

Culture Clash: Canadian Periodical Policies and the World Trade Organization

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I. INTRODUCTION: THE POLITICS OF TRADE AND CULTURE

ON 27 JANUARY 1997, Canada's Minister for International Trade delivered a speech on the topic of globalisation and culture in which he obliquely suggested that Canada reconsider its traditional approach to protecting and promoting national culture in light of changing technology and international trade relations.¹ Made against the backdrop of ongoing dispute resolution proceedings within the World Trade Organization [hereinafter WTO] concerning Canada's protectionist periodical policies,² the Minister's address was a watershed in the relationship between Canada's cultural and trade policies. For the first time, the Canadian government had acknowledged, if only tentatively, that a conflict might exist between Canada's own nationalist cultural policies and the current international trade policies—a conflict which had been noted by many unofficial observers since the commencement of the negotiations on the Canada-United States Free Trade Agreement [hereinafter FTA] over a decade ago. During those negotiations, and the wrenching public debate and national election preceding the FTA's implementation, Canadians expressed serious concern over the possibility of their national economic and cultural identities becoming consumed by their southern neighbour.³

The desire of Canadians to maintain a distinct national cultural identity has manifested itself in a somewhat defensive posture vis-à-vis the United States.

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¹ The speech was delivered by Art Eggleton, who has since been replaced in the International Trade portfolio by Sergio Marchi. See A. Eggleton, *Notes for an Address by the Honourable Art Eggleton, Minister for International Trade, on the Occasion of a Panel Discussion "Can Canada maintain its cultural identity in the face of globalization?"* (1997), online: Department of Foreign Affairs and International Trade http://www.dfait-maeci.gc.ca/english/news/statem-1/97_003e.htm (date accessed: 15 September 1997).

² The terms "periodical" and "magazine" are interchangeable in this paper.

³ See generally G.B. Doern & B.W. Tomlin, *Faith and Fear: The Free Trade Story* (Toronto: Stoddard Publishing Co., 1991).

This defensiveness explains in part the pains Canada has taken to promote the development and recognition of independent Canadian cultural industries.⁴ Canada's neighbour and largest trading partner views culture quite differently. Secure in its unique position of cultural hegemony, the United States does not see a need to adopt defensive cultural policies. Instead, due to the relatively universal appeal of U.S. cultural goods and services, culture is like any other commercial category in the U.S. One commentator summarised: "[f]or Canadians, culture is a nation-building exercise. In the United States, it is simply an enormous industry."⁵ These different views have led to conflicting perspectives on the position of cultural policies in the context of emerging international trade regimes. What Canadians see as policies designed to pursue legitimate cultural and national goals, Americans see as barriers to free trade.

These clashing perspectives on trade in cultural goods and services have reached a climax with Canadian policies respecting periodicals. Although Canada's laws and policies on trade in goods (e.g., books, periodicals, films) are really quite liberal, Canada has maintained measures designed to exclude certain types of foreign periodicals from the Canadian marketplace in order to protect the financial viability of its own periodicals. These measures successfully excluded a particular variety of U.S. publications from the mid-1960s until the early 1990s. In recent years, however, new technologies have provided U.S. publishers with the means by which to circumvent traditional Canadian protectionist measures. Efforts by the Canadian government to close these loopholes have provoked the commencement of dispute resolution proceedings under the auspices of the WTO. The result was a decision stating that Canadian periodical policies are contrary to Canada's international trade obligations. The response has been a statement of intention to abandon the offending policy measures, *and* to propose a new measure which, on its face, appears no more likely to be consistent with trade law. Clearly, the WTO decision has opened a Pandora's box. Questions have arisen concerning not only how Canada can continue to support domestic magazines, but also about how Canada and other countries can protect national culture in an era where international treaties increasingly intrude into areas previously thought to be purely domestic.

This paper describes the issues which give rise to the WTO case concerning Canada's periodical policies, summarises the WTO case at the Panel and Appellate Body levels, discusses the implications for Canada's periodical and other cultural policies, and addresses the significance of the case for international

⁴ That Canadian culture is perceived as being under siege does not mean that it is not big business. Rather, the Canadian culture industry contains an estimated 670 000 employees and in 1995 generated an annual revenue of \$16 billion. See WTO, *Trade Policy Review: Canada, Report by the Secretariat*, WT/TPR/S/22 (1996) at 120.

⁵ D. Saunders, "Magazine industry fears trade decision" *The Globe & Mail* (30 June 1997) A8.

trade law generally. The paper concludes that the Canadian government can no longer avoid addressing squarely the conflict between its nationalist cultural policies and its international trade obligations. The Canadian government must now exercise creativity in developing modes of cultural support that are consistent with trade law. Also, international alliances should be formed to negotiate a specific comprehensive agreement within the WTO to clarify the relationship between cultural protection and trade disciplines.

II. THE CANADIAN PERIODICAL INDUSTRY: PRECARIOUS AND PROTECTED

BEFORE DELVING INTO THE WTO decision regarding Canadian periodical policies, two key economic features of the Canadian periodical industry must be understood. First, the magazine publishing industry in Canada is, at best, only marginally profitable. Second, since the mid-1960s the industry has benefited from government policies designed to prevent the entry of foreign split-run magazines into the Canadian market, thus providing Canadian magazines with a degree of protection from foreign competition.

A. The Economics of Periodical Publishing in Canada

Many Canadian periodicals lead a financially precarious existence. The Task Force on the Canadian Magazine Industry reported that in 1991 Canadian periodicals returned an average pre-tax operating profit of only 2.36 percent, while over half of all Canadian periodicals failed to create any operating profit at all.⁶ Periodicals generally derive their revenue from two sources: circulation and advertising. Circulation revenues rarely cover the cost of production, thus most periodicals depend on advertising revenue to either cut losses or attain profits.⁷ Profit generated from these revenue streams affects the quality of a periodical's editorial content, which in turn may affect levels of circulation and advertising in a type of symbiotic relationship.⁸

In other words, circulation, levels of advertising, and quality of editorial content are directly related. If any one of these factors is affected, the others follow suit. Higher advertising revenues can lead to better editorial content, which may result in higher circulation and higher advertising revenues. Likewise, decreased circulation can lead to lower advertising revenues, poorer editorial content, and further decreases in circulation. These movements feed each

⁶ Canada, *Report of the Task Force on the Canadian Magazine Industry: A Question of Balance* (Ottawa: Supply and Services Canada, 1994) (Co-chairs: J.P. O'Callaghan & R. Tassé) at 27. [hereinafter *Task Force*].

⁷ *Ibid.* at 29.

⁸ *Ibid.* at 9.

other, creating a positive or negative spiralling effect. However, the key to increasing advertising revenues (and so too begins the cycle described previously) is not simply a matter of increasing circulation among more potential consumers, but of increasing circulation among the appropriate group of consumers. As was explained in the *Globe & Mail*:

Publishing is no longer a matter of reaching the greatest number of readers each week: increasingly it has to do with delivering a smaller, carefully selected group of readers to an increasingly fickle group of advertisers. Where magazines once boasted of their enormous readerships ... today they flaunt the high incomes and consumer habits of their readers.⁹

A magazine's ability to appeal to a particular demographic group will strongly influence its ability to attract advertising revenue, and thus commence the virtuous advertising/content/circulation circle. Accordingly, the demand for a periodical at the news-stand matters less than the demand from advertisers aiming at a particular market. The pool of advertising expenditures from which magazines in Canada can draw revenue is limited, and the competition among magazines for access to that pool is fierce.

B. The Competitive Challenge of Split-Run Periodicals

The competition for advertising revenues takes on an added dimension when the effect of foreign competition is considered. Until the 1960s, foreign magazines competed with Canadian magazines for Canadian advertising revenue. American publishers imported and distributed in Canada reproductions of the same magazine marketed in the United States, but with advertisements targeted at Canadians.¹⁰ This type of publication, where issues in the primary and secondary markets have the same editorial content, but contain advertisements tailored to the different markets, is known as a "split-run" periodical.

Split-run periodicals provide publishers with numerous economic advantages. There is little extra cost to inserting new advertising into a periodical sold in a second market. Moreover, as the costs of production have usually been recovered from sales and advertising in the first market, advertising in the second market can be offered at lower rates and still generate profits.¹¹ As a result, publishers of foreign split-runs can charge substantially lower rates for advertising than their Canadian counterparts, leaving the latter at a competitive disadvantage. For Canadian magazines this represents a serious challenge. If, with their lower advertising rates, split-run magazines are able to attract significant amounts of advertising revenue otherwise claimed by Canadian magazines tar-

⁹ D. Saunders, "Going Mago a Mago" *The Globe & Mail* (12 July 1997) C6.

¹⁰ *Task Force*, *supra* note 6 at 4.

¹¹ *Ibid.* at 44.

getting the same demographic, those affected Canadian magazines may decline in quality or cease production altogether.¹²

C. Canada's Protectionist Periodical Policies

During the early 1960s, it became apparent that Canadian magazines were losing ground to American split-run magazines. The Canadian government responded by adding tax and tariff measures designed to stem foreign competition and to preserve Canadian advertising revenue for their own periodicals.¹³ These policy measures, combined with an already existing postal subsidy for Canadian magazines, succeeded in maintaining the viability of the domestic magazine industry. As the Task Force on the Canadian Magazine Industry noted:

At the time of the 1961 Royal Commission on Publications, roughly 25 per cent of the magazines circulating in Canada were Canadian; as of 1992, that had increased to almost 68 per cent.¹⁴

In 1993, Time Warner, an American publisher, began transmitting magazine content for *Sports Illustrated Canada* to a printer in Canada via satellite, thus circumventing the border measures that had prevented the entry of American split-run magazines for almost 30 years. Time Warner's actions re-kindled concerns that split-runs would begin to draw advertising revenues away from Canadian periodicals and so start the spiral of reduced editorial content expenditures, leading to reduced circulation and advertising. Fearing dire consequences for the Canadian periodical industry, the government responded by buttressing existing protectionist periodical policies with a new excise tax measure. Thus far, the early tax and tariff measures, the postal subsidy, and the recent excise tax measure, have proven successful in keeping the Canadian magazine industry alive.

1. S. 19 of the Income Tax Act and Customs Tariff Code 9958

Since their implementation in 1965, s. 19 of the *Income Tax Act* and *Customs Tariff Code 9958* have jointly supported the Canadian government's policy of protecting the Canadian market from foreign split-run periodicals. The *Income Tax Act* provision provides that only advertisements placed in magazines which are at least 75 percent Canadian owned and have at least 80 percent original

¹² A foreign split-run periodical would not have to capture all or even most of the advertising revenues that would have gone to a Canadian periodical to cause severe financial hardship to the latter. So long as the two periodicals appealed to advertisers targeting the same demographic group, and the foreign periodical, because of its lower cost advertising, was able to capture even relatively small amounts of a Canadian magazines' traditional advertising revenue, it could cause a typical marginally-profitable Canadian magazine to suffer losses.

¹³ *Task Force*, *supra* note 6 at iii.

¹⁴ *Ibid.* at 2.

editorial content are deductible expenses for the advertiser.¹⁵ Though long lived, s. 19 has likely not been a significant influence on advertising decisions. The savings from running an advertisement in a split-run magazine still far outweigh the tax savings gained by running the same advertisement in a magazine meeting the s. 19 requirements.¹⁶ This means that the Code 9958 measure has provided the primary barrier to entry for foreign split-run magazines.

Customs Tariff Code 9958 is found in Schedule VII of the *Customs Tariff*, and is executed through Article 114 of the *Customs Tariff*.¹⁷ Code 9958 bars the importation of editions of periodicals containing advertisements primarily directed to the Canadian market which do not also appear in all editions in the periodicals' country of origin. It also bars importation where an issue of a periodical imported into Canada contains advertising more than five percent of which is directed to the Canadian market. Indicia of whether advertisements are targeting the Canadian market include the use of enticements to the Canadian market, references to the GST, listing of Canadian addresses (and not foreign addresses), and invitations addressed specifically to Canadian consumers.¹⁸

The *Customs Tariff* Code 9958 has effectively excluded foreign competition for Canadian advertising dollars for over 30 years. By 1994, however, technology had rendered it obsolete. As a tariff barrier, the Code prohibited foreign split-run periodicals printed abroad from physically crossing the Canadian border. It was ineffective, however, in preventing the content of periodicals from being transmitted across the border electronically and then printed in Canada. Recognising the inadequacies of this old protectionist measure, the Canadian government established the Task Force on the Canadian Magazine Industry to recommend modifications to the existing regime or new measures for maintaining the viability of the Canadian periodical industry.¹⁹ Central among the resulting recommendations was that the federal government implement an excise tax on advertising in split-run periodicals.²⁰ The Canadian government followed the Task Force's recommendation by modifying Part V.I of the *Excise Tax Act*.

¹⁵ *Income Tax Act*, R.S.C. 1985, c. 1, s. 19.

¹⁶ For example, the Task Force reported that *Sport's Illustrated* was offering full page four colour advertisements in its Canadian split-run to advertisers for \$6 250, which is approximately half the cost of an equivalent ad for advertisers in a regional edition with similar circulation in the U.S. See *Task Force*, *supra* note 6 at 44.

¹⁷ See *Customs Tariff*, R.S.C. 1985, c.41 (3rd supp.).

¹⁸ Department of National Revenue for Customs and Excise guidelines for the application and administration of Code 9958 (Revenue Canada Memorandum D9-1-10, 21 May 1993).

¹⁹ *Task Force*, *supra* note 6 at 4-5.

²⁰ *Ibid.* at 64.

2. Part V.I of the Excise Tax Act

On 15 December 1995, the *Excise Tax Act* was amended by introducing a tax equal to 80 percent of the value of all advertising contained in each split-run edition periodical.²¹ The tax was meant to close the loophole of satellite transmission of split-run content.²² The policy rationale behind the tax was made clear in the Task Force's recommendations, "[t]he rate of tax should be sufficiently high to improve the ability of original editorial material to attract advertising directed at Canadian consumers."²³

The provision targets magazines that do not produce "original editorial material," which would encompass any split-run periodical, domestic or foreign.²⁴ Because both domestic and foreign split-run magazines would be caught by the legislation, the Task Force was of the opinion that the tax complied with the international trade law requirement of "national treatment."²⁵ Although, *de jure*, the measure appears to affect Canadian and U.S. periodicals equally, in fact the measure affects very few Canadian periodicals.²⁶

3. Preferential Postal Rates

Unlike the tax and tariff measures, Canada's preferential postal rates policies were initially implemented for purely domestic reasons. Two separate postal rate issues were disputed by the U.S. The first concerned subsidised rates, known as funded postal rates. The second pertained to "commercial" postal rates applied

²¹ See *An Act to Amend the Excise Tax Act and the Income Tax Act*, S.C. 1995, c.46, s. 35(1) "split-run edition," and s. 36(1), respectively.

²² In introducing Bill C-103, which contained the excise tax measure, to the House of Commons, then Minister for Canadian Heritage Michel Dupuy said: "*Sports Illustrated Canada* managed to get around Custom Tariff 9958 because most of its content was sent electronically from the United States. It was simply a loophole in the tariff laws since electronic transmission made it possible to avoid tariff regulations." *House of Commons Debates* (25 September 1995) at 14790-1.

²³ *Task Force*, *supra* note 6 at 65.

²⁴ There are two exceptions. Magazines that would be split-runs but which are distributed primarily outside of Canada are considered not to be split-runs (this amounts to an exemption for split-runs that whose primary target is a country other than Canada, but which have a minimal distribution in Canada as well). Also, there is a grandfather clause exempting the application of the tax to split-run periodicals that had been distributed in Canada prior to 26 March 1993. This section continues an exemption from Canada's policies regarding split-runs that had been negotiated during the 1970s, and from which only Reader's Digest and Time Magazine benefited. See *An Act to Amend the Excise Tax Act and the Income Tax Act*, *supra* note 21, s. 35(5) and s. 39, respectively.

²⁵ *Task Force*, *supra* note 6 at 66.

²⁶ Few Canadian periodicals would be affected because few Canadian periodicals are sold in the American market.

to Canadian periodicals not benefiting from the funded rates and to foreign periodicals.

Since the early part of this century, Canada has provided funded postal rates for Canadian magazines in order to ensure their availability at low cost throughout Canada.²⁷ These rates are administered through the Publications Assistance Program under the auspices of the Department of Canadian Heritage and Canada Post. The Program is aimed at assisting certain Canadian-owned, controlled, and published publications by providing them with below-cost postage.²⁸ Pursuant to an agreement between the two Ministries, Canada Post underwrites the below-cost funding for designated periodicals in return for quarterly payments from Canadian Heritage.²⁹ In the early 1990s, the Canadian government began to phase out this program, but it was extended for a period of three years commencing in May 1996.³⁰

The second postal rate issue is concerned with the different commercial rates charged to Canadian versus foreign publishers. Canadian periodicals that do not benefit from the funded rates may enter into an agreement with Canada Post for bulk mailing rates and related services. Foreign publishers mailing periodicals in Canada may enter into similar agreements, but are required to pay a different, more expensive postal rate than Canadian publishers. The commercial Canadian rates, which range from \$0.103 per copy to \$0.378 per copy, are considerably less than the commercial international rate, which is \$0.436 per copy. Canadian publishers also benefit from further discounts for postal procedures, known as palletisation and pre-sort discounts, which are not available to foreign publishers.

III. THE CASE BEFORE THE WTO

A. The Resort to Formal Dispute Settlement Mechanisms

In the past, the United States and Canada have attempted to settle their disputes about Canada's cultural policies in the political arena.³¹ It is therefore remarkable that the U.S. commenced formal dispute settlement proceedings

²⁷ *Task Force*, *supra* note 6 at 45.

²⁸ In addition to ownership, control, and place of publication, eligibility criteria include factors such as length of time in operation, minimum paid circulation (*i.e.*, number of paying subscribers), editing, typesetting and printing, advertising content, frequency, and sale price. See Department of Canadian Heritage, Publications Assistance Program http://www.pch.gc.ca/culture/cult_ind/pap_e.htm (date accessed: 29 October 1997).

²⁹ *Newspapers and Periodicals Regulations*, SOR/96-209.

³⁰ *Ibid.*

³¹ K. Acheson & C.J. Maule, "Canada's Cultural Policies—You Can't Have It Both Ways" (1996) 4:3 *Canadian Foreign Policy* at 20.

against Canada. The excise tax measure has essentially the same effect as the tariff Code 9958 measure, which excluded foreign split-run periodicals from Canada for over thirty years—however, the new measure provoked American ire in a way that the other measures have not. The American reaction cannot be explained by anything intrinsic to the excise tax itself, but rather should be understood as a reflection of changing American policies regarding international trade. The United States has become increasingly activist concerning trade in cultural products, as those products have come to represent a larger portion of U.S. export earnings. It is against this backdrop that the U.S. decision to challenge Canada's periodical support measures must be viewed.

In deciding to use a formal dispute mechanism as a method of resolving its dispute with Canada, the U.S. had to choose between the NAFTA and WTO dispute resolution systems.³² While the NAFTA forum might seem more appropriate for addressing a dispute between two NAFTA members, there were clear advantages if the WTO route was chosen. Winning a case in the WTO would set a precedent that the United States could later apply in similar disputes with other WTO members, e.g. France. In fact, the NAFTA contains "cultural exemption" clauses that would have made victory less certain for the U.S.³³

The WTO dispute resolution system is legalistic and judicial in nature, involving "a high degree of automaticity in decision-making at every stage of the dispute settlement process."³⁴ This ensures that disputes progress through various stages within defined time frames without the disputing countries blocking

³² In cases where a dispute arises under both the WTO and NAFTA rules, Article 2005 of NAFTA allows the complaining party a choice between the two. However, once proceedings have been commenced in either forum that forum must be used exclusively. See North American Free Trade Agreement: between the government of Canada, the government of the United Mexican States and the government of the United States of America (Ottawa: Minister of Supply and Services, 1992) [hereinafter NAFTA].

³³ Although the U.S. argues that it would have a right to retaliate against Canada's protectionist policies under the NAFTA, Canada argues that the cultural "exemptions" in the Agreement shield it from such a right of retaliation. As the law is unsettled at this point, the U.S. decided it would press its advantage in the WTO. See J.A. Ragosta, J.R. Magnus, & K.L. Shaw, "Having your cake and eating it too" (Visited 20 September 1997) <<http://www.dbtrade.com/publications/180898a>>. Also, as Bernier has noted, Canada has the option of invoking NAFTA Article 103, which provides that NAFTA prevails over GATT in the event of an inconsistency, but as this provision has no validity under GATT, Canada would not be released from its GATT obligations. See: I. Bernier, "Cultural Goods and Services in International Trade Law" (Paper presented at Centre for Trade Policy and Law seminar, *The Culture/Trade Quandary: Canada's Policy Options*, Ottawa, 9 October 1997) [unpublished] at 14.

³⁴ D.P. Steger, "WTO Dispute Settlement: Revitalisation of Multilateralism After the Uruguay Round" (Draft paper presented at Centre for Asia-Pacific Initiatives conference, *The Asia-Pacific Region and the Expanding Borders of the WTO: Implications, Challenges and Opportunities*, Vancouver, 7–8 June 1996) [unpublished] at 5.

or delaying the process. The process formally begins with a request by a complainant for the establishment of a panel to hear the dispute³⁵—such requests are granted automatically.³⁶ Likewise, the adoption of the panel's report and the authorisation of retaliatory measures are also automatic, should the losing party not comply with the panel's rulings.³⁷

Member nations may only resort to the formal WTO dispute resolution process after bilateral settlement consultations have failed to produce results.³⁸ The United States Trade Representative filed an initial complaint with the WTO on 12 March 1996. Initial consultations, in Ottawa in April and Washington in May, proved unfruitful. One month later, the U.S. requested the establishment of a WTO Panel to decide whether Canadian policies relating to periodicals were in keeping with GATT rules.³⁹ The U.S. and Canada then made submissions to the WTO dispute settlement panel in September 1996 and the Panel released its report on 14 March 1997. Both Canada and the United States appealed certain issues in the Panel Report to the WTO Appellate Body,⁴⁰ which released its report on 30 June 1997. The issues and arguments raised before the Panel and the Appellate Body are discussed below.

B. Before the Panel

The U.S. challenged all three of Canada's main policy planks which support domestic periodicals before the WTO Panel.

³⁵ *General Agreement on Tariffs and Trade 1994, Understanding on Rules and Procedures Governing the Settlement of Disputes*, 1994, World Trade Organization, Article 5.4 (visited 25 September 1997) <<http://www.wto.org/wto/legal/finalact.htm>> [hereinafter *Dispute Settlement Understanding*].

³⁶ That is, unless there is consensus within the WTO General Council that such a panel should not be granted. See *Ibid.* at Article 6.

³⁷ If a party fails to comply with a panel decision, the Dispute Settlement Body which oversees the dispute settlement process may authorise the aggrieved party to take retaliatory measures against that party by imposing higher tariffs on an equivalent value of products imported from the non-complying country. The tariffs imposed in retaliation should, where possible, be in the same economic sector as those products affected by the measures which gave rise to the complaint. See *Ibid.* at Articles 22.2 and 22.3.

³⁸ The WTO Director General may, at the parties' request, use his good offices to assist in the mediation process prior to the commencement of formal dispute settlement procedures. See *Ibid.* at Articles 5 and 5.4.

³⁹ R.G. Atkey, & R.A. Young, "Canadian Cultural Policy: Guard Posts Along the 'Undefended Border'" (Address to the Canada-US Law Institute Conference on NAFTA Revisited, Case Western Reserve University School of Law, Cleveland, Ohio, 18–20 April 1997)[unpublished] at 21.

⁴⁰ Parties may appeal Panel Reports on points of law to the WTO Appellate Body. See *Dispute Settlement Understanding*, *supra* note 35 at Article 17.5.

1. Customs Tariff Code 9958

Two legal issues were raised in relation to *Customs Tariff Code 9958*. The first issue related to GATT Art. XI:1,⁴¹ which forbids imposition of prohibitions or restrictions other than duties, taxes, or other charges on imported products. The second, more contentious issue concerned GATT 1994 Art. XX(d).

Article XX(d) allows WTO members to adopt measures that would otherwise be contrary to the GATT, provided those measures are necessary to “secure compliance with laws or regulations,” which themselves are not inconsistent with the GATT. The exception provided under Article XX(d) is a narrow one, and applies only if the measures contrary to GATT do not arbitrarily or unjustifiably discriminate between countries, and if they are not a disguised restriction on international trade.⁴² Furthermore, the party claiming the exception has the burden of proving that the measure in question falls within the exception.⁴³

In the arguments made before the Panel, the United States claimed that Code 9958 violated Article XI:1 by banning foreign split-run periodicals from the Canadian market.⁴⁴ Canada did not contest the point, but countered that Code 9958 was intended to work in conjunction with s. 19 of the *Income Tax Act*⁴⁵ and was justifiable under GATT Article XX(d) as a measure necessary to secure *substantial* compliance with s. 19.⁴⁶ The United States argued that the Code did not come within the Article XX(d) exemption claimed by Canada.⁴⁷

⁴¹ The relevant part of the article reads: “[n]o prohibitions or restrictions other than duties, taxes or other charges ... shall be instituted or maintained by any [Member] on the importation of any product of the territory of any other [Member]” See *General Agreement on Tariffs and Trade 1994*, 1994, World Trade Organization, Article XI:1 (visited 25 September 1997) <<http://www.wto.org/wto/legal/finalact.htm>> [hereinafter “GATT 1994”].

⁴² See E. McGovern, *International Trade Regulation*, 3rd ed. (Exeter: Globefield Press, 1995) at 13.11–2.

⁴³ *Ibid.* at 13.11–3.

⁴⁴ *Canada—Certain Measures Concerning Periodicals* (United States v. Canada) (14 March 1997) WT/DS31/R, (97–0939) at para 3.3 [hereinafter *Panel Report*].

⁴⁵ See E. McGovern, *supra* note 42. The GATT-consistency of s. 19 of the *Income Tax Act* was not challenged by the United States in this case.

⁴⁶ Canada’s argument was that Code 9958 worked in conjunction with s. 19 by helping to fulfil the objectives of s. 19. This argument required Canada to distinguish a previous WTO case *EEC- Regulations on Parts and Components* (16 May 1990) BISD 37S/132 which held that non-conforming measures had to be necessary for enforcing another law, and not merely to fulfil the objectives of that law. Canada attempted to distinguish the case on the grounds that the enforceability test it required was appropriate for cases where the real goal was formal compliance, but not where the goal was substantial compliance inseparable from the social and economic objectives the measure aimed to secure. See *Panel Report, supra* note 45 at para.3.5, 3.10.

⁴⁷ *Ibid.* at para. 3.6, 3.7.

The Panel concluded that Code 9958 was indeed, by its terms, inconsistent with GATT 1994 Article XI:1⁴⁸ and not justifiable under GATT Article XX(d).⁴⁹ It failed to qualify as a measure necessary “to secure compliance” because, although it was aimed at securing the same objective, any such compliance with s. 19 would have been merely an “incidental effect of a separate measure distinct from the tax provision.”⁵⁰ The Panel noted that if the Canadian argument were followed, whenever a policy objective could not be attained by enforcing obligations of a GATT-consistent law, countries would be allowed to turn to GATT-inconsistent measures to secure compliance with the policy objective.⁵¹

2. Part V.I of the Excise Tax Act

The arguments regarding the GATT-consistency of the *Excise Tax Act* focussed mainly on the national treatment principle, as embodied in GATT 1994 Article III:2.⁵² A secondary issue concerned whether the excise tax was being imposed upon a good or service, and therefore whether it was an issue appropriately decided with reference to GATT 1994 or with reference to the General Agreement on Trade in Services (GATS).

Generally speaking, the national treatment principle requires that once imported goods have cleared a nation’s customs agency and complied with required border procedures, they are to receive treatment under domestic regulatory or tax policies which is no worse than that applied to domestically produced goods.⁵³ The principle is expressed in GATT 1994 Article III as a prohibition on governments from adopting measures applied to imported or domestic products which affords protection to domestic production alone.⁵⁴ Article III:2 specifically prohibits taxes on imports in excess of those applied, directly or indirectly, to like domestic products.⁵⁵

⁴⁸ *Ibid.* at para. 5.5.

⁴⁹ *Ibid.* at para. 5.11.

⁵⁰ *Ibid.* at para. 5.10.

⁵¹ In arriving at this decision, the Panel followed closely the reasoning in *European Economic Communities—Regulations on Imports of Parts and Components*, *supra* note 47. See *Ibid.* at para. 5.9, 5.10.

⁵² See GATT 1994, *supra* note 41 at Article III.

⁵³ See generally, J.H. Jackson, *The World Trading System: Law and Policy of International Economic Relations*, (Cambridge: Massachusetts Institute of Technology, 1994) at Chapter 8.

⁵⁴ See *Article III*, *supra* note 52.

⁵⁵ See *Article III*, *supra* note 52.

The United States argued that the excise tax on split-run periodicals violated the national treatment principle in GATT Art. III:2.⁵⁶ Specifically, it claimed that the excise tax created an “artificial distinction between split-run magazines and other types of magazines.”⁵⁷ The U.S. asserted that by imposing a tax only on split-run magazines, Canada was treating imported magazines in a manner different than “like domestic products,” *i.e.*, domestic magazines.⁵⁸

Canada maintained that Part V.I of the *Excise Tax Act* was a measure designed to tax advertising services provided to Canadian advertisers, not to tax periodicals as “goods.”⁵⁹ Therefore, it was argued, the measure fell under the General Agreement on Trade in Services (GATS), and not the GATT 1994.⁶⁰ Canada noted that it had not made specific commitments regarding advertising services under GATS. As a result, there were no restrictions on Canada concerning measures relating to advertising services, and it was not obliged to provide national treatment to members of the WTO concerning advertising services in Canada.⁶¹ In addition, Canada argued that since editorial content was an essential characteristic of a periodical, periodicals with Canadian market-specific editorial content were distinguishable from split-runs reproducing foreign editorial content; the two types of periodicals were not like products for the purposes of Article III:2.⁶²

The Panel concluded that imported split-run periodicals and domestic non split-run periodicals were like products within the meaning of Article III:2.⁶³ In arriving at this conclusion, a narrow reading of the term like products was taken. An examination ensued, comparing the treatment of imported split-run periodicals and domestic non split-run periodicals on the facts of the case considering such factors as the product’s end-use, consumer tastes, and the prod-

⁵⁶ The United States also made a very brief argument in the alternative, that if Article III:2 was not violated, then Article III:4 was. Canada did not respond to this argument, and it was not considered in the Panel’s decision as it disposed of the case on other grounds. See *Panel Report*, *supra* note 44 at para. 3.144, 3.145 and 5.30.

⁵⁷ *Ibid.* at para. 3.32.

⁵⁸ Article III:2 also requires that imports be treated the same as like domestic products. See *supra* note 52.

⁵⁹ *Panel Report*, *supra* note 44 at para. 3.33.

⁶⁰ *Ibid.* at para. 3.33.

⁶¹ *Ibid.* at para. 3.34. Canada and the U.S. generated lengthy, elaborate arguments about whether the excise tax applied “directly or indirectly” (within the meaning of Article III:2) to a product. This debate hinged in large part on whether the tax was aimed at a product, *i.e.*, each split-run edition, or to a service, *i.e.*, the value of advertising carried by each issue of the magazine assessed against the seller of the magazine. *Ibid.* at para. 3.43 to 3.56.

⁶² *Ibid.* at para. 3.61.

⁶³ *Ibid.* at para. 5.26.

uct's properties, nature, and quality.⁶⁴ As there were no imported split-run periodicals marketed in Canada due to the operation of Code 9958, the Panel made the comparison on the basis of a hypothetical import.⁶⁵

Regarding a potential conflict between obligations under GATT 1994 and GATS, the Panel concluded that the two agreements "can co-exist and that one does not override the other."⁶⁶ Therefore, GATT 1994 was applicable to Part V.I of the *Excise Tax Act*. The Panel rejected Canada's argument that GATT 1994 did not apply to the excise tax because the tax was a tax on services, and not on goods. The Panel found that the tax applied indirectly to periodicals within the meaning of Article III:2⁶⁷—Canada's policy of imposing an excise tax on the advertising in foreign split-runs was contrary to the obligations Canada had assumed under GATT 1994.

3. Preferential Postal Rates

The legal issues raised in the context of Canada's postal rate policies concerned GATT 1994 Article III:4 and Article III:8(b). Article III:4 provides that laws, regulations, and requirements of the domestic market must afford competitive opportunities to imported products no less favourable than those accorded to like domestic products.⁶⁸ Article III:8(b) sets out a limitation on Article III, as it allows subsidies to be paid to domestic producers provided they are paid to them exclusively.⁶⁹

The U.S. argued that the offer of postal rates for funded and commercial Canadian publications preferential to those for commercial international publications contravened GATT Article III:4.⁷⁰ The U.S. also argued that the subsidies resulting in funded postal rates provided by Canada Post to Canadian magazines pursuant to its agreement with Canadian Heritage were not paid exclusively and directly to domestic producers, as required by Article III:8(b).

⁶⁴ Here the Panel was following the reasoning in the *Japan—Taxes on Alcoholic Beverages* case [(1 November 1996) WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R] See *Ibid.* at para. 5.22.

⁶⁵ *Ibid.* at paragraphs 5.23 and 5.25.

⁶⁶ *Ibid.* To arrive at this conclusion, the Panel examined the GATT, GATS and WTO Article II:2 in light of Article 31(1) of the *Vienna Convention on the Law of Treaties*, (1969) 1155 U.N.T.S. 331, and followed reasoning in the Appellate Body Report on *Japan—Taxes on Alcoholic Beverages* case, *supra* note 65.

⁶⁷ *Panel Report*, *supra* note 44 at para. 5.29.

⁶⁸ McGovern notes that several panels have arrived at this interpretation of Article III:4. See McGovern, *supra* note 42 at 8.23–1. See also GATT 1994, *supra* note 41 at Article III:4.

⁶⁹ See *Ibid.* at Article III:8(b).

⁷⁰ The parties did not disagree that in the context of this issue international and domestic periodicals were like products. See *Panel Report*, *supra* note 44 at para. 3.146.

Thus, these discounts “modify the conditions of competition between domestic and imported products in contravention of Article III:4.”⁷¹

In response, Canada argued that Canada Post, as a Crown Corporation, sits at arm’s length from the government and operates according to commercial imperatives—that it was these commercial imperatives, not government policy, which resulted in the different commercial Canadian and International postage rates.⁷² Accordingly, Canada argued, the national treatment principle mandated in Article III:4 did not apply to the commercial rates set by Canada Post.⁷³ Regarding the funded postal rates, Canada argued that “the specific form in which the subsidy is paid is irrelevant to the operation of Article III:8(b). This provided that a payment is made by the government for the exclusive benefit of domestic producers and that, regardless of to whom the subsidy was paid, it had the same end economic effect of benefiting the eligible publishers.”⁷⁴

The Panel decided that Canada Post, as a Crown Corporation, was found to be “generally dependent upon government action” and that its pricing policy for periodical postal rates fell within the meaning of government regulations or requirements in Article III:4.⁷⁵ Since Canada Post maintained lower rates for funded periodicals and commercial Canadian periodicals than for the like product of commercial international periodicals, the pricing policy was inconsistent with Canada’s obligations under GATT 1994 Article III:4.⁷⁶ However, the Panel found that as Canada Post did not retain any economic benefits from the funded rate scheme, and that the payments were made exclusively to Canadian publishers, the subsidy was justifiable under Article III:8(b).⁷⁷ Canada could maintain its postal subsidy for funded periodicals without coming into conflict with its WTO obligations.

⁷¹ *Panel Report*, *supra* note 44 at para. 3.182.

⁷² *Ibid.* at para. 3.150 to 3.156.

⁷³ *Ibid.* at para. 3.153.

⁷⁴ *Ibid.* at para. 3.186.

⁷⁵ *Ibid.* at para. 5.36.

⁷⁶ The Panel stated: “[w]e find that the design, architecture and structure of Canada Post’s different pricing policy on domestic and imported periodicals all point to the effect that the measure is applied so as to afford protection to the domestic production of periodicals.” *Ibid.* at para. 5.38, 5.39.

⁷⁷ The Panel noted a contradiction in the United States’ argument that Canada Post was a governmental actor and that the subsidies originating with Canadian Heritage but dispensed through Canada Post contradicted GATT because they did not go directly to the end recipient. The Panel stated, “[i]f Canada Post is a government agency, the payment of funds from Canadian Heritage to Canada Post is merely an internal transfer of resources, and the payment of the subsidy is made directly to Canadian publishers.” *Ibid.* at para. 5.42 to 5.44.

C. Before the Appellate Body

The original Panel decision ruled against the GATT-consistency of the excise tax in Code 9958, and a portion of the postal subsidies measure, while at the same time allowing Canada to continue to provide lower postal rates to Canadian magazines. Canada was not satisfied with this decision, and notified the WTO Dispute Settlement Body on 29 April 1997 of its intention to appeal certain issues of law and legal interpretations made in the Panel Report. Both Canada and the United States had the opportunity to present arguments and answer questions from the Division of the Appellate Body at the oral hearing held on 2 June 1997.

The issues raised by Canada on appeal were the Panel's findings regarding the applicability of GATT 1994 to Part V.I of the *Excise Tax Act*, and the consistency of Part V.I of the *Excise Tax Act* with Article III:2 of GATT 1994. The U.S. appealed the Panel's findings regarding the consistency of the funded postal rate scheme with Article III:8(b) of the GATT 1994.

1. *Applicability of GATT 1994 to Part V.I of the Excise Tax Act*

Canada argued that the Panel made an error in law in its characterisation of Part V.I of the *Excise Tax Act* as a measure regulating goods according to GATT Article III:2, and not services under GATS.⁷⁸ In Canada's opinion, Part V.I of the *Excise Tax Act* was a measure for regulating trade in services, and therefore an appropriate subject matter for GATS, but not GATT.⁷⁹ The U.S. claimed that if Canada's view prevailed floodgates would open for WTO members to adopt services measures that would have discriminatory impact on imported goods, contrary to the purpose of Article III of GATT 1994.⁸⁰

The Appellate Body held that the excise tax was a tax on split-run magazines, citing several indicators (including the tax's name) that the actual target of the tax was the periodicals themselves, and not the service.⁸¹ The Appellate Body also noted that the tax was a companion to Code 9958, which Canada had acknowledged prohibited the importation of split-run periodicals. Since the two shared the "same objective and purpose," they "should be analysed in the same manner."⁸² As a result of this analysis, the Appellate Body found that the excise tax was a tax on the periodical⁸³—GATT 1994 did apply. The Appellate

⁷⁸ *Canada—Certain Measures Concerning Periodicals (Complaint by the United States) (1997)*, WTO Doc. WT/DS31/AB/R at 4 (Report of the Appellate Body) [hereinafter *Appellate Body Report*].

⁷⁹ *Ibid.* at 4.

⁸⁰ *Ibid.* at 11.

⁸¹ *Ibid.* at 18, 19.

⁸² *Ibid.* at 20.

⁸³ *Ibid.* at 19, 20.

Body also supported the Panel's finding that the obligations of GATT 1994 and GATS co-exist.

2. Consistency of Part V.I of the Excise Tax Act with Article III:2 of GATT 1994

In considering the consistency of the *Excise Tax Act* with GATT 1994 Article III:2, two central issues were raised. The first was whether imported split-run periodicals and domestic non split-run periodicals were like products within the meaning of Article III:2. The second issue was whether the excise tax was applied so as to afford protection to domestic production, as prohibited by the second sentence of Article III:2.⁸⁴

Canada challenged the Panel's finding that Canadian non split-run and imported split-run periodicals were like products on the basis that the Panel made a series of errors in law when it relied on a hypothetical example in applying the like products test.⁸⁵ It argued that even if imported split-run periodicals and Canadian non-split run periodicals were like products, Part V.I of the *Excise Tax Act* did not discriminate against the imported products.⁸⁶ Canada also maintained that the Appellate Body did not have the jurisdiction to decide the issue raised by the second sentence of Article III:2, as this would involve an examination of factual elements not addressed by the Panel in the first instance, and which the United States failed to raise as an issue on appeal.⁸⁷

On the issue of like products, the Appellate Body found that the Panel erred in legal reasoning by looking away from the evidence and exhibits before it. Instead, it had relied on a single hypothetical example in concluding that domestic non split-run magazines and foreign split-run magazines can be like products.⁸⁸ On these grounds, the Appellate Body reversed the conclusions of the Panel on like products⁸⁹ before arriving at the same conclusion *via* different reasoning. The Appellate Body decided that it could examine issues raised by the

⁸⁴ See GATT 1994, *supra* note 41, at Article III.

⁸⁵ Briefly stated, these arguments were: that rather than resorting to a hypothetical example, the Panel should have considered the evidence that had been put before it, which included examples of split-run and non-split-run magazines; that in the hypothetical example, the Panel compared two imported "Canadian" editions rather than an imported product and a domestic product; that the Panel failed to approach the issue on a case-by-case basis analysing the specific properties of the magazines in a Canadian context. See *Appellate Body Report*, *supra* note 78 at 6, 7.

⁸⁶ *Ibid.* at 7.

⁸⁷ *Ibid.* at 8.

⁸⁸ *Ibid.* at 25.

⁸⁹ The Appellate Body is confined to examining questions of law, not of fact, and therefore was not empowered to determine the factual issue of whether these articles were or were not like products. See *Ibid.* at 25.

second sentence of Article III:2 because the first and second sentences were part of a logical continuum.⁹⁰

In its analysis, the Appellate Body found that the Task Force report and statements by the Minister for Canadian Heritage and other Canadian officials acknowledged that imported split-run and domestic non-split run magazines are substitutable, contrary to Canada's assertions.⁹¹ The Appellate Body stated:

Our conclusion that imported split-run periodicals and domestic non-split-run periodicals are "directly competitive and substitutable" does not mean that all periodicals belong to the same relevant market, whatever their editorial content. A periodical containing mainly current news is not directly competitive or substitutable with a periodical dedicated to gardening, chess, sports, music or cuisine. But newsmagazines, like TIME, TIME Canada and Maclean's, are directly competitive or substitutable in spite of the "Canadian" content of Maclean's.⁹²

The Appellate Body went on to conclude that the magnitude of taxation levied by Part V.I of the *Excise Tax Act* was sufficient to prevent the production and sale of split-run periodicals in Canada, and as such, was inconsistent with the provisions of the second sentence of Article III:2.⁹³ In arriving at this finding, the Appellate Body referred to the Task Force Report, Ministerial statements and the demonstrated effect of the measure in concluding that the "design and structure of Part V.I of the *Excise Tax Act* is clearly to afford protection to the production of Canadian periodicals."⁹⁴

⁹⁰ Canada and the U.S. differed in opinion over whether the Appellate Body had the jurisdiction to examine a claim under Article III:2, second sentence. Canada argued that, because it had not been raised in the appeal to the Panel's findings, it was beyond the jurisdiction of the Appellate Body. The U.S. argued that the goals of Article 3.3 of the Dispute Settlement Understanding should be adhered to, which stipulates the importance to the WTO of the prompt settling of disputes. The Appellate Body decided that it could examine the second sentence of Article III:2 because the first and second sentences of the Article were closely-linked and "part of a logical continuum." *Ibid.* at 26.

⁹¹ *Ibid.* at 31.

⁹² *Ibid.*

⁹³ *Ibid.* at 33.

⁹⁴ *Ibid.* at 34, 35.

3. Consistency of the funded postal rate scheme with Article III:8(b) of the GATT 1994

The U.S. questioned the Panel's finding that the funded rate scheme was justified under Art. III:(b) of GATT 1994. The United States and Canada agreed that the funded postal rates amounted to a "payment of subsidies." The two countries disagreed, however, on whether the subsidies were paid "exclusively to domestic producers," as required under Article III:8(b).

The Appellate Body interpreted the text of Article III:8(b) in relation to Articles III:2 and III:4 of GATT 1994 and their drafting history to arrive at the conclusion that the Panel's interpretation of the provision was incorrect.⁹⁵ The Appellate Body held that only the payment of subsidies involving the direct expenditure of revenue by government (and not tax exemptions or reduced postal rates) are exempted from the application of Article III.⁹⁶ Accordingly, the Appellate Body reversed the Panel's findings that the funded postal rates for periodicals were justified under Article III:8(b) of the GATT 1994.⁹⁷

IV. SIGNIFICANCE OF THE DECISION FOR INTERNATIONAL TRADE LAW

THERE ARE MANY ASPECTS of the WTO decision that have significance well beyond the facts of the case. First, the decision was the first to consider the possibility of conflict between the GATT and the GATS.⁹⁸ Second, it broadened the concept of like products in Article III of GATT 1994. Finally, it altered and narrowed the understanding of the role of state corporations in subsidising culture and of what types of subsidies are permissible within the international trade law regime.

A. GATT vs. GATS

The finding that Part V.I of the *Excise Tax Act*, a measure Canada claimed related to services, was GATT-applicable will likely have important ramifications for countries employing services-related measures to protect or promote national culture. Now that the GATT system has been existent for over fifty years, countries have a fairly well developed understanding of the obligations it imposes upon them in terms of what sort of domestic cultural policies they can adopt without contravening GATT. GATS, on the other hand, is a still evolving four-year-old agreement. Understandably, countries are cautious in their

⁹⁵ *Ibid.* at 36, 37.

⁹⁶ *Ibid.* at 37.

⁹⁷ *Ibid.* at 36, 37.

⁹⁸ See Bernier, *supra* note 32 at 4.

approach to cultural issues under GATS, and many have made no or limited commitments in cultural services related under GATS. However, there is not always a clear distinction between cultural goods and services.⁹⁹

The decision in *Canada—Certain Measures Concerning Periodicals* regarding the relationship between GATT and G.A.T.S. holds out the prospect that countries protecting services-related cultural policies by not making specific commitments under the G.A.T.S. may find those policies challenged for impinging upon the GATT 1994. The periodicals case made it clear that neither agreement takes priority over the other in instances where issues do not neatly divide into either the services or goods categories.¹⁰⁰ The effect of the Canadian periodicals cases will be to cause nations to consider what they have in fact committed themselves to in what may have seemed clear and separate goods (GATT) and services (G.A.T.S.) regimes.

The WTO decision spawns many questions, such as whether a greater distinction should be made between trade in services and trade in goods. As things stand, scenarios can be envisioned where countries have made limited specific commitments under GATS, or have made no commitments at all, and yet still may be challenged through the GATT.¹⁰¹ To the extent that overlapping goods and services regimes are contrary to the original intentions of the parties, WTO members may be far more leery of further commitments within a Uruguay Round style multi-treaty regime. Countries hoping to preserve some sort of freedom to protect culture will have to take *Canada—Certain Measures Concerning Periodicals* into account when negotiating future trade treaties.

B. GATT Article III (National Treatment)

The *Canada—Certain Measures Concerning Periodicals* decision also sheds light on the like products aspect of the GATT Article III national treatment obligation. In determining the meaning of like products the Appellate Body did not distinguish between periodicals on the basis of intellectual content, but decided that they are directly competitive or substitutable if they can legitimately com-

⁹⁹ As proof of this point, Bernier has noted that cinema is specifically mentioned in Articles III and IV of GATT 1994, and is also considered as a service in the GATS. *Ibid.* at 3, 4.

¹⁰⁰ The Appellate Body supported the Panel's determination that "the ordinary meaning of the texts of GATT 1994 and G.A.T.S. as well as Article II:2 of the WTO Agreement, taken together, indicates that obligations under GATT 1994 and G.A.T.S. can co-exist and that one does not override the other." See *Appellate Body Report, supra* note 78 at 19. The very same issue was considered with the same result in the case of *European Communities—Regime for the importation, distribution and sale of bananas* which determined that measures could fall exclusively within GATT, within GATS, or even within the scope of both, depending upon how the measure affects the goods or the supply of the service in question, and on the facts of the case. See *European Communities—Regime for the Importation, Distribution and Sale of Bananas* (9 September 1997) WT/DS27/AB/R (97-0000) at 86.

¹⁰¹ See *Bernier, supra* note 32 at 5.

pete with others in the marketplace. Competitive viability rather than cultural attributes or qualities, is central when deciding whether or not products are "like." One commentator described the decision this way:

The truth of the matter is that the Appellate Body, instead of addressing squarely the issue of the specificity of cultural products as vehicles of information, has simply applied to news periodicals the same type of reasoning as was applied to Japanese Alcohols case to foreign vodka and Japanese vodka.¹⁰²

By focussing on a strict market-based test, the Appellate Body's interpretation of like products fails to account for, or even acknowledge, the intangible intellectual/cultural essence of cultural products. This implies that international trade law demands that cultural products be treated no differently than non-cultural goods, leaving little room for governments to pursue policies aimed at achieving cultural goals, no matter how legitimate and important, if those policies would affect the competition between foreign and domestic products in the marketplace.

C. Allowable Subsidies

The ruling on the postal subsidy for funded periodicals narrowed the understanding of the phrase "exclusively to domestic producers." It now appears that subsidies may only take the form of direct cash payments to producers, in order to be compatible with GATT Article III:8(b). One effect is "that a serious look will have to be taken at the way financial help is granted to producers of cultural goods."¹⁰³ For example, cultural producers who often benefit from schemes such as tax remittance *e.g.*, film producers in Quebec, Ontario, Nova Scotia, and New Brunswick, could be significantly affected.¹⁰⁴ The film industry might be particularly vulnerable to WTO challenges on the issue of subsidies, as "the amounts given are sometimes quite important and of benefit to a limited number of producers"¹⁰⁵

D. Ultimate Significance

The crucial question raised by the WTO periodicals decision concerns what is to be done with the national treatment principle in instances where, for reasons not essentially economic, states do not want to treat foreigners the same way as nationals. The nascent WTO regime will be jeopardised if the perception is that nations have ceded to the WTO their sovereignty over issues at the core of national identity. In the long run, having these sorts of issues decided by third-

¹⁰² *Ibid.* at 7.

¹⁰³ *Ibid.* at 8.

¹⁰⁴ *Ibid.* at 8–9.

¹⁰⁵ *Ibid.* at 10.

party international tribunals may not be politically sustainable for domestic governments. With the restrictions placed on the definition of like products and on the way in which subsidies may be implemented, the net effect of the Canadian periodicals case is to establish that very little latitude exists for cultural protection in the WTO system.

V. CONCLUSION: POLICY OPTIONS FOR THE GOVERNMENT OF CANADA

The case makes clear that WTO rules prevent governments from using "culture" as a pretence for discriminating against imports.¹⁰⁶

—Charlene Barshefsky, United States Trade Representative

My view is that the WTO has not made a general pronouncement on protection and promotion of culture, in this case for Canada What they have said and ruled on is that the particular tool that we used infringed on our trading regime.¹⁰⁷

—Sergio Marchi, Canadian Minister for International Trade

WHEN THE WTO DISPUTE settlement process regarding Canadian periodical policies had run its course, all of Canada's measures which protected and supported domestic periodicals were found to contravene Canada's obligations as a member of the WTO. More than a complete rout of Canada's periodical policy framework, the decision considerably narrowed the latitude accorded states to undertake trade-related measures to promote domestic cultural goals.

The Canadian government has long-established commitments to open international trade, rules-based international dispute settlement, and the protection of Canadian culture. The WTO ruling exhibits an apparent contradiction between the first two commitments and the latter one. How should the Government of Canada deal with this policy quandary?

Complying with the decision presents domestic political difficulties. Canadian citizens have a very real interest in ensuring that Canadian culture is maintained and promoted through widely available, high quality, Canadian magazines. Cultural protectionism enjoys widespread support within Canada—the Canadian government knows that defending Canadian culture is popular with voters. Dismantling protective legislative framework at the WTO's behest would expose the government to criticisms of its inadequacy in protecting Canadian culture and the ceding of sovereignty to anonymous trade bureaucrats in Geneva. Cultural protection may also have ramifications in the national unity

¹⁰⁶ Quoted in L. Eggertson, "Trade body sinks magazine policy" *The Globe & Mail* (1 July 1997) A3.

¹⁰⁷ *Ibid.* at A3.

debate. If the government of Canada is not seen as a defender of culture even in the anglophone community, it will be hard pressed to explain to francophones how their culture can be maintained within Canada, let alone the world. The reasons for wanting to maintain protectionist periodical culture policies are powerful and valid.

Non-compliance with the ruling, however, is not a viable option. It should not be forgotten that the WTO dispute settlement procedures have served Canada well in the past when decisions have gone in Canada's favour.¹⁰⁸ As one of the world's major trading countries, Canada relies more on an open world trading system than do most other states. Not complying with the decision would compromise the internationalist economic principles Canada has adhered to for the past decade and make Canada a pariah state in the international trading system. This would damage its foreign commercial goodwill, and its image as a law abiding global citizen. It would also, according to WTO rules, permit the U.S. to take retaliatory action in the form of trade sanctions.¹⁰⁹ Canadians clearly have a stake in promoting respect for a rules-based international trading order which has proved a boon to the Canadian economy.

A. The Government's Response

1. Short-term Solutions

The WTO ruling does not automatically change the law in Canada. It merely states that Canada is not complying with its contractual obligations under the WTO agreements. Parliament must repeal or amend the existing legislation to ensure conformity with the WTO's ruling. Canada has notified the WTO that it will comply with the decision and bring its policies into conformance with Canada's international trade obligations.¹¹⁰

¹⁰⁸ These decisions related to the sale of Canadian bottled water in Korea, the marketing of Canadian scallops in France, the European Union's implementation of wheat concessions, and (with the U.S. and E.U. as co-complainants) to Japanese barriers to distilled liquor product imports. See "Promote Canadian Culture—But Play by the Rules," *The Financial Post* (23 January 1997) (visited 26 September 1997) <<http://www.sice.oas.org/root/forum/fp012397.htm>>.

¹⁰⁹ See *Dispute Settlement Understanding*, supra note 34 at Article 22.2. The Dispute Settlement Understanding requires that retaliatory actions take place within the same economic sector wherever possible. If this is not possible (which may very well be the case given the trade imbalance in cultural goods and services between Canada and the U.S.) the aggrieved country may cross-retaliate by applying sanctions to a different economic sector in the non-conforming country. This leaves open the possibility of an innocent industry group having to bear the brunt of the cost for policies designed to protect the cultural industries. See *Dispute Settlement Understanding*, supra note 34 at Article 22.3.4

¹¹⁰ L. Eggertson, "Ottawa vows to abide by WTO decision," *The Globe & Mail* (30 August 1997).

In the wake of the Appellate Body's decision, Heritage Minister Sheila Copps promised to introduce new periodical support measures at the resumption of the House of Commons in September 1997.¹¹¹ The new policies were not actually unveiled until July 1998, after significant lobbying of the Departments of Canadian Heritage and International Trade by the leading industry association representing Canadian periodical publishers.¹¹² The result is somewhat less than satisfactory. The Canadian government has agreed to eliminate all of the offending periodical policies, but has also announced its intention to erect a new policy in their place—one which appears unlikely to be trade law compatible.

In a joint press release, International Trade Minister Sergio Marchi and Canadian Heritage Minister Sheila Copps stated:

Canada will: ... remove the existing custom tariff prohibiting the importation of "split-run" magazines; eliminate the excise tax on "split-runs" distributed in Canada; restructure the administration of the postal subsidy program to conform to the rules on subsidies by making payments directly to magazine publishers; and harmonise the commercial and domestic postal rate for domestic and foreign publications.¹¹³

These moves, scheduled for completion in autumn of 1998, will bring Canada into concordance with the WTO regime. However, any peace they bring on the trade law front is unlikely to last, as a new scheme to support Canadian periodicals was also announced.

The new policy, to be introduced in the autumn of 1998, is known as "the advertising services measure," and will take the form of legislation designed to prevent foreign periodical publishers from selling advertising services directed at the Canadian market.¹¹⁴ The legislation will be designed to apply to the transaction of selling advertising and will use nationality of ownership criteria based on definitions similar to those contained in the *Income Tax Act*.¹¹⁵ As this proposed policy clearly runs contrary to the spirit of national treatment in GATT Article III, it appears that Canada will attempt to defend the measure—recycling the arguments it made concerning Part V.I of the *Excise Tax Act* on the grounds that the measure is aimed at a service, not a good. In other words, as it has not made specific commitments on advertising services under GATS,

¹¹¹ *Ibid.* at A3.

¹¹² See "WTO appeal denied" (1997), online: Canadian Magazine Publishers Association <http://www.cmpa.ca/newsnews.html> (date accessed: 10 October 1997).

¹¹³ Department of Foreign Affairs and International Trade, "New Advertising Services Measure to Promote Canadian Culture" (1997), online: Heritage Canada <http://www.pch.gc.ca/wn-qdn/culture/english.htm> (date accessed: 1 August 1998).

¹¹⁴ Department of Foreign Affairs and International Trade, "Backgrounder (2)" (1997), online: Heritage Canada <<http://www.pch.gc.ca/wn-qdn/culture/back2.htm>> (date accessed: 1 August 1998).

¹¹⁵ *Ibid.*

has not made specific commitments on advertising services under GATS, Canada is not obliged to provide national treatment to members of the WTO regarding an advertising-services related policy. There is little reason to believe that this argument, which has already failed at the panel and appellate levels, will succeed in the future. Accordingly, the new advertising services measure should be viewed as an attempt by Canada to buy time for Canadian publishers, rather than as a serious effort at policymaking. The U.S. has recognised this, and so it is safe to assume that the clash over Canadian periodical policies will continue.¹¹⁶

A better approach would have been to employ direct subsidies to support Canadian periodicals in the face of split-run competition and this more plausible option has been much discussed in the popular press.¹¹⁷ There is wide agreement among trade experts that Canada can subsidise magazines without contravening its trade obligations, provided that the subsidies conform with certain criteria.¹¹⁸

GATT Article III:8(b) exempts certain government subsidies from the application of the national treatment principle embodied in GATT Article III.¹¹⁹ In the periodicals case, Canada attempted to rely on this exemption regarding the funded postal rates provided through Canada Post. The Appellate Body ruled against these rates on the grounds that only the payment of subsidies involving the direct expenditure of revenue by a government, paid exclusively and directly to domestic producers are exempted from the application of Article III according to Article III:8(b). Provided that any new subsidies developed by Canada meet this requirement, it appears that they would be a workable, trade-law consistent, means of continuing to support Canadian periodicals.

Unfortunately, subsidies are considered to be a less desirable option from the standpoint of the periodical publishing industry. Journalists are concerned that subsidies could impugn, or be perceived as impugning, on journalistic integrity.¹²⁰ Publishers are concerned that subsidies are an unstable source of funding,¹²¹ which may be true in this era of fiscally-constrained governments.¹²²

¹¹⁶ A spokesperson for U.S. Trade Representative Charlene Barshefsky was quoted regarding the new measure: "[i]t has the same effect: US companies would be effectively prohibited from competing in the [Canadian] marketplace." See H. Scofield, "U.S. rejects Ottawa's new magazine policy" *The Globe & Mail* (30 July 1998) A1.

¹¹⁷ See e.g. "Promote Canadian Culture—But Play by the Rules," *supra* note 108.

¹¹⁸ See *Bernier*, *supra* note 32 at 8.

¹¹⁹ See *supra* note 69 at Article III:8(b).

¹²⁰ Confidential telephone interview with Canadian Magazine Publishers Association staff-member (27 October 1997).

¹²¹ *Ibid.*

The relative transparency of subsidies may also mean that fiscally constrained citizens will find them objectionable—tax dollars supporting periodicals which they themselves do not read. In spite of their flaws, subsidies remain preferable to the proposed new advertising services measure. In the absence of financial support, many financially marginal Canadian periodicals may see substantial declines in quality or may cease production altogether.

2. Long Term Solutions

The tension between Canada's international trade policies and nationalist cultural policies cannot be eliminated by favouring one commitment over the other. Rather, resolving Canada's culture/trade dichotomy will require creativity on the part of the Canadian government in devising new GATT-consistent instruments for supporting Canadian magazines, and in developing a more robust policy for mediating the interplay between trade and culture.

The periodicals case is just another dramatic chapter in a series of spats over culture between Canada and the U.S. But this case has departed from previous experience in the recourse to the WTO. The U.S. clearly intends to use it as a demonstration to Canada and other nations that it is taking a hard line against barriers to trade based on cultural measures.¹²³ Given the success it has had with Canadian periodical measures, there is little reason for the U.S. not to continue using the WTO mechanisms to assault other barriers to trade erected in the name of cultural protection.¹²⁴ As one commentator put it, "Washington, no doubt, will keep fighting to treat culture like widgets."¹²⁵ To the extent that Canada does not want culture treated in this way, it is absolutely necessary to develop a long-term resolution to the tension between trade and culture.

It is now widely recognised that states can no longer decide domestic policy issues in isolation and "remain behind borders and regulate their economies as if

¹²² The WTO Trade Policy Review for Canada noted in late 1996 that: "... [g]overnment spending on culture is to decline over the coming years as a result of budgetary consolidation. Spending by the Department of Canadian Heritage and related agencies is to be phased down by \$676 million over three years, starting in 1995/96." As Canadian Heritage would be the likely source of any potential direct subsidies, the long-term sustainability of subsidies is questionable. See *WTO*, *supra* note 4 at 122, 123.

¹²³ As then U.S. Trade Representative Mickey Kantor said during a March 1996 press conference announcing the launch of the U.S. complaint against Canada to the WTO, the case was: "important in setting a clear precedent that the United States is prepared to act on so-called cultural issues where there is a discrimination against U.S. interests. The Clinton Administration is committed to combating the growing attack on our country's publishing and entertainment industries, whether from Canada, Europe or Asia." See Atkey & Young, *supra* note 38 at 22.

¹²⁴ See Acheson & Maule, *supra* note 31 at 79.

¹²⁵ See "Culture Fight Isn't Over" *The [Montreal] Gazette* (21 January 1997) B2.

the rest of the world does not exist."¹²⁶ Retreating from the current level of international engagement is neither desirable, nor possible. Therefore, what Canada must do is take the opposite approach—engage the WTO directly on the issue of trade and culture. There are three possible options for doing this: first, open completely Canada's cultural industries to international competition; second, follow the examples set by the FTA and NAFTA in negotiating cultural exemptions within the WTO agreements; or third, pursue a comprehensive agreement within the WTO framework, focusing explicitly on disciplines relating to culture and trade.

The first approach has been proposed by Acheson and Maule, two Canadian academics whose work has been quoted favourably by Canada's former Minister for International Trade.¹²⁷ They have argued persuasively in relation to other cultural industries, such as television, that an open regime would better serve Canadian interests than the current nationalist regime.¹²⁸ They believe that Canada's protectionist culture policies have served only to embroil Canada in trade disputes and retaliatory measures and argue that Canadian culture would be more creative and internationally commercially competitive in the absence of protection.¹²⁹

Acheson and Maule may be correct in regard to many Canadian films, television programs, sound recordings, novels, and even some periodicals. It cannot, however, be denied that many Canadian periodicals have Canada-specific content that will not gain a global audience of significant commercial value so as to offset the advertising revenue lost through the entry of split-runs into the Canadian marketplace. The same reasoning would apply to various other forms of audio, print, or video displaying cultural and political commentary which would not have a market outside of Canada. It remains clear that some form of continued support for Canadian periodicals, as well as certain other outputs of the cultural industries, will remain necessary and that simply opening-up Canada's cultural industries to world competition will not meet Canada's needs.

The second approach, that of negotiating cultural exemption clauses within the WTO Agreements, is also unpromising. This approach has been the prevailing orthodoxy—Canada has negotiated cultural industries exceptions in four bilateral investment agreements over the past few years,¹³⁰ and the Canada-

¹²⁶ D.M. McRae, "From Sovereignty to Jurisdiction: The Implications for States of the WTO" (paper presented at Centre for Asia-Pacific Initiatives conference, *The Asia-Pacific Region and the Expanding Borders of the WTO: Implications, Challenges and Opportunities* (Vancouver, 1996)[unpublished] at 16.

¹²⁷ See Eggleton, *supra* note 1.

¹²⁸ See generally Acheson & Maule, *supra* note 31 at 65–81.

¹²⁹ *Ibid.* at 6.

¹³⁰ See Bernier, *supra* note 32 at 22.

U.S. FTA and the NAFTA both contain cultural exemption clauses.¹³¹ Canada has also said it will negotiate cultural exemptions to the Multilateral Agreement on Investment being negotiated among Organization for Economic Cooperation and Development states.¹³² Unfortunately, there are signs that exemptions do little to protect cultural policies from attack.

Acheson and Maule have argued in the case of the FTA and the NAFTA that,

[R]ather than insulating Canada from disputes, the exemption will act as a lightning rod by encouraging strategically motivated complaints, as the United States has an interest in overloading the informal process of dispute arbitration.¹³³

Part of the problem is with the wording of the clauses themselves. While both Canada and the U.S. read the FTA clause in the same way, the NAFTA clause is interpreted differently. Both countries believe that the FTA provision allows the U.S. to retaliate, should it suffer any economic harm resulting from a Canadian cultural industry measure taken in derogation of the other clauses of the FTA, and the U.S. believes the same interpretation should be applied to the clause in NAFTA.¹³⁴ Canada, however, takes the position that only FTA "obligations are subject to the derogation-and-right-of-retaliation scheme."¹³⁵ The NAFTA example seems to demonstrate that there is too much room for con-

¹³¹ See *Canada-United States Free Trade Agreement Implementation Act*, R.S.C. 1988, c.65 at Articles 2005(1), 2005(2). See also *N.A.F.T.A.*, *supra* note 32 at Article 2106, Annex 2106, & Article 2107.

¹³² See Department of Foreign Affairs and International Trade, *Facts on the MAI* (visited 15 November 1997) <www.dfait-maeci.gc.ca/english/trade/keyansw2-e.htm>. The primary purpose of the Multilateral Agreement on Investment is to provide an investment climate where foreign investors will not be subject to discriminatory treatment or uncompensated nationalisation of assets. Many Canadians are concerned, however, that in seeking this goal the MAI will result in substantial limitations on Canadian cultural policy as Canadians are forced to treat foreign and Canadian cultural industry investors in the same way. Making an assessment of the MAI's impact on cultural policies is difficult at this point, as much of the content of the deal is still under negotiation. The MAI may be limited by specific exceptions or reservations claimed in advance by individual countries in particular sectors. Canada has supported a proposal by France to introduce "a broad cultural exemption into the MAI." See S. McCarthy, "Get ready. Another trade agreement is coming down the pike" *The Globe & Mail* (29 November 1997) D1.

¹³³ K. Acheson & C.J. Maule, "Canada's Cultural Exemption: Insulator or Lightning Rod?" (1996) 20:1 *World Competition* at 4.

¹³⁴ This view was expressed by then U.S. Trade Representative Carla Hills in the Congressional debates and Senate Finance Committee hearings preceding NAFTA's adoptions in the US, and by American private sector trade policy advisory committees. See Ragosta, Magnus & Shaw, *supra* note 33.

¹³⁵ *Ibid.*

flicting interpretations when cultural exemptions are used.¹³⁶ As one commentator has noted regarding the NAFTA cultural exemptions:

While the NAFTA contains a cultural industries exemption, its effect may be seen to be more diplomatic in nature than legal. Since the exemption does not protect a Party from retaliation for relying upon it, it provides little actual protection for a Party's cultural industries.¹³⁷

Nor is there any evidence of widespread support for cultural exemptions within the WTO framework. Early in the Uruguay Round negotiations, Canada had argued for the inclusion of a general cultural exception clause in the GATS covering all cultural services, but had then "dropped the idea for lack of support."¹³⁸ Likewise, an E.U. proposal made towards the end of the negotiations relating to audio-visual services was also unsuccessful.¹³⁹ The issue of culture was handled in the G.A.T.S. indirectly. Although there is no *prima facie* distinction between cultural services and other services in the GATS, states can limit their undertakings in an economic sector by avoiding "specific commitments" regarding that sector. Very few countries have made specific commitments concerning culture, and Canada itself has certainly not done so.¹⁴⁰ But, as the WTO periodicals case has demonstrated, neither the exemptions of NAFTA, nor the non-commitment in G.A.T.S. shielded Canada's advertising taxation policies at the WTO.

The third option is to take a pro-active approach, and negotiate a comprehensive agreement within the WTO on disciplines relating to trade and investment in cultural goods and services. This approach is based on the premise that cultural industries are not monolithic—some are appropriate for open international competition, while others are not. The agreement would require countries to negotiate which cultural industries or elements of those industries would be exempted from aspects of other WTO Agreements. It would codify those measures available to support cultural industries.

The time for commencing this undertaking may be propitious, as the world trading system is currently in a state of minor disorder due to a lack of leadership on the part of the United States. Congress remains somewhat isolationist, and it is uncertain whether the current or the next administration will acquire the fast-track negotiating authority necessary to participate in international

¹³⁶ It may very well have been the case that without these conflicting interpretations it would have been impossible to include a culture clause in the Agreement.

¹³⁷ B. Appleton, *Navigating NAFTA: A Concise User's Guide to the North American Free Trade Agreement* (Scarborough, Ont.: Carswell, 1994) at 191.

¹³⁸ See Bernier, *supra* note 33 at 15.

¹³⁹ *Ibid.*

¹⁴⁰ *Ibid.* at 16, 17.

talks.¹⁴¹ In the absence of American initiative, the situation is much more fluid and there is greater latitude for middle powers, such as Canada, to have an impact on setting the negotiating agenda.¹⁴² Canada has a window of opportunity to start building alliances to generate support for negotiations on trade related aspects of cultural industries.¹⁴³

The international trading system cannot be ignored in the name of defending culture. Canada is a nation that enjoys great benefits from its international involvement, both economically and culturally. It should, however, be recognised that cultural industries have unique characteristics that require a unique approach. Other sensitive industries also claim to be exceptional, such as communications, air and maritime transport, oil, gas, and uranium.¹⁴⁴ Unlike these industries, and unlike others whose relationship to international trade is also contentious, such as environmental and health regulation, cultural industries contain an inherently unquantifiable aspect.¹⁴⁵ Culture is the product of cultural industries, but has an emotional value that goes beyond dollars and cents, ideology, international law, or economic theory. Culture goes to the core of the human experience. Protecting the industries that produce national culture will require Canada to stand up and state that culture is something to which we simply do not want to accord national treatment, and not because of any economic chauvinism on our part. Rather, it is because of culture's inherent yet immeasurable value to our national project.

The multilateral rules-based trading system can ignore the resonance of cultural issues only at its peril. Nations will become increasingly isolationist to the extent that matters of vital national interest and identity will seem to be decided upon by third-party decision-makers. Accordingly, a degree of protec-

¹⁴¹ P. Knox, "Fast-track collapse 'nasty setback'" *The Globe & Mail* (12 November 1997) A12.

¹⁴² American isolationism may also have the benefit of encouraging Canada and other countries to enter into bilateral trade agreements. See "Profiting from Washington's myopia *The Globe & Mail*" (12 November 1997) A24. To the extent that Canada can negotiate broad, comprehensive cultural protections in these agreements, Canada will be able to pursue the same goal with more force in future multilateral negotiations.

¹⁴³ France would be an obvious partner in this regard. Commonwealth countries might also be interested, as English speaking countries have a mutual concern about the maintenance of distinct cultures due to the absence of the natural barrier of language ameliorating somewhat the onslaught of American cultural products. The countries that have failed to make specific commitments regarding cultural industries under the GATS would be further targets for consensus-building Canadian diplomatic efforts.

¹⁴⁴ These industries have been exempted in principle from the application of the FTA and NAFTA. See WTO, *supra* note 4 at 119.

¹⁴⁵ Things such as air quality or food safety can to some degree be scientifically debated (although political values will inform the debate). Things of a cultural nature, however, are essentially contestable and vain attempts by social scientists notwithstanding, will likely prove impervious to scientific measurement.

tion for cultural industries remains desirable, although not blanket exemptions from trade disciplines. Some competition for certain aspects of the cultural industries may very well be positive, but others may be more dependent on shelter from the exigencies of the market. A multilateral agreement specifying which aspects of which industries may be protected, and how they may or may not be protected, will help ensure that the multilateral trade system is politically sustainable in the long term. It would be a mistake to treat culture as an area too complex or contentious to allow arrival at agreement on the matter. The entire history of the GATT/WTO system proves that broad disagreements and entrenched interests in complex areas can be overcome to arrive at binding multilateral agreements. In the area of culture, all that is required is political will.

