Agreement on Internal Trade

Report of the Article 1704 Panel Concerning the Dispute Between Nova Scotia and Prince Edward Island Regarding Amendments to the *Dairy Industry Act Regulations*

January 18, 2000

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1. BACKGROUND

In October, 1996, Farmers Cooperative Dairy Limited (*Farmers*) of Bedford, Nova Scotia acquired Health Pasteurized Milk Limited (*Health*) of Hunter River, P.E.I. by way of a share purchase. At the time of the purchase, Health had licenses which allowed it to manufacture dairy products and process certain fluid milk products in Prince Edward Island.

During the Fall of 1997, some of the equipment in the Health plant used for packing milk stopped working and was deemed non-repairable. At this time Health began to distribute an increased amount of Farmers fluid milk and cream products made in Nova Scotia under the Farmers label. As well, Health began to purchase Farmers fluid milk products processed in Nova Scotia, and sell them as "Elmers" and "Health" labelled products in P.E.I. As part of its corporate strategy, Farmers rationalized product lines between the two plants.

On November 27, 1997, following several months of review, Prince Edward Island (*Respondent*) introduced amendments to the *Dairy Industry Act Regulations* by way of P.E.I. Regulation EC665/97. The amendments revoked existing licenses for dairy processors and distributors in Prince Edward Island during the current licensing year, and mandated a re-application for processors and distributors for the remainder of the licensing year. The amendments also specified that the Department of Agriculture and Forestry (the *Department*) would not issue a license unless it was “in the best interests of the general public or the dairy products trade”.

Also on November 27, 1997, Respondent issued a letter to Farmers ordering it to remove its Class I milk products from the P.E.I. market.

On December 31, 1997, both Health and Farmers applied for new licenses under the amended regulations. In January, 1998, licenses to distribute specified fluid milk products were issued to both companies, and both licenses allowed for the distribution of Farmers products. However, an attachment to these new licenses contained an explicit directive for the removal of specified unlicensed products from the Prince Edward Island market. The products which the companies were not permitted to distribute were sourced in Nova Scotia.

In February, 1998, Farmers was granted an injunction against the Department enjoining it from removing Farmers’ product from the P.E.I. market. The injunction was revoked in April 1998, resulting in Farmers entering into a co-packaging arrangement with another P.E.I. dairy for some of the noncompliant products. This co-packaging arrangement has resulted in additional expenditures for the company.

In April 1998, Farmers initiated steps to pursue a complaint under the *Agreement on Internal Trade* (the *Agreement*).

2. NATURE OF THE COMPLAINT

Nova Scotia (*Complainant*) alleges that the amended *Regulations* fail to comply with the Respondent's obligations under the *Agreement*, and that the inconsistencies cannot be justified by reference to any provision contained within the *Agreement*. Specifically, Complainant alleges that Respondent applied these regulations to exclude products from other provinces in a manner that is not consistent with the *Agreement*.

Complainant alleges that EC665/97 is inconsistent with the following provisions of the *Agreement*:

Article 100 (Objective)

Article 101 (Mutually Agreed Principles)

Article 401 (Reciprocal Non-Discrimination)

Article 403 (No Obstacles)

Article 404 (Legitimate Objectives)

Article 900 (Application of General Rules)

Article 902.3 (Scope and Coverage)

Annex 902.5 (Reports on Measures That May Affect Internal Trade)

Article 905 (Non-Sanitary and Non-Phytosanitary Measures)

Article 907 (Transparency)

Respondent maintains that EC665/97 is consistent with all provisions of the *Agreement*, including those listed by Complainant and Article 402 (Right of Entry and Exit) and 405 (Reconciliation).

3. PANEL AUTHORITY

This Panel was convened pursuant to the terms of the *Agreement*. Parties agreed that the Panel was properly constituted and had jurisdiction to hear the dispute.

Article 1705 of the *Agreement* states that the Panel shall "examine whether the actual or proposed measure or other matter at issue is or would be inconsistent with the *Agreement*."

Article 1707.2 provides that the Panel report "shall contain:

(a) findings of fact;

(b) a determination, with reasons, as to whether the measure in question is or would be inconsistent with this Agreement;

(c) a determination, with reasons, as to whether the measure has impaired or would impair internal trade and has caused or would cause injury; and

(d) recommendations, if requested by a disputing Party, to assist in resolving the dispute."

4. COMPLAINT PROCESS

On September 23, 1998, at the request of Farmers, Complainant requested consultations with Respondent in accordance with Article 906 (Consultations) of the *Agreement*.

Chapter Nine (Agricultural and Food Goods) consultations were initiated on November 9, 1998, six days after the 40-day period for consultations under Chapter Nine had expired.

On January 7, 1999, Complainant and Respondent made a joint request for the assistance of the Internal Trade Secretariat in resolving the dispute. The Secretariat facilitated a series of meetings between Complainant, Respondent and Farmers on February 15 and 16, 1999.

Consultations were unsuccessful, and on April 29, 1999 Complainant requested consultations under Chapter 17. No face-to-face consultations were held. The 40-day consultation period under Article 1702 (Consultations) expired on June 9, 1999.

On June 14, 1999, Complainant requested the Assistance of the Committee on Internal Trade. On the same day, but independently of Complainant's request, Respondent requested the Assistance of the Committee. The Committee met by teleconference on July 5, 1999.

The 50-day assistance period specified in Article 1703 (Assistance of Committee) expired on August 4, 1999. Complainant requested the establishment of a Panel under Article 1704 (Request for Panel) of the *Agreement* on August 5, 1999.

A pre-hearing conference was held on October 20, 1999, to receive presentations from Complainant and Respondent on the form of the hearings and materials to be submitted. This hearing provided the disputants with an opportunity to raise procedural issues.

A hearing was held in Halifax on December 8, 1999.

5. CHAPTER ONE (OPERATING PRINCIPLES)

"**Article 100: Objective**

It is the objective of the Parties to reduce and eliminate, to the extent possible, barriers to the free movement of persons, goods, services and investments within Canada and to establish an open, efficient and stable domestic market. All Parties recognize and agree that enhancing trade and mobility within Canada would contribute to the attainment of this goal.

Article 101: Mutually Agreed Principles

1. This Agreement applies to trade within Canada in accordance with the chapters of this Agreement.

2. This Agreement represents a reciprocally and mutually agreed balance of rights and obligations of the Parties.

3. In the application of this Agreement, the Parties shall be guided by the following principles:

(a) Parties will not establish new barriers to internal trade and will facilitate the cross-boundary movement of persons, goods, services and investments within Canada;

(b) Parties will treat persons, goods, services and investments equally, irrespective of where they originate in Canada;

(c) Parties will reconcile relevant standards and regulatory measures to provide for the free movement of persons, goods, services and investments within Canada; and

(d) Parties will ensure that their administrative policies operate to provide for the free movement of persons, goods, services and investments within Canada.

4. In applying the principles set out in paragraph 3, the Parties recognize:

(a) the need for full disclosure of information, legislation, regulations, policies and practices that have the potential to impede an open, efficient and stable domestic market;

(b) the need for exceptions and transition periods;

(c) the need for exceptions required to meet regional development objectives in Canada;

(d) the need for supporting administrative, dispute settlement and compliance mechanisms that are accessible, timely, credible and effective; and

(e) the need to take into account the importance of environmental objectives, consumer protection and labour standards."

Respondent submits that Article 101.4(b) implies that the drafters of the *Agreement* recognized that there was a need for transition periods to bring non-conforming measures into conformity with the *Agreement*. Respondent submits that, even if its fluid milk distribution measures are not consistent with the *Agreement*, they are protected during the transition period identified in Article 101.4(b). As transition periods for specific measures are listed in Chapters Four through Fifteen, this argument is dealt with in the section reviewing Chapter Nine.

While the *Agreement* provides transition periods for existing trade barriers, there is a prohibition against establishing new trade barriers inconsistent with the *Agreement*.

In developing this *Agreement*, the federal, provincial and territorial governments were determined to enhance and expand the domestic market and thereby strengthen the economic union. This process required both the reduction and eventual elimination of existing barriers and an undertaking not to introduce new barriers to internal trade.

Article 100 reflects this undertaking. Article 101.2 emphasizes that the mutually agreed balance of rights and obligations of the Parties to the *Agreement* are reciprocal, while Article 101.3 contains a commitment that new barriers will not be established. Article 101.4 recognizes factors that the Parties should consider in pursuing the objectives.

In addition to the broad statement of principles contained in Article 101, several specific conditions must be noted in that Article. While the principles are a guide to policy-makers and dispute resolution panels, the rules governing this dispute are set out in Chapters Four and Nine.

6. ARTICLE 200: DEFINITIONS OF GENERAL APPLICATION

Respondent submits that the measure under dispute is the amendment to the *Dairy Industry Act Regulations* (EC665/97), and that EC665/97 is trade-neutral. Respondent asserts that Complainant has not identified any language in EC665/97 that restricts trade in fluid milk.

Respondent concedes that the policy used by P.E.I. regulators to apply EC665/97 constitutes a trade barrier. However, Respondent argues that:

1. Complainant alleges that the breach of the *Agreement* is caused by C665/97, not the policy upon which the regulation is based;

2. the P.E.I. policy on fluid milk distribution has been unchanged for a number of years, predating the September 1, 1997 inclusion of fluid milk standards and distribution in the scope and coverage of Chapter Nine, and is therefore grandfathered under the *Agreement*; and

3. there are better methods of addressing the issue of restrictions on interprovincial trade in fluid milk than the Chapter 17 dispute resolution process.

Complainant notes that the definition of “measure” in the *Agreement* includes “any . . . directive, requirement, guideline, program, policy, administrative practice or other procedure”. Complainant submits that the term covers both the regulation and measures adopted in the application of the regulation. Complainant argues that a Party cannot circumvent the provisions of the *Agreement* by passing a trade-neutral regulation granting broad discretionary authority to the Minister or the Department, and subsequently using that authority in a discriminatory manner.

With respect to the first issue raised by Respondent, the Panel finds that the definition of “measure” in Article 200 is sufficiently broad to cover both EC665/97 and the policy

upon which that regulation is based. The application of a policy cannot be divorced from the policy itself.

The remaining issues raised by Respondent are matters of substance rather than definition and will be dealt with later in this report.

7. CHAPTER THREE (CONSTITUTIONAL POWERS AND RESPONSIBILITIES)

"**Article 300: Reaffirmation of Constitutional Powers and Responsibilities)**

> Nothing in this Agreement alters the legislative or other authority of Parliament or of the provincial legislatures or of the Government of Canada or of the provincial governments or the rights of any of them with respect to the exercise of their legislative or other authorities under the Constitution of Canada."

While the *Agreement* confirmed constitutional powers, Parties to the *Agreement* undertook to constrain the exercise of these powers in support of cooperative federalism. By entering into the *Agreement*, Parties agreed that past legislative or policy action may no longer be appropriate. Changes to actions that are constitutionally valid but inconsistent with the *Agreement* may be required.

Reflecting the terms of the *Agreement*, trade legislation must meet two tests: 1) is the legislation within the constitutional authority of the Party; and 2) is the legislation consistent with the *Agreement*? These tests are similar to those adopted by the MMT Panel in its report dated June 12, 1998.

Respondent argues that it acted within its constitutional authority to regulate intraprovincial distribution of fluid milk when it passed EC665/97. While it is agreed that such regulation is within the constitutional authority of Respondent, the fact remains that Respondent is Party to the *Agreement* now in place, and it has the corresponding obligation to ensure that its actions recognize the objectives, principles and commitments included in that *Agreement*. A Party that chooses to exercise its constitutional authority in a manner which conflicts with the *Agreement* must accept that there will be consequences of that choice, as specified in Chapter 17.

8. CHAPTER NINE (AGRICULTURAL AND FOOD GOODS)

"**Article 900: Application of General Rules**

> For greater certainty, Chapter Four (General Rules) applies to this Chapter, except as otherwise provided in this Chapter."

Both disputants agree that Article 900 provides that the General Rules contained in Chapter Four apply to measures covered by Chapter Nine.

> "**Article 901: Relationship to Other Chapters**
>
> In the event of an inconsistency between a provision of this Chapter and any other provision of this Agreement, this Chapter prevails to the extent of the inconsistency."

Respondent concedes that there is no inconsistency between the General Rules contained in Chapter Four and the specific rules in Chapter Nine, and therefore Article 901 (Relationship to Other Chapters) is not an issue in the present case.

> "**Article 902: Scope and Coverage**
>
> 3. Measures involving technical barriers with policy implications shall be included in the scope and coverage of this Chapter effective September 1, 1997. The Federal-Provincial Trade Policy Committee (the "Trade Policy Committee") shall, on or before September 1, 1997, give written notice to the Committee on Internal Trade of such measures.
>
> 5. Other measures that may affect internal trade and that are adopted by the Ministers in accordance with the process set out in Annex 902.5 shall be included in the scope and coverage of this Chapter effective on the date of their adoption.
>
> **Annex 902.5: Reports on Measures That May Affect Internal Trade**
>
> 6. The Ministers shall, within the framework of their review of Canadian agri-food policy, direct their respective officials to establish industry consultation and review work programs for the purpose of jointly preparing reports and recommendations in relation to the measures agreed to by the Ministers, in accordance with the record of decision of their meeting held on July 4-6, 1994.
>
> 7. Subject to any changes that may be agreed to by all Parties, the Parties shall adopt, with an effective date no later than September 1, 1997, the measures referred to in paragraph 6 and the recommendations made in relation to those measures that are contained in the reports prepared under that paragraph."

The disputants agree that the October 1, 1997 letter from Michael Gifford and John Schildroth, co-chairs of the Federal-Provincial Agricultural Trade Policy Committee, to the co-chairs of the Committee on Internal Trade (Appendix D), meets the requirements of Article 902.3, and that measures respecting fluid milk standards and distribution are covered by Chapter Nine.

Complainant submits that measures respecting fluid milk standards and distribution in effect on September 1, 1997 are covered by Chapter Nine, by virtue of Article 902.3. Complainant argues that Respondent's legislation, regulations, policies and administrative practices respecting fluid milk standards and distribution in existence on September 1, 1997 are subject to the provisions of the *Agreement*.

It is Respondent's position that a transition period of unspecified length began on September 1, 1997. In support of this position, Respondent notes the widespread non-compliance with the *Agreement* across economic sectors.

Relative to the language of Annex 902.5, paragraphs 6 and 7, Respondent submits that the Parties were required to have adopted recommendations on specific measures by

September 1, 1997, but were not required to have made legislative or regulatory changes by that date.

The Panel is unable to adopt this position. Article 902.5 states that "Other measures that may affect internal trade and that are adopted by the Ministers in accordance with the process set out in Annex 902.5 shall be included in the scope and coverage of this Chapter effective on the date of their adoption." (emphasis added)

The language of the *Agreement* is clear - existing measures respecting fluid milk standards and distribution must conform to the provisions of Chapter Nine on September 1, 1997. The Panel notes that fluid milk distribution was not subject to the provisions of the *Agreement* until September 1, 1997, which provided a 26-month transition period since the coming-into-force of the *Agreement*.

Having determined that existing measures are covered, the question of whether the amendments made to the *Dairy Industry Act Regulations* constitute a new measure is moot, and the Panel is not required to make a determination relative to Article 905.

9. ARTICLE 401: RECIPROCAL NON-DISCRIMINATION

> "1. Subject to Article 404, each Party shall accord to goods of any other Party treatment no less favourable than the best treatment it accords to:
>
> (a) its own like, directly competitive or substitutable goods; and
>
> (b) like, directly competitive or substitutable goods of any other Party or non-Party."

The Panel noted that the report of a previous panel dated June 12, 1998, dealing with a ban on interprovincial trade in the gasoline additive MMT, established that two factors must be considered in determining whether a measure is inconsistent with Article 401:

1. Does the measure discriminate against the goods of one Party to the benefit of the goods of another Party?

2. Are the goods discriminated against "like, directly competitive or substitutable" with the goods of another Party?

This panel adopts the same criteria in the present case.

In the MMT report, the Panel concluded that there must be a geographical component to the discrimination for a measure to be inconsistent with Article 401.3. This geographical component can be direct, where goods from one Party are favoured over identical goods from another Party, or indirect, where goods produced predominately in the territory of one Party are favoured over directly competitive or substitutable goods produced predominately in the territory of another Party.

In the present case, Respondent admitted that the reason Health was not licensed to import specified fluid milk products from Nova Scotia was based on geography. Indeed, Respondent admitted that geography was the fundamental factor in the withdrawal of the license for certain products. Respondent stated that P.E.I. regulators interpreted the phrase "in the best interest of . . . the dairy products trade" contained in EC665/97 to mean "in the best interest of Prince Edward Island dairy processors". Respondent noted that the only fluid milk imports allowed were products that did not compete with P.E.I.-produced products.

Neither disputant produced any evidence to suggest that fluid milk products from Nova Scotia were not "like, directly competitive or substitutable" with P.E.I. fluid milk products. Respondent did not invoke the Legitimate Objectives test contained in Article 404, and conceded that it did not have any health, safety or consumer concerns about fluid milk products from Farmers.

Having failed both parts of the test outlined above, this Panel concludes that the measure in dispute is inconsistent with Article 401.

10. ARTICLE 402: RIGHT OF ENTRY AND EXIT

> "**Article 402: Right of Entry and Exit**
>
> Subject to Article 404, no Party shall adopt or maintain any measure that restricts or prevents the movement of persons, goods, services or investments across provincial boundaries."

Respondent argues that EC665/97 itself is consistent with Article 402, in that it is trade-neutral, and therefore it is not necessary to invoke the Legitimate Objectives test contained in Article 404. Respondent concedes that the long-standing policy of the Government of Prince Edward Island to restrict the importation of fluid milk products that compete with P.E.I. products is a barrier to trade, but argues that this policy is not included in the measure complained of by Complainant.

Complainant did not raise the issue of Article 402. However, Complainant did argue that the measure in dispute includes the policy applying EC665/97, and that since September 1, 1997 any regulation or policy respecting fluid milk distribution must be consistent with the *Agreement*.

The Panel has found that the measure in dispute includes both the policy and the regulation, and has found that measures in force on September 1, 1997 must be consistent with the *Agreement*. The Panel concludes that the long-standing policy of Respondent, which Respondent has admitted, to restrict the importation of fluid milk products that compete with P.E.I. products restricts the movement of goods across a provincial boundary, and therefore EC665/97 is inconsistent with Article 402.

11. ARTICLE 403 : NO OBSTACLES

"**Article 403 : No Obstacles**

Subject to Article 404, each Party shall ensure that any measure it adopts or maintains does not operate to create an obstacle to internal trade."

Respondent argues that the measure is consistent with Article 403, in that EC665/97 is trade-neutral, and therefore it is not necessary to invoke the Legitimate Objectives test contained in Article 404. Respondent concedes that the long-standing policy of the Government of Prince Edward Island to restrict the importation of fluid milk products that compete with P.E.I. products is a barrier to trade, but argues that this policy is not included in the measure complained of by Complainant.

Complainant argues that the measure in dispute includes the policy applying the regulation, and that since September 1, 1997 any regulation or policy respecting fluid milk distribution must be consistent with the *Agreement*. It is Complainant's position that, if EC665/97 is a new measure, it violates Article 403's provision against adopting a measure that operates to create an obstacle to internal trade. Alternatively, if the effect of EC665/97 was intended to codify an existing measure, it violates Article 403's provision against maintaining a measure that operates to create an obstacle to internal trade.

Having found that the measure in dispute includes both the policy and the regulation, and having found that measures in force on September 1, 1997 must be consistent with the *Agreement*, the Panel concludes that EC665/97 is not consistent with Article 403.

12. DETERMINATION OF INJURY

While the issue of injury was conceded, the Parties disagreed about the level of injury, and the Panel has insufficient evidence to assess the level of injury.

13. OTHER CONSIDERATIONS

A. Regional Harmonization

Respondent states that, while its policy is a barrier to trade, there are better ways of addressing the issue than through a Chapter 17 dispute. Specifically, Respondent asserts that regional harmonization negotiations could lead to a satisfactory resolution of the issue.

Complainant agrees that regional harmonization talks are a useful exercise, but states that the fact Parties are involved in comprehensive negotiations does not preclude a Party or private person from seeking redress through Chapter 17.

The Panel finds that the right of a Party or private person to pursue redress pursuant to Chapter 17 of the *Agreement* is not abridged by the fact multilateral negotiations related to the specific issue are ongoing.

The MMT Panel noted that a panel finding that a measure is inconsistent with the *Agreement* does not preclude further multilateral negotiations to resolve outstanding harmonization issues in conformance with the *Agreement*. This Panel concurs with the MMT Panel's observation.

B. National Policy Implications

The Panel heard arguments that Respondent's policy respecting the importation of fluid milk was not dissimilar from the policies of other governments in the region, or from other governments across Canada. Respondent suggests that it would be unfair to determine that it was in breach of the *Agreement* while ignoring the policies of other governments, including the policies of Complainant. Complainant concedes that its measures regarding fluid milk distribution are not consistent with the *Agreement*.

The mandate of a Chapter 17 panel is to determine "whether the actual . . . measure or other matter at issue is . . . inconsistent with the *Agreement*." A panel does not have the mandate to examine broader issues of harmonization or intergovernmental cooperation, or to ignore provisions of the *Agreement* on the basis that they are widely violated.

The Panel anticipates that, where there is a determination that there has been a breach of the *Agreement*, other Parties with similar measures would note the Panel findings and act to make such measures consistent with the *Agreement*.

The mandate of this Panel is to determine whether Respondent's fluid milk distribution measures are consistent with the provisions of the *Agreement*.

The Panel is not blind to the fact that fluid milk distribution issues have regional and national implications. The Panel notes that the *Agreement* has been in force for more than four and one-half years. Fluid milk distribution measures have been subject to the *Agreement* for more than two years, yet the Parties to the *Agreement* have failed to negotiate a harmonized solution to the issue. Ministers of Agriculture agreed to complete a review of the scope and coverage of Chapter Nine by September 1, 1997, but issues remain unresolved.

Using the *Agreement's* dispute resolution procedures may result in a solution that is less comprehensive than multilateral negotiations. However, the rights of a Party or private person under the *Agreement* cannot be abridged by ongoing negotiations.

14. PANEL DETERMINATION

The Panel finds that Respondent's amendment to the *Dairy Industry Act Regulations* (P.E.I. Regulation EC665/97), as well as the policies, procedures and practices to implement those regulations, are inconsistent with Articles 401, 402 and 403 of the *Agreement*.

The Panel also finds that Respondent's amendment to the *Dairy Industry Act Regulations* (P.E.I. Regulation EC665/97), as well as the policies, procedures and practices to implement those regulations, are inconsistent with Articles 900, 901, and Annex 902.5.

The Panel finds that the transitional provisions of the *Agreement* do not provide a defence for the measure Respondent adopted relative to the distribution of fluid milk products.

The Panel recommends that Respondent take whatever steps are necessary to assure that the application of the *Regulations* respecting fluid milk standards and distribution are consistent with the provisions of the *Agreement*.

Pending such action, the Panel recommends that Respondent remove from all existing licenses conditions relating to the distribution of fluid milk products based on province of origin for goods or on residency for ownership.

Respondent made reference to the need for harmonization with the regulatory regimes of other Parties to the *Agreement*. It is open to Respondent and other Parties to the *Agreement* to seek resolution of the outstanding harmonization and regulatory issues in conformance with the provisions of the *Agreement*. The Federal-Provincial Agricultural Trade Policy Committee can be a useful forum for discussion and resolution of these issues. The Panel would encourage such resolution, although implementation of the Panel recommendations should not be dependent on this resolution.

Costs

Rule 52 of Annex 1706.1 (Panel Rules of Procedure) states that operational costs shall be divided equally between disputants. Accordingly, the Panel assesses the Respondent and Complainant 50% each of the panel operational costs.

APPENDIX A

Participants in the Panel Hearings

The Panel

Clay Gilson, C.M. - chair
Claude Castonguay, C.C., O.Q.
Arthur Mauro, O.C., Q.C.
Gordon Ritchie
Gilbert Winham

Assistant to the Panel
John Hope

For Nova Scotia

Internal Trade Representative
Greg Bent

Counsel
Greg Evans - Justice

Other Officials
David Robinson - Agriculture and Marketing
Brian Smith - Agriculture and Marketing
Gabriel Comeau - Dairy Commission

Farmers Cooperative Dairy
Chris Power
Jon Curry
Robert Knox (consultant)

For Prince Edward Island

Internal Trade Representative
Terry Hopkins

Counsel
Laura Kell - Justice

Other Officials
Richard Veinot - Agriculture and Forestry

APPENDIX B

Summary of Submissions

Complainant (Nova Scotia)

Nova Scotia contends that P.E.I. amended the regulations to its *Dairy Industry Act* and applied these regulations to exclude products from other provinces in a way that is inconsistent with the *Agreement*.

Specifically, Nova Scotia alleges that the inconsistency arises from three new elements introduced by the amendments to the regulations:

- all existing licenses were revoked and a re-licensing process was mandated;
- the Department was allowed to issue licenses with any terms and conditions it deemed appropriate; and
- the Department was enabled to restrict market access on a discretionary and arbitrary basis by withholding licenses deemed not to be in the best interest of the general public or the dairy products trade.

Nova Scotia asserts that, as of September 1, 1997, fluid milk distribution measures were included in the scope and coverage of Chapter Nine (Agriculture and Food Goods) by virtue of Article 902.3, and subject to its provisions and those of Chapter Four (General Rules).

Nova Scotia alleges the following breaches of the *Agreement*:

<u>New Measure Violates the Article 905 Standstill</u>

It is Nova Scotia's position that the amendments to the P.E.I. *Dairy Industry Act Regulations* (EC665/97) were new measures affecting internal trade and therefore inconsistent with Article 905 (Non-Sanitary and Non-Phytosanitary Measures).

Nova Scotia cited four provisions that it believes were not in the *Dairy Industry Act Regulations* before EC665/97 was introduced:

- the discretionary authority to include any terms and conditions in a license that the licensing authority considered appropriate;
- the discretionary authority not to issue a license or apply a term and condition that is in the "best interest of the public or the dairy products trade", when "interest" is not defined;
- a specific provision that a holder of a manufacturers and processors license had to be specifically licensed to distribute fluid milk; and

- cancellation of existing licenses effective December 31, 1997, requiring all those wishing to be licensed to produce, process or distribute fluid milk to apply under the new rules.

Nova Scotia rejects P.E.I.'s argument that these amendments were not new but confirmed existing administrative practice. According to Canadian practice, legal authority is established through legislation and regulations and attendant policy documents. The authority to apply terms and conditions or to issue licenses that were only in the public or dairy industry interest did not exist in any documentation, regulations or legislation before November 1997. Nova Scotia notes that, following the regulatory amendments, P.E.I. also produced a paper, "Policy and Procedures to be Applied in the Issuance of Conditions for Distributors Licenses". This paper introduced a requirement to apply for licenses for individual products and submit each container for approval in advance. These were new requirements - the measures that P.E.I. used to exclude products from outside P.E.I. from its market were unwritten, informal and not properly authorized before they were introduced by the regulatory amendment in November 1997.

Nova Scotia also rejects P.E.I.'s argument that the amendments were necessary to enforce existing law. Nova Scotia maintains that if the law was already in place, amendments should not have been necessary to enforce it, particularly since the amendments to the regulations apparently introduced new authorities.

Measure Violates Article 401: Reciprocal Non-Discrimination

Nova Scotia argues that, even if EC665/97 could not be construed to be a new measure, existing measures respecting trade in fluid milk products became subject to the *Agreement* on September 1, 1997, and that EC665/97 must therefore be consistent with both Chapter Four and Chapter Nine.

Nova Scotia alleges that EC665/97 violates Article 401 by extending better treatment to P.E.I. products than like, directly substitutable or competitive products from Nova Scotia.

Nova Scotia maintains that, through its application, EC665/97 restricts internal trade, particularly through the discretionary authority to apply any terms and conditions that the licensing authority considers appropriate and to issue licenses only if the licensing authority considers it to be in the best interest of the public or the dairy trade. This authority was used to exclude products from outside the province from the P.E.I. market.

For example, some Farmers products are not licensed that are in every respect the same (that is, they are competitive or substitutable) as products distributed by local dairies in P.E.I. The distinguishing feature of these unlicensed products is that they are processed and packaged outside P.E.I. and compete with products already provided by local dairies.

Nova Scotia notes that Health is allowed to acquire and distribute 2 litre cartons when they are processed and packaged by a P.E.I. dairy (referred to as a co-packing

arrangement), but it is not permitted to acquire the same product when it is processed and packaged by Farmers outside of P.E.I..

Nova Scotia points out that, in the licenses issued to Health and Farmers, mostly high volume products processed and packaged by Farmers outside of P.E.I. were excluded. The only reason provided by P.E.I. was that it was not in the interests of P.E.I. consumers or the P.E.I. dairy industry for these products to be licensed.

Nova Scotia notes that there are no specific criteria to determine what products would meet the consumer or the dairy industry interest test, but judging from comments made by P.E.I. officials it appears that this latitude allows the licensing authority to discriminate in favour of the local industry.

Nova Scotia notes that P.E.I. officials have stated in official correspondence that, in the general administration of the *Dairy Industry Act* and regulations, it has been the long-standing policy of P.E.I. that Class I products distributed in P.E.I. be sourced in P.E.I. when such products are available from local dairy plants.

Nova Scotia introduced evidence to show that, in one case, a distributors license was not granted to an applicant because the product was available from local dairies, while in another case, a license was issued to an applicant on condition that it source the products it distributed from local dairies.

Nova Scotia noted that, if a dairy from outside Nova Scotia purchased a licensed distributor in Nova Scotia, that purchaser would be allowed to move fluid milk back and forth across the Nova Scotia border.

Nova Scotia contends that Article 401 requires that P.E.I. accord the goods of any other Party, including Nova Scotia, treatment no less favourable than the best treatment it accords to its own like, directly competitive or substitutable goods. Nova Scotia argues that P.E.I.'s policy of favouring fluid milk products produced in P.E.I., which P.E.I. has acknowledged exists, is inconsistent with Article 401.

Measure Violates Article 403: No Obstacles

Nova Scotia alleges that EC665/97 provided the P.E.I. fluid milk licensing authority with new discretionary authority to apply terms and conditions to licenses and to license only products that were judged to be in the best interest of the general public or the dairy products trade. This authority was applied in a way that created obstacles to trade that are inconsistent with Article 403 (No Obstacles).

Article 403 requires that P.E.I. ensure that any measure it adopts or maintains does not operate to create an obstacle to internal trade.

Nova Scotia, citing the same examples as those used in its Article 401 argument, believes that P.E.I. applies its new regulations so as to restrict internal trade in a way that is inconsistent with the Article 403.

Measure Not Justified by Article 404: Legitimate Objectives

Nova Scotia notes that P.E.I.'s fluid milk licensing measures could be permissible under the *Agreement* if their purpose is to meet a legitimate objective. However, protecting the production of an industry does not qualify as a legitimate objective according to the definition of "legitimate objective" in Article 200. In Nova Scotia's view, the measures are not intended to accomplish any acceptable legitimate objective including consumer protection or the protection of the health and safety of workers and therefore are not permissible to the extent that they are inconsistent with the *Agreement*.

Transparency Provisions of the Agreement Not Met

Nova Scotia points out that Article 907(1) (Transparency) requires a Party amending or adopting a measure that may affect trade, to give notice of the change and provide the Federal-Provincial Trade Policy Committee with a description of the measure, the objective and the reasons for its introduction, and provide a copy of the measure to interested parties (namely the government of Nova Scotia and Farmers), and subsequently to allow time for discussion.

Nova Scotia alleges that P.E.I. did not comply with any of these provisions. Nova Scotia maintains that P.E.I. was not relieved of its responsibility to give notice of change as provided in Article 907(2) since EC665/97 did not involve sanitary or phytosanitary protection.

Nova Scotia rejects P.E.I.'s contention that notice was not required because EC665/97 was the result of a routine review of the *Dairy Industry Act* and its regulations. Nova Scotia argues that this cannot justify forgoing the notice and consultations required under Article 907(1), particularly since P.E.I. was conducting a review of its dairy industry measures for trade related reasons, and the review process began five months before the amendments were introduced.

It is the position of Nova Scotia that had P.E.I. initiated discussions with Nova Scotia and Farmers before making its amendments, the issues now being considered might have been avoided.

Measure Violates the Overall Objectives of the Agreement

Nova Scotia maintains that P.E.I. is obligated by Article 100 (Objective) to reduce and eliminate barriers to trade and to establish a more open, efficient and stable domestic market. Article 101 (Mutually Agreed Principles) establishes rights and obligations accepted by the Parties, including P.E.I., when they entered into the *Agreement*. Among these obligations are:

- an undertaking not to introduce new barriers and to facilitate cross boundary trade;
- a commitment to treat people, goods, services, and investment equally regardless of where they originate in Canada;

- a responsibility to ensure that administrative policies and practices operate to support an open domestic market.

To support the application of these principles, in Article 101(4) P.E.I. accepted the need for full disclosure of information, legislation and regulations, policies and practices that have the potential to impede an open efficient and stable domestic market.

Nova Scotia believes that P.E.I. has ignored its commitments in Article 100 and 101. Specifically it has introduced new measures that were used to restrict internal trade, inhibit cross-boundary trade in fluid milk, and permitted the licensing authority to work under the cloak of administrative policies and practices to discriminate against out-of-province products and to exclude fluid milk products from outside P.E.I. from its markets.

Furthermore Nova Scotia believes that P.E.I. has introduced discretionary measures into its fluid milk distribution licensing procedures that are intended to obscure the basis for their application (specifically Section 2(3) and 2(3.1) of P.E.I.'s *Dairy Industry Act Regulations*). There are no criteria or standards attached to these authorities that would limit their arbitrary application. This is inconsistent with the spirit and intent of Article 101(4)(a).

Administrative Arguments Not Supported

Nova Scotia notes that, in its submission, P.E.I. characterizes the dispute as one of regulatory compliance, rather than trade policy. Nova Scotia rejects P.E.I.'s position that Farmers was an unlicensed distributor of unlicensed products. Specifically, Nova Scotia:

- does not agree that Health's license was transferred to Farmers as a result of its share purchase;
- does not accept that Farmers required a distributors license when its products were acquired and distributed by Health;
- does not believe there was anything in the *Act* and the regulations that prevented Health from distributing Farmers products and that, according to the *Act* and regulations prior to EC665/97, Health was entitled to such a license if the products, in other ways, respected the *Dairy Industry Act* and its regulations; and
- does not agree that Health's manufacturers and processors license prevented them from distributing Farmers' products since these licenses were accepted by the P.E.I. regulator as a distribution license for some years.

While P.E.I. maintains that the dispute with Farmers highlighted the need for clarified regulations, Nova Scotia points out that the initial letter from P.E.I. to Farmers was sent the same day EC665/97 came into force. Therefore, Nova Scotia concludes that the regulatory change preceded the dispute, and the dispute could not have been the basis for regulatory action.

Ongoing Negotiations Not Relevant to These Proceedings

Nova Scotia rejects P.E.I.'s suggestion that, even if the measure is inconsistent with the *Agreement*, ongoing negotiations between Maritime dairy regulatory agencies are a more appropriate forum for resolving the dispute than a panel hearing.

Nova Scotia contends that the mandate of the Panel is to decide on the matter at hand, which is the question of whether or not EC665/97 is inconsistent with the *Agreement*. Nova Scotia argues that the existence of ongoing negotiations is irrelevant to the Panel proceedings.

Furthermore, Nova Scotia argues that the regional negotiations have been taking place for a considerable period of time without any progress being made. Nova Scotia contends that the regional negotiations are unlikely to resolve this dispute.

Injury Sustained

Nova Scotia alleges that, as a result of P.E.I.'s actions, Farmers has sustained the following injury:

- both Health's and Farmers' reputations among consumers and retailers have been damaged. Their products have been, implicitly, identified as unsatisfactory and foreign and their reputation as a secure and trustworthy supplier of a full range of dairy products has been undermined;
- Farmers has suffered substantial financial injury as a result of EC665/97 and the way it has been applied to arbitrarily exclude Farmers products from outside P.E.I.; and
- Farmers has been unable to implement its strategy to participate fully in the P.E.I. market as a regional dairy, and to develop a viable and productive dairy operation in P.E.I. supported by P.E.I. producer shareholders.

As remedy, Nova Scotia requests that the Panel recommend that P.E.I. remove the amendments to the *Dairy Industry Act Regulations* passed in November 1997 (EC665/97) and ensure its *Dairy Industry Act* and regulations are applied in a way that is consistent with the Agreement on Internal Trade, particularly Article 401 (Reciprocal Non-discrimination) and Article 403 (No Obstacles).

Respondent (Prince Edward Island)

Prince Edward Island submits that the issue before the Panel is to determine whether EC665/97 is inconsistent with Article 905 of Chapter Nine of the *Agreement*, or has been applied in a manner which is inconsistent with Article 905 of the *Agreement*, on the basis that it introduced a new measure or measures which restricted internal trade in dairy products.

By way of background, P.E.I. relates that the Department undertook a review of its *Dairy Industry Act* in July 1997, and determined that some aspects of its *Dairy Industry Act*

and regulations were outdated. The Department determined that the regulations should be clarified so that interested persons were better informed of the basis and manner in which Department was exercising its jurisdiction to licence persons in the dairy industry.

P.E.I. maintains that, several months after the Department commenced its review of the industry legislation, it came to the Department's attention that Farmers had been distributing product for sale to the public in P.E.I. without having been duly licensed to do so. The Department advised Farmers that the distribution of the product was in violation of several sections of the *Dairy Industry Act* and regulations.

In the midst of the conflict between P.E.I. and Farmers, the Department introduced amendments to its *Dairy Industry Act Regulations* by way of EC665/97. The regulations specified that the Department would be requiring licensees to re-apply thereby supporting documentation. The Department was of the opinion that it was necessary to do this in order to obtain the information necessary to properly administer and enforce the laws and to confirm industry compliance without singling out specific processors or manufacturers.

P.E.I. notes that the P.E.I. Supreme Court confirmed the P.E.I. Government's right to enforce the *Dairy Industry Act* provisions requiring licensing of distributors.

Issue is Whether the Measure is a New Measure under Chapter 9

P.E.I. states that the issue is whether EC665/97 introduced any new measures that restricted trade. P.E.I. submits that EC665/97 introduced no changes in the substantive law or policy respecting licensing within the dairy industry. The amended regulations contain no provisions which limit or restrict interprovincial trade. P.E.I. submits that there is no authority or provision in the *Dairy Industry Act* and its regulations that restricts interprovincial trade.

P.E.I. points to the fact that the majority of provisions respecting licensing, container labelling and other matters relevant to dairy processors and distributors under the *Dairy Industry Act* and its regulations are not confined to section 2(3) of the *Dairy Industry Act Regulations*, which was the only section of the regulations amended by EC665/97.

Furthermore, the majority of the P.E.I. *Dairy Industry Act* provisions which were applicable to Farmers Dairy as a prospective distributor of Class I products in P.E.I. were unchanged by EC665/97. These provisions include:

(1) Subsection 4(1) of the *Dairy Industry Act* which requires that every distributor of Class I milk must obtain a licence from the Department in order to legally distribute Class I milk within the province;

(2) (Subsection 2(4) of the *Regulations* which specified that an application for licensing of a new dairy manufacturing plant required specific information including a description of the location and nature of the plant site, the source of the raw milk to be processed or manufactured at the plant;

(3) Subsection 2(5) of the *Regulations* which stated that "licenses are not transferable";

(4) Subsection 2(7) which provided for licence revocation;

(5) Section 18(1)(a) of the *Regulations* which requires that any container used for sale or distribution of Class I milk or dairy product, indicate the name and address of the processing plant at which the product was processed on the container;

(6) Sections 18(2) - (4) which make it an offence to mislabel a container, misrepresent a product, or to use a container which has not been approved by the Department; and

(7) Standards and conditions in section 22 of the *Regulations* which if breached could result in licence revocation.

In summary, P.E.I. argues that, since EC665/97 does not constitute a new measure, it does not automatically violate the *Agreement*. P.E.I. contends that the *Agreement* provides transition periods for bringing existing measures into conformity with the provisions of the *Agreement*.

The Effect of Regulation EC665/97 on Dairy Licensing in P.E.I.

P.E.I. notes that, prior to EC665/97, the regulations under the P.E.I. *Dairy Industry Act* relating to "Licenses" did not explicitly reference the discretionary considerations which were taken into account by the Department in making its decisions nor were details as to the specific manner in which the Department would potentially exercise it jurisdiction provided.

P.E.I. maintains that none of the seven subsections which were added to the *Dairy Industry Act Regulations* by EC665/97 contained any measures to expand upon the Department's powers with respect to licensing. The seven subsections did introduce a more explicit statement of the basis upon which the Department had exercised its discretionary powers under its jurisdiction as provided in the *Dairy Industry Act*. However, this is distinct from actually changing the law.

P.E.I. contends that the statement contained in subsection (3.1) that the Department would take the best interests of the general public or the dairy products trade into account in issuing a licence or approving a term or condition of a licence does not introduce any additional discretionary power into the Regulations.

It is P.E.I.'s position that Subsection (3.1) represents an explicit statement of the discretionary basis upon which the Department has historically exercised its discretion. That a government body or regulatory authority would exercise its discretion in the public interest or in the general interest of the industry it regulates is almost akin to a presumption. Such a discretionary power would be implied even where the legislation does not explicitly refer to "public interest". Hence, the introduction of this provision,

which explicitly references public and industry interest as a discretionary consideration in decisions made under the *Dairy Industry Act,* does not change the fact that this would be implied in any event and was in fact the basis upon which Departmental discretion was exercised.

P.E.I. maintains that the new provision in Subsection (3.2) stating that "a licence to engage in any of the categories of work in the dairy industry listed in subsection (1) does not authorize the holder of the license to engage in any other category of work in the dairy industry listed in subsection (1)", is simply a restatement of the requirements already contained in subsection 4(1) of the *Dairy Industry Act* and subsection 2(1) of the *Regulations*, both of which stated that persons engaged in providing certain services or functions within the P.E.I. dairy industry must hold a licence appropriate to that function.

Section (3.3) states that the Department may issue a licence for more than one category of work in the dairy industry to any licence holder. It is P.E.I.'s position that this provision confirmed that the Departmental practice of issuing multiple licences authorizing a specific licence holder to carry on work in several different categories would continue.

P.E.I. maintains that Subsections (3.4) - (3.6) authorizing licence revocation and re-issuance for the 1997-98 dairy year confirmed the Department's existing power under the *Dairy Industry Act*. The actual power to revoke licences is not derived from regulation, but from the *Dairy Industry Act* which provides at clause 9(c) for the power to make regulations providing for the form of certificates and licenses issued as well as the terms and conditions upon which licenses would be issued.

The power to issue, revoke, reissue and determine the duration of licenses already existed prior to the insertion of subsection 2(3.4). Subsection 2(7) of the *Regulations*, which was not amended, explicitly stated that the Department may suspend, revoke, or refuse to issue or reissue a licence. The amendments to the *Regulations* in 1997 did not expand or affect the Department's statutory right to revoke licences and to do so would have been redundant in light of subsection 2(7).

P.E.I. argues that Subsection (3.6), which confirmed that the usual annual renewal fees prescribed by the *Regulations* would not apply to a licence renewed pursuant to subsection (3.5), was added to avoid charging the licensees twice for the same licence in one year.

In summary, P.E.I. states that the amendments contained in EC665/97 did not change the substantive law relating to licensing. It did however, implement measures to confirm the law, confirm the discretionary basis upon which the Department had been exercising its authority and gave notice to the public and industry that the Department was enforcing its power under the *Dairy Industry Act* to ensure that licensees were in compliance with the law.

The Alleged Legal Right to Distribute Class I Milk Before and After EC665/97

P.E.I. notes that Nova Scotia alleges that prior to the adoption of EC665/97, Farmers possessed a right to sell or distribute Class I milk in P.E.I., but that this "right" was removed or revoked by EC665/97. This allegation represents a key issue before the Panel in making its determination as to whether EC665/97 is inconsistent with the Agreement.

P.E.I. takes the position that this allegation is not supported by the evidence. P.E.I. notes that Farmers failed to obtain a declaration from the Supreme Court that such a right to distribute its products existed.

Furthermore, the April 14, 1998 order of Chief Justice K.R. MacDonald of the Supreme Court Trial Division rescinding an earlier interim injunction of Madam Justice Matheson confirmed the Department's jurisdiction under the *Dairy Industry Act* to require removal of Farmer's unlicensed product.

P.E.I. states that, while it was true that Farmers had been distributing Class I products in P.E.I. prior to EC665/97, it was doing so in violation of the *Dairy Industry Act* and it possessed no legal right to do so.

P.E.I. maintains that this is not a situation where a valid legal right existed which was later removed by an amendment to the law. This is actually a situation where behaviour prohibited by statute managed to persist for some time before it was discontinued in accordance with the law as it existed before the behaviour commenced.

P.E.I. submits that Farmer's non-compliance with several provisions of the law relating to dairy licensing and labelling led to removal of its unlicensed product from P.E.I. retail outlets, not the introduction of EC665/97.

P.E.I. notes that, in spite of these violations, Farmers believed it possessed a right to distribute Class I products on within the province, under the licence of Health. P.E.I. disagrees with this interpretation on the basis that it is contrary to relevant principles of law.

Farmers is a separate legal entity from Health. The relationship of Farmers to Health is that Farmers is the sole shareholder of Health. In terms of corporate law, Health could be described as a subsidiary of Farmers.

P.E.I. submits that the property and rights of subsidiary companies are separate from that of the parent company. It is an established legal principle that subsidiary corporations are separate legal entities in the same way that non-related companies are also separate legal entities.

P.E.I. argues that it is a well-accepted principle of law that licenses and permits which are the property of a business which is purchased by another company do not automatically or necessarily become the property of the purchasing company.

Furthermore, there is no question that Government licenses are not assignable or transferable, particularly where a licence states this fact on its face.

Therefore, where a corporation is considering the purchase of a licensed business in a regulated industry, it is always necessary that the purchaser-corporation contact the relevant regulatory authority in advance to obtain the required Government consents.

The terms and conditions of the licence held by Health when it was purchased by Farmers were clear on the face of the licence. The licence indicated it was "non-transferable" and it authorized only two functions, manufacturing dairy products and processing Class I milk. These functions were only authorized within the province of P.E.I.

P.E.I. argues that the licence terms would not permit use by another corporation or business given that it was "non-transferable". This was re-stated in the regulations. Even if re-assignment of the licence from Health to Farmers were possible, it could not occur in these circumstances because the licence could not authorize processing or manufacturing carried on in another province as this would be constitutionally invalid.

P.E.I. also argues that no right of product distribution was explicitly granted by the licence, even for the licensee Health. Farmer's claim that it was entitled to distribute any product it so wished without the consent or authorization of the Department is also clearly contrary to the *Dairy Industry Act,* which requires that every distributor of Class I milk must obtain a licence from the Department in order to legally distribute Class I milk within the province, pursuant to Subsection 4(1) of the *Dairy Industry Act*.

P.E.I. notes that Farmers' activity in the P.E.I. marketplace brought it within the unchanged definition of "distributor" under the definition in section 1(q) of the regulations which includes any person who directly or *indirectly* sells or distributes Class I milk to consumers, including a processor. Farmers was not licenced as a distributor within the province and it held no other form of licence under which a right of distribution could be implied.

P.E.I. submits that the action taken by the Department with respect to Farmers' unlicensed product distribution would have occurred in any event, regardless of whether the provisions contained in EC665/97 existed or not. It was not the intention of P.E.I. to introduce trade barriers or measures restricting trade in adopting the provisions of EC665/97. The intention was to introduce provisions to clarify and prevent future misinterpretations of the legislation. It was also the intention to introduce measures to assist in the enforcement of the law which was already in place, in order to ensure that distributors were complying with the law contained in the *Dairy Industry Act* and its regulations regardless of where product was produced or processed.

Measure Does Not Breach Chapter Four Obligations

In the course of the Panel hearing, P.E.I. argued that the measure in dispute was EC665/97, and that there were no provisions in EC665/97 respecting trade. P.E.I. submitted that the *Dairy Industry Act*, as well as the *Dairy Industry Act Regulations* as

amended by EC665/97, were trade-neutral, and therefore were not inconsistent with Articles 401, 402 (Right of Entry and Exit), and 403.

P.E.I. conceded that the policy implementing the *Regulations* constituted a barrier to internal trade. However, P.E.I. noted that similar policies were maintained by all four Atlantic provinces. Furthermore, P.E.I. maintained that the dispute centred on EC665/97, not on the policy implementing it.

Barrier to Trade is Being Addressed Regionally

P.E.I. states that all Parties recognize that there is a trade barrier respecting fluid milk distribution in the Maritimes. P.E.I. submits that the recognized trade barrier pre-existed the *Agreement* coming into force.

P.E.I. suggests that, while the Parties are not moving quickly to remove this barrier, they do realize their obligations and it is the intent of the Parties to comply with those obligations. P.E.I. suggests that the dispute does not seem to be with the substance or understanding of the obligations under the *Agreement* to reduce and eliminate trade barriers. Rather, the problem seems to be an issue of process as to how the Parties are to go about reducing and eliminating their trade barriers.

P.E.I. maintains that, while there is a clear obligation to eliminate and to reduce trade barriers, there are no clear cut rules as to how this is to be achieved other than the general processes which are set out in the Annexes 405.1 and 405.2.

P.E.I. argues that, while progress may be slow, Maritime provinces are working on harmonizing their fluid milk distribution policies, and therefore a Panel dispute process examining only one measure in the region will result in a piece-meal approach to resolving the issue.

Transition Period is Unspecified

It is P.E.I.'s position that the *Agreement* allows a transition period to make existing measures consistent with the *Agreement*, and the length of the transition period is not specified. P.E.I. argues that a transition period for agricultural measures began on September 1, 1997. In support of this position, P.E.I. notes the widespread non-compliance with the *Agreement* across economic sectors.

Relative to the language of Annex 902.5, paragraphs 6 and 7, P.E.I. submits that the Parties were required to have adopted recommendations on specific measures by September 1, 1997, but were not required to have made legislative or regulatory changes by that date.

P.E.I. argues that the *Agreement* recognizes that harmonization does not occur overnight, and therefore P.E.I. disagrees with Nova Scotia's submission that existing trade barriers became inconsistent with the *Agreement* on a specific date (i.e. September 1, 1997).

Based upon the foregoing, P.E.I. urges the Panel to find that EC665/97 did not introduce measures restricting interprovincial trade.

APPENDIX C

Letter Including Fluid Milk Standards and Distribution in Scope and Coverage of Chapter Nine

Agriculture
Canada

Market and Industry Services Branch
Multilateral Trade Policy Division
International Trade Policy Directorate
Room 10109, 930 Carling Avenue
Ottawa, Ontario CANADA
K1A 0C5

Direction générale des services à l'industrie et aux marchés
Division des politiques de commerce multilatéral
Direction des politiques de commerce international
Pièce 10109, 930 rue Carling
Ottawa (Ontario) CANADA
K1A 0C5

Your file / Votre référence

Our file / Notre référence
1080-2

October 1, 1997

The Honourable John Manley
Minister of Industry
11th Floor East
235 Queen Street
Ottawa, Ontario
K1A 0H5

The Honourable James E. Downey
Minister of Industry, Trade and Tourism
Room 358, Legislative Building
450 Broadway Avenue
Winnipeg, Manitoba
R3C 0V8

Dear Ministers:

We are writing to you in your capacities as co-chairs of the Federal/Provincial Committee on Trade under the Agreement on Internal Trade (AIT).

Under Article 902.3 of the AIT, the Federal Provincial Agricultural Trade Policy Committee is to notify your Committee of any unresolved measures involving technical barriers with policy implications on or before September 1, 1997. The following technical barriers with policy implications have been identified:

a) shipment of horticultural products in bulk containers;
b) absence of a Canada No. 1 Small potato grade.
c) margarine colouring restrictions and other margarine standards;
d) standards regarding dairy blends (mixtures of butter and margarine) and imitation dairy products;
e) fluid milk standards and distribution.

.../2

Canada

It is recognized that these measures will fall within the scope and coverage of Chapter Nine of the AIT from September 1, 1997.

Yours sincerely,

Michael N. Gifford
Co-Chair

John Schildroth
Co-Chair

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