,847 | 8.1 |
| 2. Family or friend <u>in Canada</u> | 3,978 | 4.7 |
| 3. Canadian government agency | 3,819 | 4.5 |
| 4. Scholarships from Canadian Sources | 3,478 | 4.1 |
| 5. Loans | 1,216 | 1.4 |
| 6. Fellowships and bursaries | 1,811 | 2.1 |
| 7. Part-time work or employment | 1,044 | 1.2 |
| Total Support from sources abroad | 62,589 | 73.8 |
| Total Support from within Canada | 22,193 | 26.1 |
| Grand Total (23,450 students) | \$ 84,782 | |

* In thousands of dollars.

ENGINEERING/CONSTRUCTION AND RELATED CONSULTING SERVICES

This document provides an overview of the Canadian engineering/construction and related consulting services of Canada. It outlines some of the sector's strengths and weaknesses as a preliminary to a discussion of the trade performance and the problems associated with developing an adequate knowledge base.

The paper then reviews Canadian legislation as it relates to trade in the sector. A brief description of impediments to Canadian exports follows, not by country but rather by group or region being an overview of other governments' activities. More investigation would be necessary to identify impediments and their seriousness on a country - by - country basis; this would of course be necessary for actual negotiations.

(1) Structure and Trade Performance

The consulting engineering industry provides a wide range of services covering a wide spectrum of sectors (see Appendix #1 for sectors identified). It supplies services commonly associated with construction of capital projects for both public and private concerns. The range of services runs from pre-feasibility studies, planning and design development to detailed construction and project management. A growing involvement in turnkey operations is adding to the capabilities of some of the larger firms.

This document was written from material supplied from a number of sources - provincial governments, individual firms, the Peter Barnard Reports, Consulting Engineering Division of DRIE, and OECD documents.

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The industry had \$1.7 billion in fees for 1980 and employed approximately 42,000 people. Approximately 80% of employed are professional or have technical training. Division of fees shows a public/private ratio of 52/48%, with the public sector being split between municipal (27%), provincial (33%), federal (22%), and foreign public (18%). There are presently approximately 1,700 firms structured into four types: (i) large heavy engineering firms concentrated in Ontario, Quebec, British Columbia and Alberta, (ii) specialty firms located in large metropolitan centers, (iii) medium-sized municipal/transportation firms and, (iv) local engineering firms; the latter two being fairly ubiquitous in their regional dispersion.

About 98% of firms are Canadian owned with the remainder being mainly U.S. controlled. Twenty-five major firms account for about 60% of industry revenue and employment. There is increased formation of joint ventures, high activity in mergers and acquisitions and a constant expansion of firms establishing subsidiaries across the Canadian/U.S. border in both directions.

Architectural services tend to be distinct from consulting engineers for primarily historical reasons. Total fees were in the order of \$450 million in 1980 and employed 9,500 persons amongst some 1,500 firms. Firms thus tend to be small, are regionally oriented, and generally have not demonstrated a capacity to develop beyond regional markets.

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The value of construction activity is expected to reach nearly \$64 billion in 1982. There are approximately 100,000 firms employing some seven percent of the countries work force. Traditionally, however, they have operated only in the domestic market.

An important factor for trade is that Canadian firms in the consulting business do not have as a rule vertical ownership links with either construction or manufacturing companies. Contrary to European or Japanese firms where engineering expertise is part of a larger package which can include a financial component and goods sales, Canadian firms are independent. As prime contractors, Canadian firms can put forth the best combination of goods and services by being selective as to sourcing, whether Canadian or foreign. Their independence is often prized by international aid granting institutions and foreign governments. However, the lack of vertical integration does make the organization of a total package, e.g. a turn key project, more difficult (especially in the financing area) and time consuming than is the case for major European or Japanese competitors. U.S. firms are traditionally independent, but a number of large companies do have the vertical integration necessary to provide all components of a contract which requires a total package of financial and goods provision on a worldwide basis.

(a) Performance and Outlook

The consulting engineer industry makes substantial contributions to the overall economy in a number of areas. It provides a direct link to other industry sectors in that demand for material is specified by these firms. It often develops the leading edge for technology implementation, contributes to production rationalization and provides the infrastructures to meet any number of private or public objectives. The macroeconomic multiplier effect is very complex but ranges from 1:2 to 1:10 depending on funding, location, timing of following sales, etc.

By sector, municipal, building and power are responsible for over 40% of total industry output and demand for all three is steady. Petroleum and natural gas projects accounted for 9% of total output in 1980; industry spokesmen are not willing to project future prospects except to say that it would be highly erratic. The energy sector nevertheless remains important and, although not all projects may go forward, there still could be some shortages of skilled manpower resources available from within Canada, particularly in certain regions.

Building and municipal remain highly important in every region of the country. Forestry is strong in B.C., power in Quebec, and petroleum and natural gas in the West. Ontario has wide diversification and is important in almost all sectors. The industry

is confident that, in some sectors such as power or resource development, they have developed and control technologies and skills which are as advanced as any in the world. In other sectors, as in petroleum and natural gas development, companies are actively establishing joint venture operation with U.S. firms which have developed the advanced technologies. Firms innovate not only in technical areas but also in management practices and organizational matters. A few larger firms are now carrying out limited amounts of R & D for their own, as opposed to clients' accounts. However, constraints on technological development exist in the cyclical nature of demand and the resultant cash flow limitations. While very much people oriented, capitalisation is occurring through such techniques as computer-aided-design and automated drafting.

The industry overall is highly cyclical (see Appendix II for actual figures). The outlook for the industry is closely tied to the overall economic performance of the country. 1978 and 1979 saw annual growth rates of -6% and -7%; 1980 saw growth of + 13%. Profits are below acceptable levels for the industry. Given the current economic condition, it will take some time for firms to make the necessary adjustments to regain their former position. Dependent upon overall economic performance and the obvious connection between engineering demand and megaproject commencement, real domestic growth is estimated at 4% to 5% (or slightly lower than historic performance).

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(b) Trade Performance

1. Imports

Statistical information on the importation of consulting engineering services is very limited. A Statistics Canada survey (1977) indicated fees paid for imports of such services totalled \$130 million, of which \$105 million originated from the U.S. Estimates from the balance of payments account for 1980 place this at over \$170 million, with again over 80% from the U.S. Importation is for all practical purposes a U.S. related issue. The above dimension of imports are commercial arms length transactions which have traditionally been in the industrial sector and related primarily to oil and gas projects. This is closely related to the MNE question where U.S. companies tend to rely on U.S. firms with whom they do business in the States.

Outside of official figures is the large scale importation of value which is only sometimes accounted for elsewhere in BOP figures (either investment or miscellaneous income) i.e. work done abroad and then charged to branch plants in Canada. Inter-company utilization of consultants which is not contracted out to Canadian firms or branch plant employees located in Canada also reduce the size of the market available to independent Canadian firms. Total value of work imported by branch plant affiliates of MNE's is estimated at \$500 million, and industry spokesmen have identified this internal engineering by MNE's as a major growth area, if MNE's become willing to contract out more in Canada.

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Change is gradually taking place with U.S. owned subsidiaries increasing Canadian content on Canadian projects. Canadian owned consulting engineering firms are in turn acquiring access to technology by establishing joint venture companies with internationally based companies. The Task Force was told that, within the oil and gas megaprojects, Canadian companies could have the capacity to be the prime contractor within 2-3 years, with this signaling that the industry has matured in its capability. The Engineer/Procure/Construct (EPC) sector of the industry would then be highly competitive with similar firms from abroad.

2. Exports

Consulting work outside of Canada has become an increasingly important source of fees. The export component of the total market is estimated to be growing at 10-15% per year, or at least twice as fast as the domestic market. A significant factor in this growth has been the push factor of slow domestic market growth and the desire to compensate for the down side of cyclical growth.

Total export fees for 1980 reached approximately \$340 million or 20% of total billings. These figures need to be treated as "ball park" only as the statistical base for this sector is weak. Nor is there any idea at present as to how much of the fee actually comes back to Canada.

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The 20% figure for exports is assessed as a comfortable overall level of export by the Association of Consulting Engineers of Canada. A few firms have a much higher orientation to export. Most companies in the export market indicate a commitment to maintain an export presence even when domestic markets pick up. If so, the Task Force was told this could exacerbate manpower constraints within Canada during the mid-1980's. Canadian companies would like control over domestic projects, but many in fact need to import manpower on either a sub-contract or straight hiring basis. On the other hand, as indicated in the discussion on tax concerns, there is some evidence that non-Canadian personnel are increasingly being used in off-shore contracts.

There have been some shifts by type of activity. Power, always an important export market, has now become the leading export sector. Those sectors associated with early stages of economic development - forestry/agriculture, municipal and transportation - have diminished in relative importance. Many countries are now in a position to call upon local expertise, international competition is much more broadly located from Newly Industrialised Countries (NIC's) as well, and many regions have already obtained the needed services. Conversely in developing country (LDC's) markets educational services (schools, technical institutes) and health services (hospitals, clinics, municipal water supply and purification) are increasingly important. The sector associated with industrializing economies - plant processing - has taken on greater importance.

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Overall there is an ever expanding market, and even more important, that market is more evenly spread amongst world regions. The most recent period shows the U.S., Latin America, Middle East, Far East, and Africa have paid virtually equal receipts (20% each) for Canadian services. Eastern European countries have not been good markets except for a few specialised contracts. The U.S. has declined in relative terms as these other markets have grown. In part, this reduction in traded services is due to Canadian firms establishing American subsidiaries. While the work from Canadian subsidiaries perform removes such fees earned from the export statistics, it increases overall Canadian benefit in terms of dividend remittal and new market development. The establishment method of trading services is becoming increasingly important in all world regions, with Canadian firms establishing offices and/or negotiating joint venture partnerships in a variety of countries.

Canadian firms enjoy a world wide reputation in some areas - forestry, power, plant processes, port development and mining notably and have consistently maintained a significant proportion of their total billings from export. Generally, however, the export market is prone to a number of uncertainties which requires sound business judgement and a major export commitment and up-front effort to obtain a good balance between the domestic and export profit centres.

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One mechanism for capturing foreign contracts is to develop a turnkey capacity. This method of contract requires all facets of a project to be under one contract from start to finish and requires a financial and goods/construction commitment as well as a design function. Canadian firms are not as well structured to win this type of contract as are some European or Japanese firms because of the lack of vertical integration. They cannot put together a package of finance and material as quickly as some international competitors as they need to sub-contract out or establish partnerships with other companies. Consequently, the types of management skills necessary to handle some of the larger turnkey contracts are not as well developed as they should be. However, some firms are acquiring these skills and have established by good working relations with other Canadian companies who to contribute their financial or goods resources. Canadian firms have the choice and freedom to commit the best overall package even if some components of it are non-Canadian. The more sophisticated international customer acknowledges that this freedom of choice often provides the best long term project costs and efficiencies.

Another approach lies in the ability of firms to respond to the proliferation of specialty niches. With well-founded technology, specialty firms have found lucrative markets in all regions of the world and are able to obtain contracts even in European home markets. An overall international trend is to utilise consulting engineering firms to interchange technology on a project by project basis. The

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export market is a moving target, with old niches being filled by local expertise but new ones constantly opening due to technological changes and/or social and economic development.

The influence of aid is an important one for the Canadian consulting engineering community. Aid per se tends to be broken into many component parts where consulting studies are often discrete entities. Thus contracts flowing from CIDA or the international funding agencies are very much suited to the Canadian structure. Established exporting companies have a substantial proportion of their business in aid-related contracts; new companies to the export scene see this avenue as the main route to international experience.

(ii) Legislation, Policies and Regulations of Governments in Canada

There are a number of policies established in legislation which can affect the consulting engineering community in Canada. These are found in both federal and provincial levels of government, with the result that the Canadian market is balkanized to a certain extent. At the same time, the political, commercial, legal, and financial infrastructures of Canada are all well developed so that business operates in a well understood environment (not like some countries where ad hocery abounds).

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As in all countries, there are a number of non-legislated guidelines and practices which in effect can provide special treatment to domestic firms. These are not trade restrictions per se, but are attempts to obtain maximum regional benefits. Foreign firms established at regional levels tend not to be discriminated against.

At the federal level, FIRA requires the government to review new foreign investment to insure that establishment and takeover carries with them significant benefits to Canada. The presence of U.S. firms in Canada is felt however, with many American controlled firms well established in Canada and doing considerable amounts of business. The recently announced Federal Industrial and Regional Benefits Objectives and Guidelines relate specifically to the mega-projects and are intended to help Canadian industry supply goods and services on a competitive basis. This program is designed to ensure that Canadian firms are given every opportunity to bid on Canadian projects whenever they are competitive. Especially in the energy sector, recent government policies have as a main thrust the development of Canadian capabilities. The engineering community in Canada sees this as a major benefit in the short term. They feel that sufficient capability can be developed in the next few years which would make it more likely that Canadian firms would win in any competitive process even if the industrial benefits program were removed. In this respect, Canada is learning by example from many other OECD countries where domestic engineering firms have dominated their respective local markets. The

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current thrust of Canadian policy development provides Canadian firms with a level of support equitable to many developed countries. Some developed and developing countries have in fact set up public corporations which do engineering consulting work that private enterprise would normally do in Canada. Examples are government owned consulting engineering firms in Holland, Great Britain, Germany and Italy, and of course, the U.S. Army Corps of Engineers.

Entry of foreign personnel to Canada is regulated by the Immigration Act - 1976 and regulations thereunder. Practically all persons entering Canada to work on a temporary (non-immigrant) basis must have a work permit. Entry of executive and managerial personnel transferring to Canadian subsidiaries and affiliated companies may be allowed subject to immigration clearance only. Other professionals must also have Canada Manpower clearances to the effect that suitable equivalent personnel are not available from among Canadian permanent residents. In either case, work permits are generally issued for periods of up to one year and are subject to renewal. Canadian regulatory procedures are applied on a national i.e. not regional basis.

If manpower shortage projections are true for engineers over the coming years it would appear that these regulations will be a control factor but would not serve as trade impediments. A too rigorous application of the regulations could hurt Canadian companies as much as foreign companies insofar as all firms may be looking for foreign expertise, either on a straight hire or on a subcontract basis.

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Canadian Customs Regulations stipulate that engineering drawings are nominally dutiable on entry. Canadian Customs value building drawings related to heavy industry at 1% of the works, other building drawings are 3% of the works, various other drawings at cost of producing plans (including engineering materials, labour and drafting room overhead) plus an advance of 25%.

The tariff rate on these values are now (81) 15.7% and this will decline more or less uniformly to 10.2% in 1987 under the MTN agreements. Canada is committed to move to a wholly transaction price approach for valuation by January 1, 1985. Canadian Customs memorandum D4-1 now permits temporary duty remission for drawings for use in a) bidding in a foreign country b) producing goods for exports c) giving professional advice in respect to work in the foreign country. The process now requires evaluation and bonding at the time of entry against re-export or destruction under customs supervision within the prescribed time. The possibility of exempting drawings described in duty and tax is under review with a view to decisions later in 1982. Contractors' machinery and equipment are granted temporary entry duty free at the discretion of Canadian Customs authorities.

Customs and tariffs are particularly relevant to the Canada/U.S. situation. The amount of duty levied respectively by Canada and the U.S. appears to be similar despite differences of approach, and the philosophy appears to be similar in its application. Electronic

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transmittal complicates these arrangements by making tariff collection very difficult.

All engineering corporations carrying on a business in Canada are liable for federal and provincial tax on income in Canada, but there is an increasing network of tax agreements whereby double taxation can be avoided. A small business incentive exists with a low rate of federal corporate tax being only 25% on the first U.S. \$100,000 of business income for Canadian controlled private corporations. It is not available to public or foreign controlled corporations; they pay 46%. All provinces levy a tax on the incomes of individuals who reside in Canada, or who earn income there. Such persons are liable also for federal income tax if resident in Canada for 183 days or longer.

Engineers are required to be registered with the proper provincial or territorial association of professional engineers. Transfer of licenses between provinces is relatively simple, however some provinces have set out more stringent regulations for professional engineers practicing as consultants. Graduation from a school recognized by the Canadian Council of Professional Engineers makes a license easy to obtain. Licenses are regarded as necessary for all engineers to ensure safety and are not established as a trade barrier. In Quebec, a foreign consultant must collaborate with an engineer registered in Quebec in order to practice. Newfoundland and Alberta also have relatively strict establishment laws if one is to practice engineering in those provinces. Ontario has by statute given the Association of

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Professional Engineers of Ontario the power to attach a joint partnership qualification to the licensing of offshore engineers but so far they have not exercised the option. If they do, it is expected to be tied to requirements for technology transfer and the development of Canadian expertise in advanced fields. The Task Force heard from several respondents in the engineering community in Canada that Canadian regulations with regard to licensing of consultants are less strict than they are in the United States.

The provincial and municipal level of governments attempt to maximize local development. A range of policies and practices are implemented to varying degrees by provinces to favour local firms or encourage the development of local capabilities. These include, for instance, establishment requirements to be met in order to obtain project approval or financing where government procurement is involved. Standards are often local or provincial in nature. In some cases, provincial restrictions apply to professionals or firms from other provinces (and by extension to foreigners); to the point where Canadian firms often expressed frustration at not being able to expand in their own country.

(iii) Impediments to Canadian Exports

The working party of the Trade Committee of the OECD has taken the consulting engineering sector as a trial sector in which to investigate

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and define trade impediments for service industries. The investigation applies equally to trade impediments found outside the OECD member countries. Canadian companies have been asked for their input to this exercise and the problems identified at the OECD level have been verified and expanded further by consultations with the consulting engineering community of Canada.

There is clearly evident a difference of opinion as to the extent of transborder market potential within the developed world. According to some OECD countries, the OECD area generated relatively little trade as developed industry was well entrenched in each country at national and local levels and (apart from specialized work) there was no incentive to call on outside competition: this was described as a de facto situation. Certain other OECD countries consider that the "private preserve" which prevails in OECD countries is related to protectionist attitudes and the lack of substantial markets was an expression of trade barriers. The latter viewpoint of course would mean that the developed world as a whole was one with major problems which could eventually be a subject of negotiation.

The OECD survey did find that firms came up against trade obstacles in the LDC zone. These are countries with large prospective markets (insofar as local capacity is not well developed) and where competition was fierce. This fierce competition has led to the identification of numerous trade barriers. In many of the LDC areas,

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the question of bidding and obtaining markets is very closely tied to overall government procurement policy. In part, trade impediments are substantially reduced when the contract bidding goes through international financial agencies such as the World Bank. The consulting engineering sector in LDC's is composed mainly of government contracts where government procurement practices tend to reduce the market available to foreign firms.

Specific examples of protectionism were identified by the survey. The degree to which such measures may be found in any one country depends both on its economic and political philosophy. They are also a reflection of the state of development of the consulting engineering sector in that country; the situation ranges from open market conditions for "liberal" countries without expertise to highly protectionist countries where industry is developed and/or there is a tendency to government intervention.

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(a) Subsidization

Subsidization and related issues such as dumping is far more important than any other in causing distortions to trade. Some problems and situations are similar to those found in goods trade, others are specific to consulting engineers, and still others are exacerbated by the structural framework under which Canadian firms function i.e. lack of vertical intergration. To a certain extent, distortions are similar by - stage of development OECD, NIC's, LDC, and Eastern Block or are caused by third country competition for export contracts. Problems are generally described as related to:

1. state participation
2. domestic subsidies
3. export subsidies
4. discriminatory practices in granting of aid
5. competitive practices of firms, and
6. other distortions of a more general nature.

1. State participation is seen in some developed and many third world countries. There are firms with state capital or which are offshoots of nationalized goods producing industries. Some states in the third world place these services in a quasi-monopolistic enterprise and channel all contracts (government procurement at the very least) through these firms. The Eastern block, with rare exceptions tied to financial or technology tranfer, refuses to admit that consulting exists as a separate form of business.

It becomes a trade question if state agencies, in making work accessible to bidding, adopt certain protectionist, preferential or discriminatory attitudes. Principles of non-discrimination, policies based on commercial consideration and adequate opportunity to compete, limitation of obstacles and transparency could be brought to bear.

2. Domestic subsidies such as direct financial aid and tax incentives or the provision of goods or services by the State on favourable terms, are some of the forms taken by domestic subsidies. This is especially true where there is a strong goods/service link, as there is a multitude of programs designed to protect goods production by most governments. Of particular importance given the nature of consultancy as a major user and innovator of technology are the subsidies granted for research and development.

Domestic subsidies on services reduces the chances of non-subsidized foreign contractors breaking into a market. They also give the recipient firms a competitive advantage in foreign markets. They are even more effective if right of establishment is refused or if subsidization regulations exclude foreign controlled firms, i.e. if national treatment is not fully granted. Because some of this domestic subsidy may be put in place for economic and social reasons having nothing to do with trade, it would need to be determined on a case by case basis if there were a deliberate protectionist or discriminatory intention involved.

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3. Export subsidies, as with goods trade, take many forms.

Subsidies for exports of goods could have a very favourable impact vertically integrated firms, as they might assist such firms to provide their consultancy services at less than cost (which Canadian firms are unable to do). It has been found that firms in four or five developed countries and half a dozen developing countries pose this kind of problem in third country markets. In particular, the following forms of subsidization have been found.

- export credits for feasibility studies;
- government guarantees to cover the risk of unsuccessful tendering;
- export credits to finance operational costs of a specific foreign project;
- government guarantees for private bank loans to provide working capital for firms;
- tax subsidies - corporation tax exemptions on export sales; tax exemptions for exports of capital goods and building materials, tax exemptions for technical staff working abroad, etc., and
- government risk sharing

There is a strong linkage between firms hired to do feasibility studies and service/goods sales in cases where a vertically integrated company structure exists. The prime objective may not be the

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consulting contract but the subsequent sales. Some of the more sophisticated markets realize that firms without vertical links may be able to provide better service and better/cheaper goods as they can shop for the best combination of products. However, a disadvantage is the time required to do this. Moreover, direct government participation in negotiations to win contracts, which is felt to be a standard part of doing business by some other governments, will often win contracts in third country markets.

There is a more general set of policies in developed countries whereby consulting engineering firms can receive financial assistance for business prospection. Guarantees for firms establishing abroad, investing or acquiring abroad, credit insurance systems for contracts, etc., are all "normal" export packages which can be obtained by service firms. It was put to the Task Force that, to a large extent, difficulties Canadian firms encounter in this area are due to unfavourable comparison between Canadian programs and their competitors' countries programs.

4. Discriminatory practices in the granting of aid is seen as a problem caused by both the granting nation and some recipients. Some companies receive business for non-competitive reasons; for example, preference is given to public companies or the auxiliary financing is given to selected private insurance and export financing contractors. In the recipient country, discrimination in the distribution of aid can occur against local subsidiaries of foreign firms.

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Invitations to tender for projects funded by international agencies or regional banks give preference to the specifications with which the tender writer is familiar. Cases exist of a positive correlation between the nationality of consultants working for institutions and the countries from which engineering supplies and services are purchased.

It is interesting to note that both the U.S. AID and CIDA have rules and regulations which open up a number of projects to greater competition by allowing international firms (from Code 941 countries) to compete on an equal footing with nationals. While industrial spokesmen in both countries are unhappy with this situation, it does present an area where the total world aid structure has been made more open.

When aid dollars flow through international agencies such as the World Bank or the regional banks, consulting engineers are fairly comfortable that there is no discrimination except in those rare instances where an "old boy network" may exist between agency officials (consultants) and their national firms.

5. Business practices of firms can be a problem albeit little can be done in the way of government negotiations. In pure consulting services, Canadian firms rank well in terms of size: Lavalin (1), Monenco (2), Nedeco (Netherlands) (3) and SNC (4). Where there are

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goods and/or financial requirements, e.g. when the contract goes beyond consulting, other firms can be more competitive at least in terms of timing and interest charges. Canadian firms are only now getting more into this market, but the structural problems associated with trade are not due to government action except in those areas mentioned in points one to four above.

6. Other distortions impact on competition. Direct government intervention occurs, particularly to major projects where various forms of co-operation are involved (technology transfer, financing, supply of goods, etc). Political pressures and economic distortions are introduced, with such activity being prevalent in the least developed countries but found wherever government "blessing" is required on either side of the contract.

Proposals which need to include the financing of not only the consulting engineering content but also on the cost of plant and construction have been serious impediments up to now, as have counterpurchase requirements. Canadian firms, who do not have the closely knit ties to other sectors of the economy, are only now learning how to operate successfully in that type of market.

Technical assistance and provision of training agreements between countries often include considerable funds for project development and consulting studies. The provision of technical assistance can often

remove a large part of the development market from open competition. Reasons for "free work" are often to further political interests as well as enhance goods sales.

(b) Other Impediments

Compared to the problems of "unfair competition", Canadian consulting firms would class the following categories as merely irritants. It would make business easier and more profitable if they were removed, but familiarity with the export market can give consultants the ability to do business in any case. Many of the problems arise for non-trade reasons and were not initially envisaged as of particular importance to trade. Others are specific in nature having to do with the characteristics of trade in services. Canadian firms often encounter these irritants in developing countries where 80% of their export fees have been generated, but some are also found in developed countries.

1. Problems of access can often determine whether or not contracts in particular countries are worth pursuing. There is a growing tendency to limit the right of establishment in third world countries or to restrict that right to a certain range of activities. The establishment in many countries often has to take the route of joint venture, with some countries mandating a controlling interest by the local firm. Most consulting engineering firms see this as a normal and even

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beneficial means of doing business and transmitting technological advances from developed to underdeveloped areas and sectors. It is simply good business practice if the local partner is qualified and carries his own weight, but becomes an irritant if revenues earned don't correspond to efforts put into the project.

There are visa provisions concerning the entry of persons. In most developed countries these are no more and are often less onerous than similar regulations in Canada. In other countries, problems can arise with administrative capability, not with regulations themselves. Where there is direct government funding, or personnel are working under contracts awarded by international institutions, visa requirements are not a problem. With specific reference to the U.S., the Task Force did receive the impression that the industry would feel better if access to the U.S. was made easier, although the general philosophy of regulation was thought to be the same in both countries.

There are licensing restrictions by state in the U.S. but this is not at present a problem in other countries. The U.K. and South Africa are in the process of establishing a licensing system. Most American States require that a professional engineer pass an exam before getting a license to practice even though the degree granting university might be accredited. These licences are often not transferable across state lines. However, in most states a person can work without a license if there is another licensed person in the firm who will sign off the finished material.

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4. Engineers often require goods (equipment, drawings, etc.) which fall under customs regulations. U.S. Customs authorities levy a 3% duty on the "value" of engineering drawings (as represented by Manpower and other costs to prepare). They permit temporary entry (6 months) for review and reproduction against a bond guaranteeing re-export. The amount of duty levied by Canada and the U.S. appears to be roughly similar, although they are computed differently. In other countries, both OECD and LDC's, customs delays may inhibit foreign contractors' ability to complete projects within the time specified. Customs - related costs and delays create problems for foreign contractors and, it was suggested to the Task Force, may have been deliberately used to reduce a market's attractiveness.

In LDC's especially, there are customs barriers including

- quantitative restrictions
- obligation to purchase materials locally
- obligation to use local shipping and insurance companies for goods
- arbitrariness and lack of transparency on how value is determined
- lack of tariff exemption rules
- lack of temporary importation rules

Of course, a number of these problems could be covered by existing GATT provisions, if applicable in the countries in question. With

Canadian companies not having vertical integration, costs incurred by these barriers assume a higher proportion of the contract than is the case of other country competitors.

5. Problems of standards, technical regulations, etc. are found in all other countries as there is no uniformity in engineering quality control. In certain cases, regulations by the very nature under which they are imposed can result in significant trade barriers, far beyond normal adaptation potential by firms. The trade barrier might be aggravated by a transparency problem or frequent modification to the regulations. This field of government control is one where continued harmonization efforts are desirable.

6. Interfirm relations within particular countries and the activities of MNE's can restrict the market size but for the most part this type of restriction is not due to government action. Even where governments can take action, e.g. dumping provision, this type of private enterprise activity is particularly difficult to prove as a nefarious trade activity and, in any case, is limited by a lack of dispute mechanisms covering service trade.

7. Restrictions in other service areas can reduce the dimensions of a country's market and increase costs for what is biddable by foreign consulting firms. Intellectual property or information tied up in patents or restricted from moving to certain markets can place firms not having access to this knowledge at a competitive disadvantage. A

straight technological competitive edge is not a trade problem. However, if the advantage becomes locked into place by government imposed standards, regulations, etc, so that equally advantageous foreign technologies are excluded, then a trade restriction has become established.

The increasing amounts of regulation and restrictive practices surrounding data flows has caused some markets to be much less profitable than they used to be. The transmittal of information (or inability to do so easily) has the potential of becoming a major trade barrier for consulting engineers in many of the developing countries. As countries develop, these restrictions could multiply in scope, by sectors and regions.

Transportation becomes a problem when consultants need to move material. Shipping or air freight often needs to be through national flag carriers which can add direct costs and indirect costs caused by time delays.

Insurance on personnel and material often needs to be placed in the local market. With a decision that more reliability is needed, insurance is often duplicated with respectable international firms.

All of the above have been encountered by Canadian firms but they have all developed ways of either getting around such irritants or

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passing the costs on to the consumer. Such irritants tend to make doing business more costly and places a requirement to commit more front end costs to the project. Negotiations on contracts can resolve many of these problems or at least obtain adequate monetary compensation for costs incurred. However, in markets where there is fierce competition, time delays and unreasonable costs incurred can (i) tip the scales to local firms, or (ii) allow vertically integrated companies to shift many of the costs from the consulting function to the goods supply function, where profits on follow up sales can be several orders of magnitude larger.

Where the Canadian company has developed an exceedingly good reputation and/or has control over highly specialized technologies, then markets can be developed and won at least as far as the companies ability to export. The above array of trade impediments do, however, make some countries unattractive as markets.

(c) Problems in Conducting Business

During the project or upon its completion, various Canadian companies have run into additional problems which can be considered as trade impediments. Most of these revolve around tax issues or payment problems. Some other developed countries have a more supportive tax structure for professionals working abroad than does Canada. This can either be interpreted as an unhelpful domestic Canadian policy or as

another form of subsidization by Canada's major competitors. Many Canadian companies are increasingly recruiting personnel offshore for offshore projects, the Task Force was informed that this trend was at least due to Canadian tax policy.

Other questions arise on payment problems. Some countries withhold payment until all tax rulings have been resolved. Payments are often delayed, but it is probable that this is an administrative rather than trade barrier problem. Payment by counterpurchase has already been mentioned.

Of a more serious nature is the limitation on remittances. Some countries have very strict limitations on the amounts of profit which can be removed from the country. This can now be recognized as a principle barrier whereby some countries discourage foreign firms from bidding on projects. Of a similar nature is the rapidly increasing cost of non-reimbursable items - i.e. bonds, bank guarantees, etc.

(d) Government Procurement

Much of the preceeding discussion on trade impediments has relevance to government procurement. Many governments use their own contracts as a means of testing services programs and policies and in many LDC's the government is the largest buyer of services. As there is a government procurement paper elsewhere in the report, problems faced in this area will be described there.

(iv) The Negotiating Position

For purposes of negotiation, there are sound industry and policy reasons why issues related to the U.S. should be handled differently from a broader set of issues found in a multinational context. Some issues are common, others clearly are bilateral in nature.

(a) The U.S.

For this sector, there is a North American market which shows common technologies, ways of doing business, integrated communication systems, and roughly similar standards. There is already, and the trend is growing, a substantial number of firms which have important subsidiaries in each other's country. Others, without formal subsidiaries, are accustomed to work in the U.S. if they have developed an export capability.

By simple historical effort, both companies and professional associations have developed mechanisms and procedures which work to overcome problems caused by nationality. There are jurisdictional problems as each state and each province has their own peculiar regulations and licensing requirements. As well, each country controls such things as immigration and customs. The message comes through loud and clear that, while government support would be welcome on certain specific issues (given below), nothing should be done to rock the boat

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and/or change existing Canadian policy. The fear of retaliation to restrict markets in the U.S. outweighs what can be gained. Canadian industry at least is opting for the status quo except in the following technical areas.

Customs regulations on goods necessary to conduct business is a concern. Meetings between ACEC/Canada and ACEA/U.S. have identified that the amount of duty levied respectively by Canada and the U.S. appears to be similar although there are differences of approach. Negotiations should work towards removing the duty altogether and thus simplifying border transit.

Foreign personnel movement is regulated by the Immigration Act-1976 in Canada and by Immigration and Nationality Act in the U.S. All persons entering Canada to work on a temporary basis must have a work permit, personnel transferring to Canadian subsidiaries may be allowed entry subject to Immigration clearance only, and other personnel must also have Canada Manpower clearances to the effect that suitable equivalent personnel are not available from Canadian permanent residents. U.S. regulations categorize somewhat differently, but it is judged that the philosophy and regulatory instruments for control are similar on both sides of the border.

Negotiations should not remove these controls, but the industry would clearly like an application regime which was not capricious (either in time or local) and which had roughly equal degrees of stringency. Improved processing on the part of both countries (speed) would be desirable.

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Professional licencing requirements are established by provinces and states respectively, with legislative authorities devolved to professional associations. Here Canadians appear to be at a disadvantage insofar as they have to pass exams for each state while Americans do not have to go through a similar process in Canada. Once registered in a state or province, an engineer (regardless of nationality) finds it an easy process to establish his or her professional qualifications in other provinces. In the U.S., this establishment can be easy or very complicated depending on each States' regulatory environment.

Negotiations can utilize this difference if Canada needs a little something extra to throw on the scales, however, these are professional regulations and cannot be changed without professional and provincial (state) approval. The professional associations in both countries has taken this under advisement. One solution would be to establish exams and tighten provincial regulations to harmonize with the state.

Government procurement is raised as an issue, but it is an accepted fact of business that governments would shift business to local firms and that it was a business requirement to establish a local entity and/or joint venture arrangement. In practice, governments do not have formal regulations encouraging local procurement but in most cases policies and judgments assess overall benefit to the community. Problems do occur when the policies are implemented arbitrarily for all engineering services procured. Local and regional policies are for all

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practical purposes unnegotiable in both countries. Large national projects should be selected on the basis of ability/budget/time schedule and at this level Canada should express concern about the Buy American (State) proliferations. We would have to be prepared to discuss buy provincial (Alberta, Nfld., Quebec), the NEP and the moral suasion surrounding the megaprojects. Overall, negotiations should develop a status quo stance for the next 5 years, and/or the removal of formal legislated authorities. Any move to restrict joint venture and right of access should be vigorously opposed.

(b) The Developing World

Virtually all developing countries are in the process of establishing and/or strengthening various components of the consulting engineering field. Thus, in order to export, Canadian firms have to transmit technologies and infrastructure which are at the leading edge of each countries' development. In most cases, as local talent becomes developed, regulations and policies are introduced for protection but the development process has opened new markets.

In recognition of restrictive government policies in areas which were once thought of as free markets, negotiations could either be handled bilaterally with each country (or perhaps a small group of countries with similar restrictions) or could ultimately have a set of negotiations for services similar to those leading up to the Tokyo round.

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The problem of highest priority for the sector revolves around unfair subsidization of firms by third country governments; the various form of such subsidization are spelled out in the body of this paper. Many of the large foreign consulting engineering firms offer consulting services at subsidized rates or, in many cases, even free to serve as a loss leader for the sale of goods. Major governments who participate extensively in this endeavour are Japan, France, Great Britain, Italy and other OECD countries in selected developing countries. There are also a number of developing countries who unfairly compete in this matter, specifically, Brazil, India, Mexico, Israel and Korea and Taiwan at times. Such export subsidies are in many cases tied to or are similar to the subsidies given for goods and could be treated under GATT Guidelines and Codes. The work done by the OECD Secretariat on Export Credits would also be useful in correcting the problem.

In practical terms, negotiations could commence with the small group of countries identified above to search out ways subsidization practices could be rolled back and/or eliminated altogether. The U.S. would be a natural ally in supporting this position.

Many of the other impediments to trade were considered to be irritants rather than major problems. It would make life easier for firms to have these irritants negotiated out of existence. Some time should be spent on them, but very little should be given up from Canada's view point.

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Things like revised tax agreements to overcome double taxation and withholding tax problems would fall into existing bilateral negotiating frameworks. Right of access could be an appropriate subject for bilateral talks with some of the more important markets which are too restrictive in this fashion.

(c) The Developed Countries

The Trade Committee of the OECD is devoting a lot of attention and resources in identifying trade barriers amongst its member countries in this sector. The work plan is quite detailed with major categories being

- (i) obstacles to trade in goods necessary for services;
- (ii) competition problems associated with the functioning of the market and with practices of firms in the sector;
- (iii) establishment/investment;
- (iv) government procurement;
- (v) government regulations - people, subsidies, taxation.

By the time work is advanced and OECD countries have participated in analysing their own and other countries' policies, a good inventory of trade barriers and unfair trade practices will be obtained.

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Canada's negotiating stance should be for active and increasing participation in this exercise. The long list of trade barriers currently identified make it increasingly clear that West European and Japan are closed markets. If developed country markets were liberalized as an OECD exercise it would not impact negatively on overall Canadian engineering performance. Reductions would sharpen competition and facilitate technology transfer in specialty areas of engineering, allowing Canadian firms to participate in markets now essentially of little interest to them.

(d) Eastern Europe

These countries do not normally purchase consulting services separately but rather procure technology as part of a turnkey contract. In addition, export sales to these countries often require barter arrangements not familiar to Canadian firms. Therefore, even allowing for improved trade access, this market will remain difficult to penetrate.

(e) Program Adjustments

The consulting engineering fraternity makes a positive contribution to Canada's trade position in exporting services and can provide opportunities for the sale of manufactured goods. A cohesive domestic/trade policy package needed to be developed to ensure that the

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domestic industry can take advantage of opportunities abroad and withstand the increased competition at home resulting from a trade liberalization trend. The following check-list is certainly not all-inclusive, and removal of government support in other countries could equally solve the problem, but to enhance competitive ability the government could

- (i) enhance the financial packages available to support the front-end costs of bidding on export projects;
- (ii) assess the adequacy of the risk-sharing facility (to be done by the Export Trade Development Board);
- (iii) streamline and improve the insurance and financing package specifically to acknowledge the requirements of service (versus goods) exports;
- (iv) re-negotiate existing tax treaties and put in place tax policies comparable in leniency to our major international competitors;
- (v) adjust the rules of existing programs for trade and aid to allow greater maneuverability and speed in obtaining contracts.

APPENDIX I

THE 12 SECTORS OF CONSULTING ENGINEERS SERVICES

| | <u>Fields Covered*</u> |
|--|--|
| 1. MUNICIPAL | Water supply, sewage disposal, waste disposal roads and streets, traffic engineering, urban and regional planning |
| 2. BUILDINGS | Acoustics, communications, electrical, elevators, escalators, and moving sidewalks, heating, ventilating and air conditioning, illumination, mechanical, piping systems, refrigeration, structural |
| 3. PETROLEUM & NATURAL GAS | Exploration, extraction and separation, pipelines, gas process plants, oil refineries |
| 4. POWER (Power Generation, Transmission and Distribution) | Systems planning and operation, hydro power, thermal power, nuclear, transmission and distribution |
| 5. MINING & METALLURGY | Exploration, mine planning and production, mineral beneficiation, smelting, refining |
| 6. PLANT PROCESS | Alum. fabricating, alum. smelting, automotive plants, breweries, cement plants, chemical plants, distilleries, feed and flour mills, fertilizer plants, food processing, foundries, glass and ceramics, industrial environmental control facilities, industrial power houses, metal working, misc. manufacturing plants, petro-chemical plants, steel mills, textile mills, wood working |
| 7. TRANSPORTATION (Bridges, Tunnels, Highways and Railways) | Bridges, tunnels, highways and expressways, railways, public transit, transportation studies |
| 8. FORESTRY, ETC. (Agriculture, Fisheries, Forestry, Forest Products) | Agricultural engineering, fisheries, forestry, logging, sawmills, veneer and plywood, particle-board and waferboard mills, hard and soft board mills, pulp mills, paper mills |
| 9. DAMS & IRRIGATION | Dams, irrigation, flood control |
| 10. AIR & SEAPORTS | Airports, harbours, docks and jetties, dredging river and coastal works, terminals and warehouses, transportation studies, oceanography and hydrography |
| 11. TELECOMMUNICATIONS | Microwave, broadcasting, wire line transmission, telephone systems, supervisory control and data transmission |
| 12. MISCELLANEOUS | Air and noise pollution control, arbitration and litigation, computer science and data processing, environmental impact studies, interior design, naval architecture, remote sensing and photogrammetric soil mechanics |

APPENDIX II

SECTORS CONTINUE TO BE HIGHLY CYCLICAL

| AVERAGE ANNUAL REAL RATE OF GROWTH | THE 1960's 1961-71 | EARLY 1970's 1971-74 | MID 1970's 1974-77 | LATE 1970's 1978-80 |
|--|--|---|--|--|
| Substantial Growth (Over 10%) | Mining & Metallurgy | Power Dams & Irrigation | Power Petroleum & Natural Gas | Power Plant Process |
| Good Growth (5 to 10%) | Power Plant Process Municipal Petroleum & Natural Gas Buildings | Municipal Forestry, etc. Air and Sea Ports Petroleum & Natural Gas Communication | | |
| Modest Growth (0 to 5%) | Communications Transportation Forestry, etc. | Buildings Plant Process Transportation | Transportation Telecomm | Telecomm Petroleum & Natural Gas |
| Negative Growth | Air and Sea Ports Dams & Irrigation | Mining & Metallurgy | Buildings Municipal Mining & Metallurgy Plant Process Forestry Dams & Irr. Air & Seaports | Buildings Municipal Mining/Metallurgy Transportation Forestry Dams/Irrigation Air/Seaports |

ANNEX

TASK FORCE ON

TRADE IN SERVICES

FRANCHISING

(i) Structure

The term franchising is used to describe a particular marketing system for selling both goods and services.* It takes many different forms, but two generally accepted categories are: (i) the traditional which is a closely tied relationship between franchisor and franchisee (e.g. the car dealership) and (ii) the modern, which has a wide variety of business formats, ranging from use of name only to a rigidly applied total marketing system.

The assumption has been that this method of marketing is rapidly growing, with the domestic market reaching saturation levels in many sub-sectors. However, no statistics are available which give an overall picture of the role of franchising in the Canadian marketplace. Nor is employment or labour statistics available, so it becomes impossible to assess levels of productivity or profitability.

* Commentary and statistical information have been obtained from the Franchise Section, Merchandising Division, Office of Service Industries, DRIE

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The Canadian marketplace has a large degree of foreign penetration, with over 7,500 franchised outlets of American firms (1979) and several hundred from other foreign countries. Statistics Canada estimates that there were approximately 12.3 thousand outlets in 1979 with sales of \$15 billion.

(ii) Trade Performance

Imports

Imports relate to the degree to which foreign companies use the franchising mode to bring in supplies and services. Statistics Canada reports an \$11 million importation (1977) which presumably is related to management fees, royalties, dividends, etc. While this figure is highly questionable, no better one exists. How imports are factored between tradeable and non-tradeable services is not known. The average legal fee of \$50,000 in the U.S. to establish a franchise company serves as one example as to the expense involved.

Exports

Canadian franchisors concentrate on relatively few foreign markets (U.S., U.K., France, Japan) and often use master franchise agreements with local business interests to add local expertise and satisfy legal requirements. Firms generally experience difficulties due to cultural barriers rather than government barriers.

Exports appear to be weak except for those few companies who are beginning to export their name and some components of their marketing

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system. In the "desirable" foreign marketplace, Canadian firms are often in direct competition with American-based franchise systems. The major problem is one of marketing - positioning. At the present time, it is probable that the capital outflows necessary to become established abroad are more than the profits and royalties remitted.

For trade in services purposes, franchising has its major impact in the non-tradeable sector with regard to balance of payments. The potential for using this method as a vehicle for export has not been determined.

(iii) Legislation, Policies and Regulations of Governments in Canada

There are no Canadian laws or policies which apply specifically to franchising which can be interpreted as being trade barriers. One needs to go to business policy in general, as for example FIRA. Provinces (Alberta, Quebec) are placing franchise laws into effect, but they are generally applied to all business both domestic and foreign with no discrimination on the basis of ownership.

(iv) Impediments to Canadian Exports

Impediments in other countries have not been analysed as being specifically applied against foreign franchisors. There are general business laws which have been identified (e.g. right of establishment) which are applicable. However, no knowledge exists where franchising

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per se has been singled out as an area where trade impediments are being imposed.

(v) Conclusions

With regard to negotiation, Canada should be wary of participation until more is known about the subject and some linkages can be established between this type of marketing and its impact upon the balance of payments and trade in general.

It appears that, at least between the U.S. and Canada, markets are fairly open with few restrictions being applied. With the information provided to date, U.S. companies have the market advantage. However no assessment of potential future benefits of trade liberalization or restriction has been made. Thus, at the present time, it would be advisable to ignore this subject in a trade negotiation context until other countries place it on the table.

ANNEX

HEALTH SERVICES

The health sector in Canada, although mainly in the public domain, exhibits characteristics and trends which make it deserving of consideration in terms of trade in services.* As there are not a large number of restrictions which need to be negotiated in an international forum, this sector will be discussed for its potential contribution to Canada's trade patterns.

I STRUCTURE

In 1979, the Canadian health care industry accounted for 7.2% of GNP, or 18.9 billion dollars. This amount is split between public expenditures of 14 billion and the private sector for almost 5 billion. Trends indicate that the sector will grow to 8% of GNP by 1990, and then stabilize. This level of demand is typical of a developed country which has shown major efforts to enhance health care levels for its population.

The locus of services rendered to Canadians is usually determined by demographic need. Medical schools, research, teaching, specialized service, and those surgical procedures and investigations which are relatively new are found in larger population centres. Specialized treatment centres, rehabilitation, children's hospitals, cancer centres, research centres, are usually centralized. It is

* This paper was written from material presented by Health and Welfare and other organizations with a health responsibility.

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estimated that over 90% of all Canadians are within one hour driving time of a physician's office and/or hospital.

This sector is characterized by a high degree of Canadian ownership. The public sector - hospitals, institutions, etc., are publicly owned and non-profit. Hospitals are independently controlled by a local voluntary board and are financed through joint federal-provincial agreements that guarantee Canadians accessibility, comprehensiveness, portability, and public administration for hospital medical services.

The private sector is also mainly Canadian owned. Professionals and professional services are almost exclusively Canadian. The pharmaceutical industry is largely foreign owned. Proprietary Canadian nursing homes, usually affiliated with major real estate or insurance companies, have some degree of foreign ownership, but these are governed closely by provincial regulations. In marketing terms, the institutional services sector is regulated by many of the same principles affecting a public utility i.e., public licence, standards, budgeting fee control, etc.

The labour characteristics of this sector accrue from its public sector orientation. As a percentage of the work force, the industry represents over 6%, with the key professional groups being physicians (43,000), nurses (225,000), health services executives (3,000), pharmacists (6,000). Without exception, all of these groups are highly regulated, and standards of responsibility are set between various

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professional associations and governments. There appears to be an adequate stock of people at all levels, with the possible exception of nursing. With saturation levels on demand being attained, there is growing indications that the numbers of people involved in the medical industry will not grow substantially. There may not be a real need for some of these people within five to ten years, which would free resources for an export orientation. Salaries for Canadian professionals rank amongst the highest in the world. Salaries for doctors, for example, would rank within the first five countries, even though they are roughly 20% below the U.S. The productivity of Canadian doctors and professionals, hospitals, etc., rank high in relation to comparative centres i.e., the U.S., England and France. In economic terms, the Canadian health system would be competitive in third country markets.

II TRADE PERFORMANCE

Imports

The public nature of hospital care has effectively precluded the internationally oriented hospital management companies from penetrating the Canadian market. However, there is growing awareness on the part of public health administrators that complete health care packages by private foreign companies (U.S., European, Japan) are available. In fact, this type of export by these countries provides the mainstay of their health exports. The type of package offered would find ready markets in smaller communities and in the more remote areas of Canada.