

1989

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Recommended Citation

Richard Mendelson, Timothy Josling, John Barton, and Scott Morse, *Wine Trade with Canada: A Case Study in Trade Deregulation*, 7 *INT'L TAX & BUS. LAW.* 91 (1989).

Available at: <http://scholarship.law.berkeley.edu/bjil/vol7/iss1/3>

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Wine Trade with Canada: A Case Study in Trade Deregulation

by
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INTRODUCTION

Canada has occupied center stage in recent efforts to deregulate international trade in wine, even though Canada is not among the world's major wine producers or consumers.¹ The widespread interest in Canadian wine deregulation stems from the significance the Canadian wine market has for the United States and for the European Community [hereinafter EC]. It also reflects the special role held by Canada's provinces in regulating the importation, distribution and sale of wine.

This article reviews the recent efforts, bilateral and multilateral, to deregulate international trade in wine with Canada. For each of the three principal actors — Canada, the United States, and the EC — there are different internal commercial, legal and policy issues which have affected the trade negotiation process. This complex set of issues sheds light on the dynamics of international trade deregulation in the wine sector and has some interesting implications for the future of trade regulations among developed countries.

The first part of this article explores the significance of Canada's wine market for the United States and the EC. Part I also briefly outlines the specific provincial controls that affect the Canadian wine market and the structure of the Canadian domestic wine industry. Part II compares recent

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1. In 1987, Canada ranked twenty-first in world wine consumption and twenty-sixth in world wine production. WINE INSTITUTE, ECONOMIC RESEARCH REPORT: INTERNATIONAL GRAPE AND WINE STATISTICS Tables 7, 9, at 8, 10 (Apr. 1988) [hereinafter WINE INSTITUTE INTERNATIONAL STATISTICS].

multilateral and bilateral international wine trade negotiations. Part III focuses more precisely on the concerns of the United States in these negotiations, and Part IV addresses European concerns. Part V discusses the division of Canadian provincial and federal authority over trade. The Conclusion suggests other, broader implications that the deregulation in wine trade will have on the international trading system as a whole.

I.

THE CANADIAN WINE MARKET

A. Significance for the United States and the EC

There are several reasons for the importance of wine market deregulation in Canada. Two of the world's leading wine producers, the United States and the EC, each have very strong commercial interests in the Canadian wine market (see Table 1) and, consequently, in its deregulation. The United States is the world's sixth largest wine producing nation and accounted for 5.3% of world wine production in 1987.² The EC's twelve member states³ accounted for 64.9% of world wine production in 1987.⁴

Canada is the United States' largest single export market for wine.⁵ This relationship has existed throughout the 1980's, with U.S. wine exports to Canada ranging from twenty-eight percent to fifty-nine percent of total U.S. wine exports.⁶ In 1987, for example, 124,801 hectoliters of U.S. wine were exported in bulk or bottle to Canada.⁷

The EC also has a significant interest in the Canadian wine market. Approximately forty-nine percent of the bottled wines sold in Canada come from an EC country, more than from any other single source (see Table 1). Canadian wines have a forty-five percent market share, compared to just over one percent for U.S. wines and about four percent for other imports (see Table 1). The Europeans jealously guard this special market position and endeavor to increase their market penetration in order to reduce their internal wine surplus.

2. *Id.* Table 7, at 8.

3. The European Community [hereinafter the EC] is currently comprised of twelve Member States: Belgium, Denmark, France, the Federal Republic of Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, and the United Kingdom. These nations [hereinafter Member States] adhere to the provisions of the Treaty Establishing the European Economic Community, Mar. 25, 1957, 294-297 U.N.T.S. 2 (French, German, Italian, and Dutch), *reprinted in* 1979 Gr. Brit. T.S. No. 15 (Cmd. 7460) (official English version) [hereinafter Treaty of Rome].

4. WINE INSTITUTE INTERNATIONAL STATISTICS, *supra* note 1, Table 7, at 8.

5. *Id.* Table 11, at 12.

6. Data provided by Wade Stevenson of the Wine Institute Economic Research Department, San Francisco, Cal. (Jan. 1989).

7. WINE INSTITUTE INTERNATIONAL STATISTICS, *supra* note 1, Table 11, at 12. Wine volume is expressed in liters not gallons. Gallonage equivalents may be determined by multiplying total liters by a conversion factor of 0.26417 gallons per liter.

TABLE 1
SALES OF DOMESTIC AND IMPORTED BOTTLED WINES
IN CANADA
1986

	<u>Hectoliters</u>	<u>Percent of Total</u>
Domestic	1,177,474	44.46
Imported	1,241,183	55.54
Total	2,418,657	100.00

Imported wine origin:

<u>Country</u>	<u>Hectoliters</u>	<u>Percent of Imported Total</u>
France	639,158	51.5
Italy	218,437	17.6
West Germany	122,268	9.9
Spain and Portugal	109,256	8.8
United States ⁸	26,515	2.1
Australia	12,440	1.0
Austria	7,747	0.6
South Africa	6,895	0.6
Other	98,467	7.9
Total	1,241,183	100.0

Source: CANADIAN WINE INSTITUTE, 1986 ANNUAL STATISTICAL REPORT (Sept. 1987).

B. Provincial Controls

Another reason for the considerable recent interest in Canadian wine deregulation efforts is the tight control over the internal wine market exerted by provincial governments, rather than by the federal government. Wine is a heavily regulated commodity throughout the world, partly as a result of its religious, medicinal, and cultural importance. Both the United States and the EC, however, have complained that the wine distribution and sales systems in the Canadian provinces are unusually restrictive. The situation is particularly acute in those Canadian provinces that have a local wine industry. Regulation of the wine trade in these provinces forms a part of provincial agricultural policy. In attempting to support local production, the provinces also discriminate against foreign wines.

Provincial governments use two different regulatory practices to protect local wine markets: limited listings of foreign wines and discriminatory price

8. These figures do not include over 90,000 hectoliters of bulk wine exported from the U.S. to Canada. Because many provinces have minimal domestic content rules for wine, most of the U.S. bulk wine is sold as Canadian wine. See WINE INSTITUTE INTERNATIONAL STATISTICS, *supra* note 1, Table 12, at 13.

markups. While the wine-listing issue is of prime concern to the U.S. producers, the question of differential markups is the most problematic issue for the EC, which already has its fair share of listings.

Each province and territory has an alcohol monopoly usually run by a government liquor control board or liquor commission.⁹ These entities administer nearly every aspect of importation and distribution of alcoholic beverages in Canada. In order for a wine to be sold in a given province, the provincial liquor board or commission must buy and "list" the product.¹⁰ There are two types of listings: (1) general listings, for wines that remain in the monopoly stores so long as they meet established sales quotas; and (2) special listings, for wines that are offered only once. The U.S. wine industry complains that general listings for its wines are sparse. Less than three percent of such listings in 1987 were for U.S. wines (see Table 2).

TABLE 2
WINE LISTINGS IN SELECTED PROVINCES
April 1987

<u>Province</u>	<u>Canada</u>	<u>U.S.</u>	<u>France</u>	<u>Italy</u>	<u>Other</u>	<u>Total</u>
British Columbia	380	21	139	49	123	712
Manitoba	217	27	227	87	197	755
New Brunswick	169	16	36	45	151*	417
Ontario**	495	42	304	182	42	1,065
Pr. Edward I.	78	19	50	20	55	222
Quebec**	2,369	13	400	100	218	3,100
Saskatchewan	125	23	126	53	119	446

Total Number of Listings Shown: 5,717

Total Number of U.S. Listings Shown: 161

* German imports accounted for all of the listings in this category.

** Figures dated July 11, 1986.

Source: Letter from James Clawson, consultant to the Wine Institute, to Richard Mendelson (Apr. 30, 1987).

Sharp restrictions on general listings, in effect, exclude U.S. producers from the Canadian wine market. Special listings alone are too limited to build consumers' confidence in U.S. labels and thus prevent any growth in brand loyalty.

Even when listed, foreign wines are subject to discriminatory markups, which discourage the purchase of imported wines in favor of cheaper domestic ones.¹¹ These markups, typically a fixed percentage of the cost of the

9. M. BROWN, M. DEWAR & P. WALLACE, INTERNATIONAL SURVEY: ALCOHOLIC BEVERAGE TAXATION AND CONTROL POLICIES 49-50 (5th ed. Nov. 1982).

10. OFFICE OF THE U.S. TRADE REPRESENTATIVE, NATIONAL TRADE ESTIMATE: 1986 REPORT ON FOREIGN TRADE BARRIERS 48 (1986) [hereinafter NATIONAL TRADE ESTIMATE].

11. COMMENTS OF THE CALIFORNIA WINE INSTITUTE ON THE U.S.-CANADA FREE TRADE AGREEMENT LEGISLATION BEFORE THE U.S. SENATE FINANCE COMMITTEE (Feb. 23,

wine, are set by the provincial liquor authorities and are paid by retail wine consumers. The discriminatory aspects of these markups are particularly noticeable in the wine-producing provinces of Ontario and British Columbia. In Ontario, the 1986 markup on local wines was one percent, on wine from other provinces in Canada it was forty-eight percent, and on imported wine the markup reached sixty-six percent (see Table 3). An imported wine would cost the consumer sixty-four percent more than a similar-value local wine. In British Columbia, imported (or other Canadian) wines would cost forty percent more than the local varieties as a result of the differential markups. Table 3 also indicates an increase in differential markups from 1979 through 1986. Thus, the disparity in retail prices between domestic and imported wines increased during the 1980's, further hindering imports.

C. *The Canadian Wine Industry*

A related issue concerning the deregulation of Canadian trade in wine is the widespread belief that the domestic wine industry cannot withstand greater competition from abroad. If more competitively priced, higher quality wines were to enter Canadian distribution channels from France, Italy, the United States, and other wine producing countries, it is feared that the local industry might not survive.

The Canadian wine industry is centered in Ontario and British Columbia, with small areas devoted to grape growing in Quebec and Nova Scotia. Ontario accounted for eighty-four percent of Canadian grape output in 1987 with over 9,000 acres under production (see Table 4). Several provinces have commercial wineries, processing grapes purchased from other areas.

Given the high degree of protection afforded by the current wine regulations, many of these wine producing areas would not be competitive under freer trade. The larger issue concerns more than just an industry protected from foreign competition; the differential markups discriminate against wines from other Canadian provinces as well as against foreign wines. In this way, the regulations have fostered protected industries within each province. The result is a fortress mentality in many of Canada's wine-producing provinces.

II.

RECENT WINE TRADE NEGOTIATIONS

Recent international wine trade negotiations have been either multilateral or bilateral. In multilateral negotiations, the emphasis has been on the application of uniform principles and practices to trade policies, even when such policies are administered by sub-national government agencies. In contrast, the bilateral negotiations have been more concerned with market access

1988) [hereinafter WINE INSTITUTE COMMENTS ON FTA] (available from the Wine Institute, San Francisco, Cal.).

TABLE 3
CANADIAN PROVINCIAL MARKUP PERCENTAGES
1979 and 1986

Province	Applied to Domestic Wines		Applied to Imported Wines	Differential (Import percentage above local)
	Local	Other Canadian		
ALBERTA				
1986		77%	83%	6%
1979		60%	64%	4%
<i>Increase in 1986 differential above 1979 differential = 2%</i>				
BRITISH COLUMBIA				
1986	50%	110%	110%	60%
1979	46%	100%	100%	54%
<i>Increase in 1986 differential above 1979 differential = 6%</i>				
MANITOBA				
1986	65%	75%	80%	15%
1979	55%	55%	55%	0%
<i>Increase in 1986 differential above 1979 differential = 15%</i>				
ONTARIO				
1986	1%	48%	66%	65%
1979	58%	105%	123%	65%
<i>Increase in 1986 differential above 1979 differential = 0%</i>				
QUEBEC				
1986	94%	105%	125%	31%
1979	87%	105%	107%	20%
<i>Increase in 1986 differential above 1979 differential = 11%</i>				
<i>Note: This markup is for imported wine bottled in Quebec.</i>				
SASKATCHEWAN				
1986	84%		89%	5%
1979	67%		72%	5%
<i>Increase in 1986 differential above 1979 differential = 0%</i>				

Source: Letter from James Clawson, consultant to the Wine Institute, to Richard Mendelson (Apr. 30, 1987).

TABLE 4
CANADIAN GRAPE AND WINE INDUSTRY

1) *Number of Grape Producers and Area Under Production by Province (estimate)*

	<u>Farms</u>	<u>Area</u> (hectares)	<u>Area</u> (acres)
Ontario	1,149	9,336	23,069
British Columbia	210	1,395	3,447
Quebec	47	69	170
Nova Scotia	42	44	109

2) *Number and Distribution of Wineries*

British Columbia	16 (8 large, 8 cottage)
Alberta	4 (2 large, 2 cottage)
Manitoba	2 (2 large bottling)
Ontario	20
Quebec	10 (5 large, 5 cottage)
New Brunswick	1
Nova Scotia	5 (2 large, 3 cottage)

3) *Grape Production in the Principal Producing Provinces (all varieties)*

Year	<u>Ontario</u>		<u>British Columbia</u>	
	<u>C\$1,000</u>	<u>Metric Tons</u>	<u>C\$1,000</u>	<u>Metric Tons</u>
1982	24,628	58,749	9,427	15,369
1983	32,914	71,048	8,514	12,770
1984	34,315	81,680	8,470	12,528
1985	27,359	62,901	9,042	13,735
1986	32,385	77,240	7,914	11,961
1987	n/a	70,760	10,553	13,680

Sources: Statistics Canada, Catalogue No. 22-003; British Columbia Grape Board (Mar. 1988).

for particular products than with uniform principles. Canadian provincial wine policies have been prominent in both sets of negotiations.

A. *Multilateral Negotiations*

Multilateral wine trade negotiations have been held under the auspices of the General Agreement on Tariffs and Trade [hereinafter GATT].¹² One of the fundamental principles of GATT is non-discrimination. This principle is embodied in the "most-favored-nation" rule of Article I, which obligates a Contracting Party,¹³ when granting a concession to another Contracting Party, to grant the same concession immediately and unconditionally to all other Contracting Parties.¹⁴ Another non-discrimination rule within GATT is "national treatment." Contained in Article III, the national treatment rule forbids a GATT member from applying any taxation or regulation in a way that favors domestic goods over imports.¹⁵ This rule is frequently violated in the case of high value-added commodities such as wine.¹⁶

Multilateral efforts to liberalize world agricultural trade, while relatively recent, are rapidly gaining momentum. Initial multilateral negotiations under GATT, commencing after 1947, largely ignored agricultural trade, primarily because most negotiating parties considered domestic agricultural policies sacrosanct.¹⁷ In the later negotiating rounds — Dillon (1960-61), Kennedy (1963-67), and most significantly, Tokyo (1973-79) — considerable progress was made in agricultural tariff reduction, but few non-tariff barriers were removed.¹⁸ In the current Uruguay Round of multilateral trade negotiations held by GATT, agricultural trade issues are central. As stated in the Punta del Este declaration which launched the Uruguay Round in September, 1986:

12. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. (5), (6), T.I.A.S. No. 1700, 55 U.N.T.S. 194 (1948) [hereinafter GATT]. GATT, established in 1947, is a voluntary agreement among ninety-six member countries, known as Contracting Parties, governing the conduct of international trade. In order to promote world economic development, GATT seeks to ensure equal access to markets, reciprocity in trade concessions, and transparent and stable conditions for the progressive liberalization of world trade. *Id.* Preamble and pt. IV, art. XXXVI, para. 1.

13. *See id.*

14. The "most-favored-nation" rule mandates that "any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties." *Id.* pt. I, art. I, para. 1.

15. Article III of GATT provides: "The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use." *Id.* pt. II, art. III, para. 4.

16. Morse, Mendelson, Barton & Josling, *California Agriculture Barriers to Trade: Preparation for the Uruguay Round*, 3 CAL. STATE WORLD TRADE COMM'N 19 (1987) [hereinafter Morse].

17. D.E. HATHAWAY, AGRICULTURE AND THE GATT: REWRITING THE RULES 103 (Institute for International Economics No. 20, 1987).

18. Morse, *supra* note 16, at 23.

The CONTRACTING PARTIES agree that there is an urgent need to bring more discipline and predictability to world agricultural trade by correcting and preventing restrictions and distortions including those related to structural surpluses so as to reduce the uncertainty, imbalances and instability in world agricultural markets.

Negotiations shall aim to achieve greater liberalization of trade in agriculture and bring all measures affecting import access and export competition under strengthened and more operationally effective GATT rules and disciplines¹⁹

To date, there has been no comprehensive GATT or other multilateral agreement concerning wine. In cases of alleged violations of GATT rules, any Contracting Party has the right to lodge a complaint. A specially assembled GATT panel will investigate the issues raised in the complaint and recommend a resolution to the trade dispute.²⁰ In April 1985, the EC filed a complaint with GATT contesting Canada's provincial liquor board pricing regulations, which discriminated against imports of wine and other alcoholic beverages. The EC complaint resulted in a preliminary panel report, recently adopted by the GATT council, calling for the removal of the discriminatory Canadian regulations covering beer, wine and spirits.²¹

GATT has no independent enforcement mechanism, so the decision to adopt the panel recommendations rests ultimately with the Canadian federal and provincial governments. If Canada does follow the GATT council's recommendations, the "most-favored-nation" rule will also require Canada to remove the same discriminatory restrictions from its trade with the United States and other GATT members.²² If Canada chooses not to accept these findings, then no further action can be taken within GATT. Canadian rejection of the GATT panel's findings, however, could constitute a basis for retaliatory measures by the EC against Canadian exports. Europe is a major export market for Canada. Because of the damage that such retaliatory measures could have on Canadian trade, Canada is likely to follow the recommendations of the GATT council, in whole or in part.

19. Ministerial Declaration of September 20, 1986, on the Uruguay Round, GENERAL AGREEMENT ON TARIFFS AND TRADE, BASIC INSTRUMENTS AND SELECTED DOCUMENTS 19, 24 (33d Supp. 1987) [hereinafter Ministerial Declaration].

20. In general, if a Contracting Party or the EC determines that certain Canadian trade practices constitute violations of GATT, then the injured party may seek a resolution pursuant to the dispute settlement procedures of Article XXIII of GATT, *supra* note 12, and Articles 16-18 of the Agreement on Interpretation and Application of Articles VI, XVI, and XXIII of the GATT (the so-called "Subsidies Code"), 31 U.S.T. 513, GATT, Basic Instruments and Selected Documents, Twenty-sixth Supplement 56 (1980).

21. GATT PANEL REPORT ON IMPORT, DISTRIBUTION AND SALE OF ALCOHOLIC DRINKS BY CANADIAN PROVINCIAL MARKETING AGENCIES, Doc. No. L/6304 (Feb. 5, 1988) [hereinafter GATT PANEL REPORT]; see also *Canadian Government Studying Implementation of GATT Panel Rulings on Trade Practices*, 4 INT'L TRADE REP. (BNA) 1464 (Nov. 25, 1987). The panel ruling declares the practices inconsistent with GATT.

22. See *supra* note 14 and accompanying text.

B. Bilateral Negotiations

There are several examples of bilateral negotiations in the wine sector which have been successful where multilateral efforts have failed. Perhaps the best example is the Canada-United States Free Trade Agreement [hereinafter FTA].²³ The FTA represents a comprehensive attempt to remove trade barriers and expand market access between Canada and the United States. Although agricultural issues form only a small part of the overall pact, specific provisions within the FTA cover trade in wine.

The FTA provides that, as of January 1, 1989,²⁴ listing measures and all other Canadian distribution measures must not discriminate against U.S. wines.²⁵ Canadian pricing discrimination in the form of differential markups also must be discontinued over a seven-year phase-out period commencing on the effective date of the FTA (see Table 5).²⁶ Twenty-five percent of the markup differential is to be eliminated in 1989, a further twenty-five percent in 1990, and the remaining fifty percent equally over the following five years. After that time, any remaining markup differential will be allowed only if the provincial liquor board can show an audited difference in the administrative costs of service or handling between the United States and the Canadian product.²⁷

Several exceptions have been "grandfathered" into the FTA: (i) automatic listings in British Columbia for local estate wineries that produce less than 30,000 gallons of wine annually;²⁸ (ii) measures limiting on-premise sales by Canadian wineries to wines produced on the premises;²⁹ (iii) measures in Ontario and British Columbia that require private wine stores to discriminate in favor of provincial wines;³⁰ and (iv) Quebec's rule that any wine sold in grocery stores in Quebec must be bottled in Quebec.³¹ It is too early to tell what, if any, impact these exceptions will have on the overall wine deregulation scheme embodied in the FTA.

U.S. President Ronald Reagan and Canadian Prime Minister Brian Mulroney each signed the FTA on January 2, 1988.³² In the United States, the agreement was treated as an executive agreement that could be approved through implementing legislation under the "fast-track procedure" of the

23. Free Trade Agreement, Jan. 2, 1988, Canada-United States, — U.S.T. —, T.I.A.S. No. —, reprinted in 27 I.L.M. 281 (1988) [hereinafter FTA] (entered into force Jan. 1, 1989).

24. *Id.* art. 2105.

25. *Id.* arts. 802, 804.

26. *Id.* art. 803.

27. *Id.*

28. *Id.* art. 802(2).

29. *Id.* art. 804(2)(a).

30. *Id.* art. 804(2)(b).

31. *Id.* art. 804(3).

32. *United States, Canada Sign Free Trade Agreement*, 83 DEP'T ST. BULL. 57 (Mar. 1988).

Trade and Tariff Act of 1974.³³ Such legislation was approved by the U.S. House of Representatives in August of 1988 and by the U.S. Senate in September of 1988.³⁴ The President signed the FTA on October 3, 1988.³⁵ The implementing legislation authorized the President to determine that Canada had taken appropriate steps to comply with the FTA and to exchange diplomatic notes with Canada providing for the entry into force of the FTA.³⁶

Under the Canadian Constitution, consent of the Canadian Parliament is not needed for ratification, but the Parliament does have to enact implementing legislation.³⁷ The Canadian House of Commons originally passed such legislation, Bill C-130,³⁸ on August 31, but the Liberal (opposition) majority in the Senate held up acceptance of the legislation until after national elections, held in November of 1988.³⁹ Following the Liberals' defeat in the parliamentary elections, Parliament finally approved the FTA.⁴⁰ Prime Minister Mulroney and President Reagan exchanged diplomatic notes pursuant to the FTA. The FTA entered into force on January 1, 1989.⁴¹

C. *Bilateralism and Multilateralism Compared*

The deregulation of wine trade with Canada exemplifies the interaction between bilateral and multilateral efforts at trade deregulation. The FTA represents an apparently successful attempt at bilateral policy, but comes at a time when multilateral talks in GATT are at a crucial stage. Perspectives on the relationship between bilateral agreements and multilateral trade negotiations differ between states as well as between interest groups within each state. Such differing perspectives become apparent upon examination of the views of the concerned parties — Canada, the United States, the EC, and political interest groups — toward the FTA and GATT.

From the perspective of U.S. wine producers, the FTA is widely perceived as a bilateral, preferential arrangement outside the scope of the "most-favored-nation" rule. Free trade areas, such as the one created by the FTA, are permitted under GATT Article XXIV.⁴² If the liberalizing provisions of the FTA were extended to other countries, the United States, or at least the

33. Trade Act of 1974, Pub. L. No. 93-618, § 102, 88 Stat. 1982 (1975) (codified as amended at 19 U.S.C. § 2112 (1982 & Supp. I 1983)).

34. *Senate Approves FTA Implementing Measure 83-9, Clearing Way for U.S. Ratification*, 5 INT'L TRADE REP. (BNA) 1264 (Sept. 21, 1988).

35. 24 WEEKLY COMP. PRES. DOC. 1217 (Oct. 3, 1988). The implementing legislation is Pub. L. No. 100-449, 102 Stat. 1851 (1988).

36. *See id.*; see also *infra* text accompanying note 41.

37. P. HOGG, CONSTITUTIONAL LAW OF CANADA 244 (2d ed. 1985).

38. Act to Implement the Free Trade Agreement between Canada and the United States of America, Bill C-130, ch. 65, 1989 Can. Stat. — (1989) [hereinafter FTA Implementation Act].

39. *See House of Commons Passes FTA Implementing Legislation, Clears Way for Senate Action*, 5 INT'L TRADE REP. (BNA) 1233 (Sept. 14, 1988).

40. *See supra* note 38.

41. FTA, *supra* note 23, art. 2105.

42. For an explanation of the "most-favored-nation" rule under GATT, see *supra* note 14 and accompanying text.

U.S. wine industry, could possibly recoup some of the benefits that they “traded away” in the agreement.

Even within the U.S. alcoholic beverage industry, however, no clear consensus has emerged concerning the desirability of applying the “most-favored-nation” rule to Canadian trade. In contrast to the wine sector’s interests, for example, are those of many regional beer producers in the United States who have no base of operations in Canada. These firms are presently excluded from the Canadian market and receive no benefit from the FTA. They are anxiously awaiting the application of the “most-favored-nation” principle to extend the scope of the recent GATT panel ruling⁴³ against discriminatory Canadian purchasing and pricing practices. The panel ruling covers the distilled spirits, wine, and beer sectors.⁴⁴

In Canada, a split exists between those who favor bilateral trade policies and those who are proponents of a multilateral system. This split was reflected in the political dispute over the FTA between the ruling Conservative Party and the opposition Liberal Party. The Liberal Party blocked the FTA-implementing legislation in the Senate until after last November’s Canadian federal elections.⁴⁵ The Liberals opposed the FTA and supported multilateralism, on the principle that Canadian interests would be better served in multilateral negotiations that included the United States. In contrast, the Conservative Party strongly prefers bilateral arrangements, such as the FTA, to multilateral negotiations.

The EC has generally stressed multilateralism and favors the application of the “most-favored-nation” rule, with regard to both the GATT panel ruling⁴⁶ and the FTA provisions. EC fears of bilateralism in this area reflect the concern that bilateral agreements would discriminate against European exports. The FTA wine arrangements confirm such fears. Europe’s trading partners still criticize the EC, however, for its internal price supports and its subsidies to European wine producers.⁴⁷

In response to the recent GATT panel ruling, Canada proposed phasing out its discriminatory wine trading practices.⁴⁸ The differential markups would be phased out over a twelve-year period in the grape producing provinces of Ontario, British Columbia and Nova Scotia, and over seven years in the remaining provinces. This seven-year phase-out matched that included in the FTA.⁴⁹ When the EC objected to both the timetable and the scope of the

43. GATT PANEL REPORT, *supra* note 21.

44. *Id.*

45. On the process by which Canada is to implement the FTA, see *supra* notes 37-41 and accompanying text.

46. See GATT PANEL REPORT, *supra* note 21.

47. See *infra* notes 93, 104-20 and accompanying text.

48. Notably, Canada did not propose similar changes with regard to beer.

49. FTA, *supra* note 23, art. 803.

proposal, Canada's wine industry petitioned the Canadian federal government to impose duties and quotas on subsidized EC wines under the Canadian Special Imports Measures Act.⁵⁰ The GATT dispute was resolved only when the EC threatened to impose Can. \$150 million of trade sanctions against Canadian exports. The wine producing provinces of Ontario, British Columbia and Nova Scotia offered the EC a 10% per year, ten-year phase-out of the markup differential between imported EC wines and 100% domestic content Canadian wines. The settlement does not require changes in existing beer marketing practices in Canada.⁵¹

In general terms, the various political parties and industry sectors in Canada, the United States and the EC favor bilateralism in some contexts and multilateralism in others. This inconsistency has created an interesting political dynamic, in which states pay lip service in most situations to both bilateralism and multilateralism. This political dynamic, in turn, has affected the legal framework of the negotiations to deregulate Canadian trade in wine, in particular, and international trade, in general. The next two sections examine actual bilateral and multilateral negotiating efforts to deregulate the Canadian wine trade from the perspective of the United States and the EC.

III. THE UNITED STATES PERSPECTIVE

The United States has long strived to deregulate the Canadian wine market in order to achieve greater market penetration. With the exception of Quebec, where there is an established historical and cultural preference for French wines, U.S. producers generally believe that the Canadian market is receptive to the consumption of U.S. wines. As a result, the United States has pursued its case against Canada in GATT and sought direct access to Canadian markets through the FTA. The negotiations and agreements to date hold much promise but have resulted in little progress.

A. Commercial Context

The volume of all trade between the United States and Canada is significant and continues to grow. In 1986, bilateral trade amounted to \$124 billion,⁵² the largest amount between any two countries in the world.⁵³ Of special concern to the United States, the value of U.S. imports from Canada have exceeded U.S. exports to Canada in recent years. In 1986, the U.S.

50. Act of June 28, 1984, ch. 25, 7 Can. Gaz. 739 (1984); see also *Stop Being 'Boy Scouts' to EC, Wine Industry Tells Ottawa*, *The Globe and Mail* (Toronto), Mar. 17, 1988, at 85, col. 1.

51. The terms of the GATT agreement reached by Canada and the EC are set forth in Canadian Minister for International Trade, News Release No. 254 (Dec. 20, 1988).

52. M. NORMILE & C. GOODLOE, U.S.-CANADIAN AGRICULTURAL TRADE ISSUES 9 (U.S. Dep't of Agriculture Economic Research Service, Mar. 1988) [hereinafter AGRICULTURAL TRADE ISSUES].

53. *Id.*

trade deficit with Canada totalled \$13 billion, second only to that with Japan.⁵⁴

Agricultural products account for a small proportion of overall U.S.-Canada trade (see Table 5). In the agricultural sector, however, the United States has typically had a trade surplus with Canada.⁵⁵ This surplus is particularly evident in the wine sector. Canada exports negligible quantities of its wines, mostly to the United States (3,255 hectoliters in 1987).⁵⁶ By contrast, in 1987 the United States exported 2.8% of its domestic production (449,415 hectoliters),⁵⁷ with more than 25% of that total going to Canada,⁵⁸ principally in bulk.

TABLE 5
SUMMARY OF U.S. TRADE WITH CANADA
1986
(Millions of U.S. dollars)

	<u>Total Trade</u>	<u>Agriculture</u>	<u>Wine</u>
U.S. Exports	\$55,633	\$2,591	\$7.16
U.S. Imports	\$68,123	\$2,010	\$0.66

Source: Normile & C. Goodloe, U.S.-CANADIAN AGRICULTURAL TRADE ISSUES, Table 8, at 9 (U.S. Department of Agriculture Economic Research Service, Mar. 1988); WINE INSTITUTE, ECONOMIC RESEARCH REPORT: INTERNATIONAL GRAPE AND WINE STATISTICS, Table 12, at 13 and Table 16, at 17 (Apr. 1988).

The U.S. agricultural surplus with Canada has decreased during the 1980's.⁵⁹ As overall trade flows have changed, the prevalence of trade disputes between Canada and the United States has increased, particularly in the agricultural sector where government intervention is most evident. Disputes have occurred over trade in fruit and vegetables, livestock, grain, wood products, and wine.

For U.S. wine producers, and particularly for the wine producers of California, which account for ninety percent of total U.S. wine production, the potential trade benefits of the FTA are enormous. According to the Wine Institute, the U.S. wine industry expects to increase its annual sales to Canada by \$40 to \$60 million by the end of the seven-year implementation period.⁶⁰

54. *Id.* Table 8, at 9.

55. *Id.*

56. WINE INSTITUTE INTERNATIONAL STATISTICS, *supra* note 1, Table 16, at 17.

57. *Id.* Table 12, at 13.

58. *Id.*

59. AGRICULTURAL TRADE ISSUES, *supra* note 52, at 10.

60. WINE INSTITUTE COMMENTS ON FTA, *supra* note 11

B. Legal and Policy Concerns

The United States has employed a variety of trade remedies in an effort to dismantle the discriminatory features of the provincial alcoholic beverage monopolies.⁶¹ In the 1979 Tokyo Round of GATT negotiations, for example, the United States focused on Canada's non-tariff barriers. Specifically, the unwillingness of Canadian provincial liquor boards to list U.S. wines and the different markups on domestic and imported wines frustrated the United States.⁶² In the resulting exchange of letters between the federal governments of the United States and Canada,⁶³ the United States agreed to eliminate the "wine gallon" method of tax assessment on Canadian whiskey, and Canada affirmed its intention not to increase, and to use its best efforts to reduce, the discriminatory practices of the provincial liquor boards.⁶⁴

Despite this agreement, the situation worsened. Canada, as cited in a report made pursuant to Section 854(a) of the Trade Agreements Act of 1979,⁶⁵ still maintained significant tariff and non-tariff export barriers. In 1981, several provincial liquor control boards established a special handling charge for imported wines as part of a program to assist Canadian wine producers. The United States threatened to file an action under Section 301 of the Trade and Tariff Act of 1984,⁶⁶ citing violations of the 1979 GATT commitment.⁶⁷ In response, Canada agreed to eliminate the special handling charges.⁶⁸

In 1984, Canada's provincial liquor control boards increased the markup differentials between domestic and imported wines⁶⁹ and the United States again threatened a Section 301 complaint.⁷⁰ Canada defended the markup as

61. The authors wish to thank James B. Clawson of the Clawson Co. in Potomac, Maryland, for his invaluable contribution to this section of the article. As the international trade consultant to Wine Institute since 1983, Mr. Clawson has participated directly or indirectly in virtually all of the wine trade negotiations with Canada discussed herein.

62. The chronology in this section is based on conversations with Ellen Terpstra and William Merkin of the Office of the United States Trade Representative, Washington, D.C., and James Clawson, *supra* note 61, during December 1988 and January 1989.

63. GATT PANEL REPORT, *supra* note 21, Annex I, at 51-53. The same letter was sent by the Canadian delegation to the U.S.

64. AGRICULTURAL TRADE ISSUES, *supra* note 52, Appendix Table 7, at 70.

65. Trade Agreements Act, Pub. L. No. 96-39, 93 Stat. 144 (1979) (codified as amended at 19 U.S.C. § 2501 (1988)).

66. Trade and Tariff Act of 1984, Pub. L. No. 98-573, 98 Stat. 2948 (1984) (codified as amended in scattered sections of 19 U.S.C.). Section 301(a) of the Trade and Tariff Act provides broad authority for the President to enforce U.S. rights under trade agreements and to respond to other acts, policies, or practices which are unjustifiable, unreasonable, or discriminatory and which burden or restrict U.S. commerce. If the President determines that action is appropriate, then he must take action to enforce such rights or to obtain elimination of the act, policy or practice, and may (1) suspend, withdraw, or prevent application of trade agreement benefits and (2) impose duties or other import restrictions. 19 U.S.C. § 2411(a) (1987).

67. AGRICULTURAL TRADE ISSUES, *supra* note 52, Appendix Table 7, at 70.

68. *Id.*

69. *Id.*

70. *Id.*

reflecting the differential distribution costs between domestic and imported wines.⁷¹

These barriers against imports are especially significant in light of the fact that Canada was designated under the Wine Equity and Export Expansion Act [hereinafter Wine Equity Act]⁷² as a potential significant market for U.S. wine exports that maintains tariff or non-tariff barriers to trade in wine.⁷³ Progress toward free trade seemed to be made in 1984 when the industries of both countries negotiated the Niagara Accord,⁷⁴ in which the Ontario wine and grape industries agreed, *inter alia*, to "adopt measures to permit more general listings for U.S. wines."⁷⁵ The province of Ontario, however, failed to implement the Niagara Accord.

Primarily in response to longstanding U.S. wine industry complaints, Canada agreed in principle to the bilateral talks mandated by the Wine Equity Act⁷⁶ in order to provide fairer treatment of U.S. wines in Canada. These negotiations, which led ultimately to the FTA, benefit both Canada and the United States. From the Canadian perspective, the various free trade negotiations and the FTA offer a way to secure access to the U.S. market for merchandise trade generally (agricultural and non-agricultural). To U.S. wine producers, the FTA creates an opportunity for significantly increasing exports to Canada. In anticipation of FTA ratification and as a result of increased U.S. promotional activities in Canada, U.S. listings increased dramatically in 1987 over 1986: 26% in British Columbia, 19% in Alberta, 57% in Ontario, and 150% in Quebec.⁷⁷ Nevertheless, it remains to be seen whether there will be real wine trade liberalization in Canada under either the FTA or GATT.

IV. THE EUROPEAN PERSPECTIVE

Three factors determine the EC perspective toward the deregulation of the Canadian wine sector. First, the EC holds the dominant position in world

71. *Id.*

72. Wine Equity and Export Expansion Act (Title IX of the Trade and Tariff Act of 1984, *supra* note 66), Pub. L. No. 98-573, 98 Stat. 3047-3050 (codified as amended at 19 U.S.C. §§ 2801-2806 (1987)) [hereinafter Wine Equity Act]. The purposes of the legislation were to expand wine consumer choice, to encourage wine export promotion, and to achieve greater foreign market access for U.S. wine. The legislation called on the U.S. Trade Representative to designate major wine trading countries which are significant potential markets for U.S. wine and which maintain tariff and nontariff barriers to U.S. wine trade. The Trade Representative then must consult with each country to seek a reduction or an elimination of its barriers or other distortion of trade in U.S. wine.

73. *See id.*; *see also* NATIONAL TRADE ESTIMATE, *supra* note 10.

74. AGREED MINUTES, NIAGARA-ON-THE-LAKE (July 23, 1984).

75. *Id.* at 2, item 6.

76. 19 U.S.C. § 2804(a).

77. J. Clawson, International Trade Barriers/Certification Procedures, part II (Mar. 1988) (available from the Wine Institute, San Francisco, Cal.).

wine production and trade.⁷⁸ As such, the EC has an interest in the expansion of wine consumption in industrial countries through the deregulation of tightly controlled overseas markets. Second, the EC has chronic surplus problems in its own internal market.⁷⁹ These problems make the EC particularly sensitive to any exacerbating trade developments that might influence its ability to organize its own domestic market.⁸⁰ Third, Canadian wine trade deregulation is related to the wider GATT regime of world trade in ways that will be discussed below.

A. Commercial Context

The countries of the EC dominate world wine production. In 1986, about 199 million hectoliters of wine were produced in the EC, out of a global total of 330 million hectoliters.⁸¹ France and Italy each produced about 70 million hectoliters, followed by Spain (34.5 million hectoliters) and Germany (almost 10 million hectoliters).⁸² Outside of the EC, only Argentina (23 million hectoliters), the Union of Soviet Socialist Republics (25 million hectoliters), and the United States (20 million hectoliters) produced comparable amounts of wine.⁸³ About sixteen percent of world wine production is traded internationally, and the EC accounts for about two-thirds of this trade.⁸⁴ Much of the trade is among EC members, but in 1986 the EC earned \$4.74 billion from sales to non-member countries.⁸⁵ Canada is the third-largest overseas market for EC wine, importing 1.14 million hectoliters in the marketing year 1985-86⁸⁶ from the Community of Ten.⁸⁷ Only the United States

78. WINE INSTITUTE INTERNATIONAL STATISTICS, *supra* note 1 and accompanying text, and *infra* note 81 and accompanying text.

79. See *infra* notes 104-20 for a detailed explanation of European wine surpluses and related policy concerns.

80. For a detailed discussion of the interplay between international wine trade deregulation, trade policy, and the EC's internal agricultural policy, see *infra* pt. IV.B.1.

81. The trade statistics in this section are derived from the COMMISSION OF THE EUROPEAN COMMUNITIES, THE AGRICULTURAL SITUATION IN THE COMMUNITY: 1987 REPORT (1988) [hereinafter 1987 REPORT].

82. *Id.* Table 218.

83. European Community, *Wine in the European Community* (European Documentation Periodical No. 1/1988) 13 (1988) [hereinafter European Documentation].

84. 1987 REPORT, *supra* note 81, Table 219.

85. WESTERN EUROPE AGRICULTURE AND TRADE REPORT, Appendix Table 5, at 78 (U.S. Dep't of Agriculture Economic Research Service, June 1988).

86. European Documentation, *supra* note 83, at 35.

87. Prior to January 1, 1986, the EC consisted of only ten Member States. On that date, Spain and Portugal were admitted to the EC, increasing its size to twelve states. The terms of admission of these two countries are contained in the treaty between the ten existing Member States of the EC, Spain, and Portugal concerning the accession of the two new members to the European Economic Community, to the European Coal and Steel Community, and to the European Atomic Energy Community. See generally *Act Concerning the Conditions of Accession of the Kingdom of Spain and the Portuguese Republic to the European Community*, 28 O.J. EUR. COMM. (No. L 302) 23 (1985). Although Spain and Portugal have been full members since January 1986, various transitional arrangements have been made with respect to the harmonization of agricultural policies and prices. In the case of Portugal, a two-stage transition has been adopted, with the initial five year stage giving Portugal time to reorganize its wine sector and the

(3.8 million hectoliters) and Switzerland (1.16 million hectoliters) were larger consumers of wine exported from the EC.⁸⁸

The gap is narrowing between those countries that have traditionally produced and consumed most of the world's wine and those that until recently had smaller wine markets. In particular, consumption of wine in industrialized countries has shown two distinct trends in recent years. In the traditional wine growing countries of southern Europe and South America, per capita consumption has been decreasing over the past twenty years.⁸⁹ By contrast, consumption has climbed steadily in North America and in the non-traditional wine countries of northern Europe.⁹⁰

This narrowing gap has major implications for international trade. Despite increased production from newly-established wine sectors in the United States, Canada, and northern Europe, especially the United Kingdom, increased consumption in these sectors has led to greater importation from southern Europe. At the same time, demand for wine is weakening in these traditional, southern European producer nations, in particular France and Italy. This trend could continue for some time — per capita consumption in France and Italy is just over 75 liters per year, compared to slightly more than 9 liters in the United States and 7.5 liters in Canada.⁹¹

Much of the bottled wine exported from the EC is of recognized quality, produced in specific regions.⁹² In marketing such wine, exporters rely on consumers' familiarity with and loyalty to brand names and regional appellations. Marketers of European wine also use price as a tool when competing with wines from other areas.

Like U.S. wine producers, Europeans complain that the Canadian provincial liquor control boards have made it difficult to develop markets for imported wines. The listing process limits the variety and the information available to the consumer and hinders the development of name recognition and brand loyalty. By restricting competition, discrimination in favor of local wines limits consumer choice and slows down the development of the Canadian industry itself by protecting it from competition.

second five-year stage representing a harmonization of price levels. For Spain, a one-stage transition was chosen, with an eight-year phase-out of customs duties on wine between the EC and Spain and a seven-year harmonization of wine support prices.

88. 1987 REPORT, *supra* note 81.

89. European Documentation, *supra* note 83, at 20.

90. *Id.*

91. FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS, WINE MARKET SITUATION 1987/88 AND PROSPECTS 1988/89, Table 5, at 7 (1988).

92. Such wine is known in EC terminology as "quality psr." Quality psr wines are those meeting the requirements of Regulation No. 823/87, produced "in an area or set of wine-growing areas the name of which is used to designate them and which have special quality characteristics." European Documentation, *supra* note 83, at 109. These wines include the French AOC and VDQS labels, German Qualittswein, Italian DOC and DOCG wines and Spanish DO and DOC designations, together with comparable qualities in Greece, Luxembourg, and Portugal.

B. Legal and Policy Concerns

1. The EC Internal Market

The Canadian wine regulations are of particular concern to the EC Commission [hereinafter the Commission] and to the Council of Ministers because of their implications for the balance of Europe's internal wine market. In general, issues become important to EC institutions when they impinge on internal decision-making or on common financing. Over the past twenty years, generous price supports under the EC's Common Agricultural Policy [hereinafter CAP]⁹³ have created a large wine surplus.⁹⁴ Consequently, Europeans welcome the deregulation of the Canadian wine market as a relief to the problems created by their internal wine surplus.

Wine surpluses in the EC reflect both changing consumption patterns among the Member States⁹⁵ and agricultural price support and regional development policies under the CAP. With regard to consumption patterns, per capita wine consumption has been falling in the Mediterranean regions of the EC.⁹⁶ Increased demand in the northern Member States⁹⁷ has not prevented a chronic surplus from developing in the EC, a situation that threatens to worsen now that Spain and Portugal have acceded to the EC.⁹⁸

EC wine surpluses are also a symptom of generous price policies coupled with direct market intervention. Because the CAP mandates intervention in the wine sector,⁹⁹ adverse market developments create policy problems. When the CAP was established in the 1960's, a balanced wine market was not seen as a problem,¹⁰⁰ because the EC market needed imports from North Africa and Spain¹⁰¹ to meet domestic demand.¹⁰² In the wine sector the

93. The CAP is authorized under the Treaty of Rome, *supra* note 3, Article 39. The CAP consumes approximately two-thirds of the EC's annual budget. *Budget No. 1 of the European Communities for the Financial Year 1988* (Final Adoption of the European Parliament 88/494) 31 O.J. EUR. COMM. (No. L 265) 16 (1988); *see also* Commission of the European Communities, EAGGF: THE EUROPEAN COMMUNITY'S EXPENDITURE ON THE COMMON AGRICULTURAL POLICY (GREEN EUROPE NO. 42) at 4 (1988) [hereinafter GREEN EUROPE NO. 42].

94. *See infra* notes 104-20 and accompanying text for a detailed explanation of the European wine surplus and related policy concerns.

95. For a list of the Member States, *see supra* note 3.

96. *See* European Documentation, *supra* note 83.

97. *Id.*

98. *See infra* note 115 and accompanying text.

99. The EC wine policy is incorporated in *Council Regulation No. 822/87 of Mar. 16, 1987 on the Common Organization of the Market in Wine*, 30 O.J. EUR. COMM. (No. L 84) 1 (1987) and *Council Regulation No. 823/87 of Mar. 16, 1987 on Special Provisions Relating to Quality Wines Produced in Specified Regions*, 30 O.J. EUR. COMM. (No. L 84) 59 (1987). These regulations consolidate the considerable number of changes which *have* occurred since the wine regime entered into force in 1970.

100. Throughout the 1960's, tightly regulated French production contrasted with the more loosely organized Italian wine sector, each aimed mostly at domestic consumption. The small German wine industry produced its own style of high-quality wines, leading to some problems of product-definition but causing no threat to the overall balance of the European wine market. *See* European Documentation, *supra* note 83, at 44.

101. At the time, Spain was not yet a member of the EC. *See supra* note 87.

102. European Documentation, *supra* note 83, at 50.

Commission was primarily concerned with the harmonization of national regulations and the liberalization of internal EC trade.¹⁰³

By 1970, economic imbalances arose in the European wine market due to regulations that liberalized intra-Community trade.¹⁰⁴ France imported large quantities of Italian wine, which displaced not only North African imports¹⁰⁵ but also many local French wines. The wines flowing in from Italy were not quality wine produced in specific regions,¹⁰⁶ pursuant to the EC's common wine regulations,¹⁰⁷ but rather table wine.¹⁰⁸

Political problems ensued, and the so-called "wine lake" — much of it low-quality wine from France and Italy — became a problem for the CAP.¹⁰⁹ Expenditures on wine price supports have averaged over \$1 billion for the past five years,¹¹⁰ accounting for approximately five percent of the EC's total annual guarantee expenditure on agricultural surpluses.¹¹¹ Distillation, originally conceived as an emergency device for occasional surplus years,¹¹² became by the mid-1970's a regular means of disposal.¹¹³ The wine surplus flooded the market for industrial alcohol, an expense borne by the EC.

The CAP already induces the removal, through distillation, of up to twenty percent of EC wine production.¹¹⁴ Therefore, the Spanish accession to the EC is likely to have a substantial exacerbating impact.¹¹⁵ Spain cultivates about 1.6 million hectares of vineyards, compared to about 1.0 million hectares in France.¹¹⁶ Spanish vineyards, however, yield only one-third as much as French vineyards.¹¹⁷ These lower yields stem, in part, from a ban

103. The common wine regulations, *see supra* note 99, passed in 1970, provide measures to support prices through distillation and storage and rules on the planting of specific grape varieties.

104. European Documentation, *supra* note 83, at 57.

105. *Id.*

106. *See supra* notes 92 and 99.

107. *See supra* notes 99 and 103.

108. In theory, the market for table wines is separate from that for quality wines. The EC wine regulations assume such a distinction. In practice, however, the two markets are linked in a variety of ways. At the production level, there has been an expansion of vineyards in areas that produce quality wines and an abandonment of vineyards devoted to table wine. At the level of winery production, EC winemakers can switch between labelled bottles with wine from specific regions and blended (generic) wines or bulk wine bottled in another location. Strong demand for quality wines relieves pressure on the table wine market. Restrictive marketing practices on quality wines exacerbate the problem of surplus disposal for table wines.

109. For an account of the political aspects of the wine issue, see E. NEVILLE-ROLFE, *THE POLITICS OF AGRICULTURE IN THE EUROPEAN COMMUNITY* 511-15 (1984).

110. GREEN EUROPE NO. 42, *supra* note 93, at 6.

111. *Id.*; *see also* E. NEVILLE-ROLFE, *supra* note 109, at 511.

112. *See, e.g., supra* note 103.

113. *See* European Documentation, *supra* note 83, at 52.

114. *Id.*

115. On Spain's accession to the EC, *see supra* note 87; on Spanish wine production, *see supra* note 82 and accompanying text; on Spanish and Portuguese wine exports to Canada, *see* Table 1, *supra* in the text.

116. *See* European Documentation, *supra* note 83, at 24. One hectare equals 2.471 acres.

117. In 1984-85, for example, vineyards in Spain yielded on average 23.3 hectoliters per hectare. In France, the average vineyard yielded 61.5 hectoliters per hectare. COMMISSION OF

on vineyard irrigation¹¹⁸ and lower price support levels in Spain.¹¹⁹ Spanish prices will rise by at least fifty percent in the period up to 1992, when the EC wine regime will fully apply in Spain.¹²⁰ Even a modest yield increase would swamp the EC's internal market and escalate the cost of the CAP, further straining the EC's budget.

In these circumstances, opening up the Canadian market would clearly offer an attractive channel for the movement of more European wine into world trade. A consistent desire of the European Commission is to expand export markets for wine and hence alleviate domestic surpluses.¹²¹ If Canada can be persuaded to liberalize imports, then the benefits would be felt in lower costs for domestic intervention and distillation in the EC. U.S. preferences in the Canadian market, however, could further exacerbate the EC's situation and lead to higher budget costs.

2. *Europe's View on the FTA and GATT*

Policy changes by Canada or by EC Member States in response to adverse GATT panel rulings would indicate a new and more receptive attitude toward multilateral enforcement of GATT principles in international agricultural trade disputes. The EC traditionally has regarded GATT rather than bilateral negotiations as the proper forum in which to harmonize international trade policies and resolve trade disputes. In the past, GATT panels of inquiry frequently have ruled against the EC, which has generally defended its internal agricultural marketing policies as sovereign and legally justifiable. Interestingly, the Canadian wine case, in which the EC was the complainant, has been widely regarded as a test of whether countries that have argued in the past for the use of the GATT process to regulate the "internal" policies of others are prepared to abide by such a rule when regulating their own internal markets.

3. *Significance of the EC's Perspective*

In summary, from the EC's vantage, expansion of wine consumption in northern Europe and in North America is essential in order to compensate

THE EUROPEAN COMMUNITIES, THE AGRICULTURAL SITUATION IN THE COMMUNITY: 1986 REPORT 398, Table 4.6.1.1 (1987).

118. Morse, *supra* note 16, at 126-28.

119. *Id.*

120. See generally Final Act of the Conference of Representatives of the European Communities' Member States with Treaty Modifications Concerning Community Institutions, Monetary Cooperation, Research and Technology, Environmental Protection, Social Policy, and Foreign Policy Coordination, Feb. 17 and 28, 1986, 30 O.J. EUR. COMM. (No. L 169) 1 (1987), reprinted in 25 I.L.M. 506 (1986) (commonly known as the Single European Act); see also Treaty of Rome, *supra* note 3, art. 40.

121. European Commission, PERSPECTIVES FOR THE COMMON AGRICULTURAL POLICY (GREEN EUROPE No. 33) at 44 (1985) (commonly known as THE GREEN PAPER).

for the declining domestic consumption in France, Italy, and other Mediterranean countries. The Europeans believe that their quality wines can compete in the Canadian market on the strength of name-recognition and reputation; table wines are likely to compete by price. In each case, additional foreign wine sales would ease the problems caused by attempts to restructure the European market under the CAP and reduce the burden these economic policies impose on the EC's budget.

The failure to deregulate the Canadian wine market could hinder efforts to liberalize world trade. If the Canadian market remains regulated in a discriminatory fashion despite the bilateral agreement or the findings of the GATT panel, then EC confidence in the multilateral trading system would erode. With considerable pressure to turn inward for the deregulation of the internal European market by the end of 1992,¹²² the EC's negative reaction to continued Canadian discriminatory trade practices would adversely affect progress in the GATT Uruguay Round and the GATT process in general.

V.

THE INTERNAL DIVISION OF CANADIAN AUTHORITY OVER TRADE

Among the issues outside the wine sector raised by the Canadian wine deregulation dispute is the relationship between national and subnational levels of authority in matters of trade policy. The success or failure of either bilateral or multilateral attempts to deregulate the Canadian wine market depends on Canada's implementation of legislation at the national and provincial levels. The interplay between national and provincial control over wine marketing highlights an issue that extends both to other agricultural crops and to nonagricultural sectors, such as energy and services. The Canadian arrangement and its consequences are discussed here, but the issue arises in other countries with federal systems.

A. The Status of International Agreements: The United States and Canada Compared

In Canada, as in the United States, the enforcement of the FTA or GATT depends on federal authority to bind the action and policies of states or provinces.¹²³ The legal effectiveness of the FTA is particularly limited by the extent to which the states of the United States and the provinces of Canada can be bound. The drafters of the FTA, aware of this problem, sought to reach provincial and state governments by way of the federal government in each country. Article 103 of the FTA states:

The Parties to this Agreement shall ensure that all necessary measures are taken in order to give effect to its provisions, including their observance, except

122. *Id.*

123. 5 INT'L TRADE REP. (BNA) 803 (June 1, 1988).

as otherwise provided in this Agreement, by state, provincial and local governments.

The relationship that the national government, as the signatory of the FTA, bears to state or provincial governments presents a greater legal obstacle to implementation of the FTA in Canada than in the United States.

1. U.S. Implementation of the FTA

The U.S. implementing legislation assumes that there is no constitutional impediment to state compliance with the terms of the FTA. Thus, it simply states:

- (1) The provisions of the Agreement prevail over —
 - (A) any conflicting State law; and
 - (B) any conflicting application of any State law to any person or circumstance . . . to the extent of the conflict.
- (3) The United States may bring an action challenging any provision of State law, or the application thereof to any person or circumstance, on the ground that the provision or application is inconsistent with the Agreement.¹²⁴

The validity of federal assumption of authority is beyond doubt under the doctrine of *Missouri v. Holland*,¹²⁵ which held that the federal government could validly execute a treaty and enact enforceable implementing legislation even in areas that had been constitutionally reserved to the states.¹²⁶

The House Ways and Means Committee also has dealt with the special federalism questions posed in the alcoholic beverages area:

Pursuant to the 21st Amendment to the Constitution, which repealed the 18th Amendment's prohibition on alcoholic beverages, the regulation and control of the sale and distribution of alcoholic beverages was explicitly left to the States. The Constitution does not permit, however, any State to discriminate in their regulation of alcoholic beverages between the products produced within the State and those produced in other States or countries.¹²⁷

Thus, while the states have the inherent power to regulate wine, Congress retains its authority in interstate and international commerce.¹²⁸

124. Free Trade Agreement Implementation Act, United States-Canada, Pub. L. No. 100-449, 102 Stat. 1851, § 102(b) (1988). The omitted subsection (2) creates a procedure for consultations with state governments.

125. *Missouri v. Holland*, 252 U.S. 416 (1920).

126. *Missouri v. Holland* dealt with the protection of migratory birds, an area that, at least in the absence of a treaty, was reserved to the states under contemporary interpretations of the interstate commerce clause. It is clear, however, that the constitutional provisions protecting civil rights cannot, unlike those affecting federalism, be modified by international treaty. *Reid v. Covert*, 354 U.S. 1 (1957).

127. House Ways and Means Committee Print (100-31), "Background Information and Summary of United States-Canada Free Trade Agreement and Implementing Legislation," released May 20, 1988, 5 INT'L TRADE REP. (BNA) 809 (June 1, 1988).

128. J. Manfreda & R. Mendelson, *Le droit du vin dans la législation américaine*, 61 BULLETIN DE L'O.I.V. 351 (1988).

2. Canadian Implementation of the FTA

Canadian federal supremacy over trade policy is more complex and involves difficult constitutional questions that are as yet unsettled.¹²⁹

In Canada, treaties are never self-executing and therefore require an implementing statute.¹³⁰ The Canadian statute implementing the FTA grants provincial governments an opportunity to comply voluntarily with the terms of the FTA but gives the Governor in Council¹³¹ the authority to override any inconsistent provincial legislation:

[W]here the Governor in Council is of the opinion that, for the purposes of giving effect in a province to Chapter Eight of the Agreement [the Chapter governing wine issues], regulations are necessary in relation to any matter dealt with by that Chapter, [he or she may] make regulations for that purpose¹³²

In addition, Section 6 of the implementing statute states:

for greater certainty, nothing in the act, explicitly or by omission, limits in any manner the right of Parliament to enact legislation implementing any provision of the agreement or fulfilling any of the obligations of the government of Canada under the agreement.¹³³

The difficulty is that, according to *Att'y Gen. (Canada) v. Att'y Gen. (Ontario) (Labour Conventions)*,¹³⁴ the Canadian federal government lacks inherent authority to implement treaty provisions.¹³⁵ Unless this case law is modified, which is quite possible,¹³⁶ the FTA can be enforced against the provinces only under the normal federal allocation of authority.

The Canadian allocation of authority over matters of trade is spelled out in Sections 91 and 92 of the Constitution Act, 1867.¹³⁷ Section 91 grants

129. One Ontario individual is reported to have said of U.S. wine, "They can make us bring it in, but they can't force us to put it on the shelves." BILATERALISM, MULTILATERALISM AND CANADA IN U.S. TRADE POLICY 139 (W. Diebold ed. 1988).

130. See P. HOGG, *supra* note 37, at 245.

131. The Governor in Council is the Governor General (the representative of the Queen) acting on the basis of an "order" or "minute" of the cabinet. *Id.* at 147.

132. FTA Implementation Act, *supra* note 38, s. 9.

133. *Id.* s. 6.

134. *Att'y Gen. (Canada) v. Att'y Gen. (Ontario) (Labour Conventions)*, [1937] A.C. 326.

135. [1937] A.C. 326. In *Labour Conventions*, the Privy Council (in London) refused to apply a *Missouri v. Holland* doctrine and interpreted the Canadian Constitution Act, 1867 ((U.K.), 30-31 Vict., c. 3 (formerly British North America Act, 1867 (U.K.) and renamed by Constitution Act, 1982 (Schedule B to Canada Act, 1982 (U.K.), c. 11)) [hereinafter Constitution Act, 1867]) as limiting the federal treaty power. *Labour Conventions* was on appeal from an equally divided decision of the Supreme Court of Canada. The Privy Council feared that a treaty-implementing power could be used to upset the carefully negotiated allocation of powers under which the provinces entered the Confederation. [1937] A.C. at 335-52. Under the Constitution Act, 1867, *supra* note 135, s. 132, there is an exception with respect to certain Commonwealth obligations for which the national government does have "all powers necessary or proper for performing the obligations of Canada."

136. The Canadian Supreme Court (from which appeal no longer lies to the Privy Council) has several times indicated that it may reconsider *Labour Conventions*, which is under attack by a number of commentators. See Sullivan, *Jurisdiction to Negotiate and Implement Free-Trade Agreements in Canada: Calling the Provincial Bluff*, 24 U.W.O.L. REV. 63 (1987).

137. Constitution Act, 1867, *supra* note 135.

exclusive legislative authority for the regulation of trade and commerce to the Canadian Parliament.¹³⁸ Section 92 allows the legislature of each province to make laws in relation to "Property and Civil Rights in the Province. . . ."¹³⁹ In addition, with regard to agriculture, Section 95 of the Constitution Act adds:

In each Province the Legislature may make Laws in relation to Agriculture in the Province . . . and it is hereby declared that the Parliament of Canada may from Time to Time make laws in relation to Agriculture in all or any of the Provinces . . . and any law of the Legislature of a Province relative to agriculture . . . shall have effect in and for the Province as long and as far only as it is not repugnant to any Act of the Parliament of Canada.¹⁴⁰

Thus, unlike in the United States, in Canada there is no clear supremacy of federal commercial law over provincial laws regulating commerce. Canadian laws regarding agriculture, however, do take precedence over contrary provincial laws.

In the 1881 case *Citizens' Insurance Co. v. Parsons*,¹⁴¹ the Privy Council laid out a framework for analyzing the relationship between Sections 91 and 92. This framework, which has been followed ever since, identified two categories of trade and commerce over which the federal government has regulatory authority: (1) interprovincial or international trade and commerce;¹⁴² and (2) the "general regulation of trade affecting the whole dominion."¹⁴³ Neither of these categories includes local trade or commerce. In addition, in *Parsons* the Privy Council said that the "authority to legislate for the regulation of trade and commerce does not comprehend the power to regulate by legislation the contracts of a particular business or trade."¹⁴⁴

Although it is possible that the FTA implementing legislation can be supported as a matter of interprovincial or international trade (the first prong of *Parsons*), the issue remains a difficult one. Even recent decisions give no clear answer. In *Dominion Stores Ltd. v. Regina*¹⁴⁵ the Canadian Supreme Court summarized the earlier precedents, saying:

[T]he power of Parliament with reference to the regulation of trade and commerce is limited to trade in the international and interprovincial sense and Parliament is not empowered thereby to regulate a local trade simply as a part of a scheme for the regulation of international and interprovincial trade.¹⁴⁶

138. *Id.* s. 91.

139. *Id.* s. 92.

140. *Id.* s. 95.

141. *Citizens' Insurance Co. v. Parsons*, [1881] A.C. 96.

142. *Id.* at 113.

143. *Id.*

144. *Id.*

145. *Dominion Stores v. Regina*, [1980] 1 S.C.R. 844, at 853-67 (as reported, second opinion is majority).

146. *Id.* at 853.

The Court went on to strike down a national statute providing for grade names for apples. The national law made the use of these grade names voluntary but also made it unlawful to label products inconsistently with the national grade names. A parallel provincial statute required that the same grade names be used. Although this clearly was a cooperative system, the national statute was regarded as infringing on "the provincial power to regulate local trade."¹⁴⁷ The controversial issue is whether the wine regulatory changes required by the FTA also infringe on this provincial power.

Under the second prong of *Parsons*, which concerns the general regulation of trade affecting the whole dominion, the picture is even less clear. Two 1980 Supreme Court cases on point strongly imply that the second prong of *Parsons* will be insufficient to support federal legislation enforcing the wine provisions of the FTA. *Dominion Stores*, which did not explicitly state to which prong of *Parsons* it applied, struck down an apple regulatory system, which could easily be viewed as a form of "general regulation of trade."¹⁴⁸

In addition, the Canadian Supreme Court in *Labatt Breweries of Canada v. Att'y Gen. (Canada) et al.*¹⁴⁹ struck down a federal compositional requirement for beer. The *Labatt Breweries* court rejected the compositional requirement as not "a matter of national concern transcending the local authorities' power to meet and solve it by legislation."¹⁵⁰ *Labatt Breweries* concerned the second prong of *Parsons*. Under the approach taken in *Labatt Breweries*, it could be very difficult for the national government to implement the FTA's wine provisions.

Nevertheless, the issue has been taken up more recently in a 1983 Canadian Supreme Court decision, *Att'y Gen. (Canada) v. Canadian National Transportation*,¹⁵¹ that has been interpreted as granting the federal government greater authority in the provincial trade area.¹⁵² In *Canadian National Transportation* the Supreme Court upheld a federal criminal prosecution under the Combines Investigation Act.¹⁵³ The dispute arose from the fact that the Constitution Act, 1867,¹⁵⁴ assigned the "Administration of Justice in the Province," to the provincial attorneys general.¹⁵⁵ The majority opinion decided the case on the grounds that the provision did not confer exclusive jurisdiction on the provincial prosecutor and that there was room for parallel national prosecution. In an important concurring opinion joined by two other justices, however, Justice Dickson affirmed the national prosecutor's

147. *Id.* at 863.

148. *Parsons*, *supra* note 141, at 113.

149. *Labatt Breweries of Canada v. Att'y Gen. (Canada) et al.*, [1980] 1 S.C.R. 914.

150. *Id.* at 945.

151. *Att'y Gen. (Canada) v. Canadian National Transportation, Ltd.*, [1983] 2 S.C.R. 206.

152. Note, *Constitutional Law — Section 91(2) of the Constitution Act, 1867 — Competition Legislation*, 62 CAN. BAR REV. 182 (1984) [hereinafter Note].

153. *Combines Investigation Act*, CAN. REV. STAT. ch. C-23 (1970).

154. *Constitution Act, 1867*, *supra* note 135.

155. *Id.* s. 92(14).

authority on the grounds that the antitrust issue was one of national authority under the national-provincial allocation of powers over commerce.¹⁵⁶

This concurrence referred to the following factors as justifying a valid exercise of the general trade and commerce power (the second prong of *Parsons*):

- (1) the presence of a national regulatory scheme;
- (2) the oversight of regulatory agency;
- (3) a concern with trade in general rather than an aspect of a particular business;
- (4) a constitutional incapability of the provinces, either jointly or severally, to pass a particular enactment;
- (5) a situation where failure to include one or more provinces or localities would jeopardize the successful operation of the entire scheme.¹⁵⁷

Except for the distinction between concern with trade in general and an aspect of a particular business, it is very likely that the FTA's wine provisions could be upheld under this standard.

In *R. v. His Honour Judge Wetmore (Kripps Pharmacy)*,¹⁵⁸ announced the same day as *Canadian National Transportation*, the Supreme Court upheld a federal prosecution under a Canadian statute prohibiting the sale of drugs manufactured under unsanitary conditions. In this case, Justice Dickson dissented, specifically rejecting a "trade and commerce" basis for the regulation. He relied on *Parsons*, recognizing that "trade and commerce does not include the regulation of a single trade or business."¹⁵⁹ Justice Dickson stated that his opinion was not, however, based solely on the factors set forth in *Canadian National Transportation*. The Justice declared:

The above does not purport to be an exhaustive list, nor is the presence of any or all of the these *indicia* necessarily decisive. The proper approach to the characterization is still the one suggested in *Parsons*, a careful case by case assessment. Nevertheless the presence of such factors does at least make it far more probable that what is being addressed in a federal enactment is genuinely a national economic concern and not just a collection of local ones.¹⁶⁰

He also determined:

. . . the limits of s. 91(2) are not fixed, and . . . questions of constitutional balance play a crucial role in determining its extent in any given case at any given time.¹⁶¹

Even under the new interpretation, it is possible that the federal wine laws mandating provincial regulation might be struck down as "the regulation of a single trade or business." Nevertheless, it is difficult to agree with *Parsons'* rejection of the regulation of a single trade or industry, particularly when that trade or industry is of international concern. Additionally, given the level of international interest in the wine trade, the FTA implementing act

156. [1983] 2 S.C.R. at 245-82.

157. Note, *supra* note 152, at 190-91.

158. *R. v. His Honour Judge Wetmore (Kripps Pharmacy)*, [1983] 2 S.C.R. 284.

159. *Id.* at 294.

160. *Id.* at 268.

161. *Id.* at 259.

would appear to be “genuinely a national economic concern and not just a collection of local ones.”

Most importantly, the evolution of the *Parsons* doctrine and the possible modification of *Labour Conventions* both imply that federal trade regulation under the FTA is constitutionally permissible. Indeed, emphasizing the philosophical differences between the London Privy Council of the past and today’s Canadian Supreme Court, one commentator noted that “the Supreme Court of Canada has the tools it needs to uphold a strong federal initiative in the area within the existing framework of Canadian constitutional law.”¹⁶² Should the issue arise, the Canadian Supreme Court has the opportunity to concentrate national authority over trade policy in the federal government. Such a constitutional ruling would signify a trend toward stronger federal enforcement of uniform provincial laws affecting external trade.

CONCLUSION: IMPLICATIONS FOR THE INTERNATIONAL TRADING SYSTEM

The post-war economic system, based on the steady liberalization of trade and capital movements under GATT, has withstood the challenges of inflation, recession, and currency crises. Continual effort is needed to preserve the gains made over the past forty years; this need is the impetus for the Uruguay Round. The attempt to bring domestic agricultural policies within the regime of international trade is part of this effort, as is the inclusion of services in the trade talks for the first time.¹⁶³ If the effort fails, countries will look for other ways of conducting trade policy, most probably through bilateral negotiations or even retaliatory trade restrictions.

Admittedly, the wine market in Canada is not likely to be a major topic of interest in the Uruguay Round. In itself, the Canadian wine issue is a minor irritation in trade relations, but it illustrates well the issues that arise in other areas. The issues of federal and provincial authority over trade and of overlapping multilateral and bilateral negotiations are seen as two aspects of a broader issue — the future development of the international trading system.

Of increasing importance is the question of whether nations, at the international level, can effectively negotiate policies that are decided and administered at the subnational level. In the case of the EC, the question is even more complex. The institutions of the EC, namely the Commission and the Council of Ministers, have the exclusive prerogative to negotiate and enter into trade agreements on behalf of the Community.¹⁶⁴ The EC negotiates in GATT on behalf of its constituent Member States. Though the Member States are each Contracting Parties to GATT, they are bound by EC trade

162. Sullivan, *supra* note 136, at 82. See also Note, *supra* note 152; Fairley, *Developments in Constitutional Law: The 1983-84 Term*, 7 SUP. CT. L. REV. 98 (1985); but see Lyman, *The Canadian Approach to Regulating Agricultural Commodities in International Trade*, 14 CAPITAL U.L. REV. 559 (1985).

163. See *supra* notes 17-19 and accompanying text.

164. Treaty of Rome, *supra* note 3, art. 113.

agreements. Agricultural trade agreements may involve both CAP and individual national agricultural policies that fall outside the competence of the EC. Hence, other countries must negotiate with the EC as a whole for matters covered by the CAP and with each country separately for specific national measures.

An international agreement that limits domestic farm price support levels, currently under discussion in GATT,¹⁶⁵ would heighten the importance of this question. Canada already administers farm price supports at the provincial level, where local policies supplement federal policy. If the related issues of international negotiating authority in trade matters and the implementation of international trade agreements are not settled, the problem could become much more significant in the future.

The issue of bilateralism is equally crucial to the trading system. The FTA in general represents a movement away from the multilateral trade arrangements embodied in GATT. Even after the EC-Canada GATT compromise, the FTA has retained some degree of discrimination in favor of U.S. wines entering Canada, at the expense of those from the EC. Such bilateral preferences run counter to the spirit, if not the letter, of GATT. Exclusionary bilateral arrangements, whether between sovereign nations or trading blocs, could significantly undermine multilateral efforts to liberalize world trade.

Two issues, therefore, will shape the deregulation of the Canadian wine market: (1) the trend toward bilateralism; and (2) the debate over national trade policy and practice. To the degree that the deregulation of the Canadian wine trade raises each of these two important issues, this case could well indicate the development of global trade relations in agriculture and other areas of commerce.

165. Ministerial Declaration, *supra* note 19, at 24.