

International Cheese Council of Canada
Submission to the Standing Committee on International Trade
December 16, 2020

The Tariff Rate Quota (TRQ) System: Background

The International Cheese Council of Canada (ICCC) has co-existed with Canada's supply-managed dairy sector for 45 years. We recognize the rationale underlying the supply management system and are not advocating for its dismantling. We simply seek to have the impediments to importing *within quota* be removed and the administration of the system made more efficient and less burdensome. The protection afforded to domestic dairy producers should be focused on a single key principle: a ceiling on the amount of foreign product allowed into Canada. Unfortunately, in practice, the current system extends much further than that. This submission elaborates on some of the obstacles to market access that have been layered on top of the quota system in the context of the transitional trade deal between Canada and the United Kingdom.

Under the TRQ system, Canada establishes a specific quantity of a product that can be imported at a lower (or zero) rate of duty¹. Cheese TRQs were made necessary by Canada's commitments – under various international trade treaties – to allow access to Canada's domestic cheese market. The TRQs are administered by Global Affairs Canada (GAC) in accordance with these treaty obligations and Canada's *Export and Import Permits Act* (EIPA). TRQs are distributed by GAC according to precise allocation methods².

As has often been asserted by our country's trade partners, Canada's cheese market is very well-protected. While there is no tariff on the relatively small amount of cheese imported under TRQs, Canada imposes a 245.5% border tax on Non-TRQ cheese³. (To put this figure into perspective, the average Canadian customs tariff is 5%.) This system means that cheese TRQs are an extremely valuable commodity.

The World Trade Organization (WTO) TRQ for 'cheese of all types' allows importers to bring cheese into Canada from EU and non-EU states. The allocations are organized into the EU pool and the non-EU pool. The WTO TRQ is given by GAC according to the historical allocation method, meaning that the "quota is fully allocated to companies who were active before the initial TRQ began, proportional to their historical activity"⁴. These companies retain their share of the allocation by demonstrating continuous activity in the sector from year-to-year, which requires using at least 95% of their quota⁵. ICCC Members are longstanding and significant holders of EU and non-EU Cheese TRQ allocations.

Under the Canada-EU Comprehensive Economic and Trade Agreement (CETA), Canada reallocated 800,000 kilograms from the non-EU pool to the EU pool and decreed that transfers between both reserves by businesses would no longer be allowed⁶. The increase in EU-origin cheese was considered a gain by the EU during the negotiations.

Canada-UK Trade

Significantly, as a result of Brexit, the UK will cease to benefit from the market access achieved by the EU as part of CETA. However, the UK and Canada agreed to a 3-year transition period during which the UK will continue to have access to the WTO cheese TRQ EU pool, despite having become a non-EU country.

¹ [https://www.international.gc.ca/trade-commerce/controls-controles/notices-avis/trq_info_ct.aspx?lang=eng#:~:text=A%20TRQ%20is%20a%20quota,over%20access\)%20rate%20of%20duty.](https://www.international.gc.ca/trade-commerce/controls-controles/notices-avis/trq_info_ct.aspx?lang=eng#:~:text=A%20TRQ%20is%20a%20quota,over%20access)%20rate%20of%20duty.)

² <https://www.international.gc.ca/trade-commerce/consultations/TRQ-CT/dpe-lvo-questions.aspx?lang=eng>

³ https://legacy.trade.gov/td/standards/toolkits/nte_canada.pdf

⁴ <https://www.international.gc.ca/trade-commerce/consultations/TRQ-CT/dpe-lvo-questions.aspx?lang=eng>

⁵ https://www.international.gc.ca/trade-commerce/controls-controles/notices-avis/998_2.aspx?lang=eng#a3

⁶ <https://www.international.gc.ca/controls-controles/prod/agri/dairy-laitiers/notices-avis/906.aspx?lang=eng>

Unfortunately, this solution provides only short-term relief to ICCM Members as the outcome of GAC's review of the TRQ system – which may change the allocation method for the TRQ – remains unclear. The uncertainty is an impediment to business planning and investment.

Moreover, after the 3-year transition period, the WTO EU TRQ will remain the same size -- despite the UK's departure. At that point, the UK will need to seek WTO TRQ from the smaller non-EU share – which already has a utilisation rate of above 97% every year and automatic renewal for any license holder whose rate is above 95%⁷. (As quota is valuable, most license holders utilise their licenses to the fullest extent possible every year.) From 2015 to 2019, cheese imports from the UK have increased from 1,014,616 to 1,778,113 kg (and they keep growing)⁸. It is clear that these quantities would not "fit" into the amount available in the pool of quota assigned to WTO non-EU TRQ countries, which stood at 6,140,034 kg in 2019⁹.

After 2023, Canadian importers who had been using CETA TRQs to import cheese from the UK to Canada, and who are not holders of (unused) WTO non-EU TRQ, will find themselves faced with three unappealing options:

- 1) cease importing UK cheese products to Canada;
- 2) substitute some of their imports from non-EU countries with imports from the UK; or
- 3) import cheese from the UK to Canada with a 245.5% tariff.

Each of these scenarios will cause economic pain to Canadian cheese importers; and, none of the scenarios deliver an improved outcome for Canadian consumers.

TRQ Allocation Methods Offend Canada's Trading Partners

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) provides yet another example of the stealthy protectionism built into GAC's TRQ administration. The most egregious example is the allocation of 85% of each CPTPP TRQ to domestic processors, leaving just 15% for distributors¹⁰. This approach forces international cheese producers to do business with their Canadian-based competitors, a policy measure that goes well beyond the protections Canada's supply management system purports to provide.

The effect of GAC's protectionist approach to TRQ administration is that there has been minimal cheese imports from CPTPP member countries: the utilisation rate of CPTPP TRQs varied from 11% to 57% in 2019¹¹. So, even though Canada theoretically opened its market as part of the CPTPP – and even though compensation has been provided to domestic producers for 'accepting' and adjusting to the increased competition – GAC's practices have effectively throttled imports from CPTPP countries.

Conclusion

UK Secretary of State for International Trade Elizabeth Truss has said accession to the CPTPP is a strategic priority of the British government; she regards the CPTPP as a way to gain access to the

⁷ https://www.eics-scei.gc.ca/report-rapport/Arc_2017_APRMT61C-C.htm ; https://www.eics-scei.gc.ca/report-rapport/Arc_2018_APRMT61C-C.htm ; <https://www.eics-scei.gc.ca/report-rapport/APRMT61C-C-19.htm>

⁸ <https://aimis-simia-cdic-ccil.agr.gc.ca/rp/index-eng.cfm?action=gR&r=168&signature=8D152F85A7FD7952E82512E44D49F1F6&pdctc=&pTpl=1&pr=1&pr=5#wb-cont>

⁹ <https://www.eics-scei.gc.ca/report-rapport/APRMT61C-C-19.htm>

¹⁰ https://www.international.gc.ca/trade-commerce/controls-contrôles/notices-avis/995_2.aspx?lang=eng;

https://www.international.gc.ca/trade-commerce/controls-contrôles/notices-avis/997_2.aspx?lang=eng;

https://www.international.gc.ca/trade-commerce/controls-contrôles/notices-avis/996_2.aspx?lang=eng

¹¹ <https://www.eics-scei.gc.ca/report-rapport/APRMT61C-C-19.htm>

Canadian dairy market. But, unless TRQ administration practices change, the UK may discover, as other of Canada's trade partners have, that the path to Canada's cheese consumers is strewn with GAC-constructed obstacles.

Though some regard GAC's protectionist approach to TRQ administration practices as producing a 'win' for domestic producers, it may turn out to be a pyrrhic victory. Canada's trade partners in the EU and U.S. have come to realize that the additional market access for cheese achieved during tough bilateral negotiations was burdened with invisible strings. And, if the benefits of a trade agreement do not flow both ways, it is unwise to consider the issue to be settled.

As recent proof of this point, United States Trade Representative Robert Lighthizer announced on December 9 that the U.S. was challenging Canada's allocation of CUSMA dairy TRQs. The U.S. contends that Canada's administration of the dairy TRQs (i.e., reserving part of each TRQ for processors) is contrary to the provisions of the trade agreement, resulting in the undermining of the ability of American farmers and producers to use the dairy TRQ to access the Canadian market¹².

While Canada's trade partners grudgingly accept our supply management system, they have consistently indicated their disapproval with the additional obstacles to market access that have been built into the TRQ administration system. Over the years, Canada has faced significant and ongoing pressure to relinquish its supply-management system. Successive federal governments have fought hard to protect the system and, more recently, have yielded relatively small percentages of protected markets as part of trade agreement negotiations. But, if Canada wants to avoid further international pressure to dismantle the entire system, it should reconsider the current approach which, via its TRQ administration, risks bringing Canada into trade disputes and into disrepute.

The ICCC recommends that the Government of Canada's approach to supply management be streamlined to a single overarching policy: **a specific limit to the amount of foreign product allowed into Canada**. Respecting that goal should not involve expending any additional time or effort on implementing supplementary, or covert, measures designed to impede foreign product or favour domestic producers.

If, for example, a trade deal leads to one of Canada's protected markets being opened to 3% of foreign product, TRQ administration should not undermine that commitment by building in complexity and administrative practices that inhibit free trade, add administrative burdens and costs for all involved, and damage trade relationships.

In 2019, Global Affairs Canada launched a review of the TRQ system. The second phase is expected to resume soon. The ICCC believes the Review should ensure the system is aligned with this 'back to basics' approach to administering Canada's supply management system.

To achieve this objective, the ICCC advocates that GAC's TRQ Review should ensure the system respects the following 6 principles:

¹² <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/december/united-states-takes-action-american-dairy-farmers-filing-first-ever-usmca-enforcement-action>

1. **Cheese exporters located in countries that are Canada's trading partners must be able to sell directly to their customers, rather than be forced to sell to their competitors.** Domestic dairy producers and processors should not be eligible for cheese TRQs because they have demonstrated that they do not wish to import cheese that competes with domestic produce and they are clearly not the most likely persons to use it – two key principles enshrined in trade agreements. Moreover, cheese TRQs should not be administered as a domestic compensation scheme intended to make up for the market share yielded in negotiations (for which Canadian cheese producers have already been compensated).
2. **Canada's imported cheese TRQ allocations should no longer be based on production or sales of domestic cheese.** Local content preferences for Canadian milk and cheese are contrary to international trade treaty obligations.
3. **All TRQ cheese allocation should be based on import performance.** Import *purchases* rather than *sales* should be used. An allocation method based on sales is inapt as it results in double-counting because several sales of the same cheese can occur in the supply chain. All cheese TRQs should be allocated according to the following formula:
 - a. The numerator is the applicant's preceding year actual total direct importations of cheese that is consumed in Canada; and
 - b. The denominator is the preceding year's total amount of all applicants' actual direct importations of cheese that is consumed in Canada.
4. **To enable New Entrants without TRQ to become eligible for TRQ, the first year of their allocation should be based on their preceding year volume of imported cheese sold into Canada.** After this first year, the New Entrants' allocation should be based on their preceding year's actual imports, and all of the foregoing other eligibility and activity requirements should apply.
5. **No transfers should be permitted.** Allocations holders with a utilization rate of less than 95% in the previous allocation year should have their allocation adjusted downward by an under-utilization penalty for the new allocation year. However, there should be no need for transfers if cheese TRQs were allocated to those that are most likely to use them. If transfers are allowed, they must not be included in calculations of Actual Level of Use.
6. **The threshold of activity for all cheese TRQs should be the amount of imports that results in an economically viable allocation of a container load.** Cheese is a perishable product and often must be shipped long distances in a container. A container load generally equates to 20,000 kilos. Despite knowing this, GAC has made many allocations of very low quantities, which are economically non-viable and often results in the allocations going unused.

The International Cheese Council of Canada

The ICCC is an association of cheese importers, which was founded in 1976 to manage the implementation of Tariff Rate Quota (TRQ) restrictions on cheese imports after it was added to the Import Control List (ICL) in 1975. For over 45 years, ICCC members have established a track record of responsible stewardship of Canada's cheese TRQ. Our Members are Canadian importers of cheese; our Associate Members include cheese importers from Britain, Europe and other countries that have entered into international trade treaties with Canada.