

**GREEN SUDS OR PROTECTIONIST POLICY: US/CANADA DISPUTE OVER BEER TRADE:
PARTICIPANT INSTRUCTIONS
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Overview

This exercise provides an interactive case simulation in which you will be assigned to a group that will assume the role of one of several stakeholder groups (government, industry, environmental groups) in an actual dispute over the trade-consistency of the Canadian Province of Ontario's application of an environmental levy on non-refillable malt beverage containers. In this case, the U.S. government, on behalf of the U.S. beer industry, objected to the tax, arguing that it violated the national treatment obligation of the General Agreement on Tariffs and Trade (now the World Trade Organization – hereafter GATT/WTO). The U.S. contemplated appealing the case to the GATT/WTO. This simulation assumes that the U.S. proceeds with the appeal, and puts participants in the roles of the various disputants: U.S. Government, Ontario and Canadian governments, U.S. brewing industry, a coalition of environmental groups, and the U.S. aluminum industry.

Background on Canada's Alcohol Policies and International Trade Obligations

The European Community (EC), Japan, and the United States have all maintained that Canadian provincial beer policies violate Canada's GATT/WTO obligations. In 1988, a GATT/WTO panel was convened at the request of the EC and found that certain practices of Canadian provincial liquor boards affecting beer imports were GATT/WTO-inconsistent. These practices included restrictions on the points of sale (where beer can be sold – generally only in provincial stores), discriminatory listing and delisting practices (requirements that only beer that achieves a certain level of sales be “listed,” disadvantaging any new listings that may have difficulty achieving sales quotas due to inferior shelf placement), and price markups (absolute [versus percentage] standard pricing markups that erode the competitiveness of popular-priced beer).

Canada had difficulty acting upon the GATT/WTO Panel's recommendations because alcohol beverage regulations are largely under provincial jurisdiction. Instead, the Government of Canada convened an interprovincial committee that developed an agreement addressing concerns about listing/delisting and markup differentials, but did not deal with Canada's GATT/WTO obligations *vis-à-vis* imported beer. Attention to distribution practices was deferred until after 1994. An agreement between Canada and the EC addressed only listing/delisting practices and established a "standstill" (no worsening of treatment) on discriminatory markups as applied to imported beer products.

Both the U.S.-Canada Free Trade Agreement (CFTA), implemented on January 1, 1989, and its successor agreement, the North American Free Trade Agreement (NAFTA), implemented on January 1, 1994, excluded provincial beer regulations from their obligations. These exclusions were due to the Canadian federal government's continuing inability to insure compliance by its provinces to these international trade obligations.

U.S.-Canada Beer Disputes

In June, 1990, G. Heilman Brewing Company requested that the Office of the U.S. Trade Representative (USTR) initiate a “Section 301” investigation alleging unfair trade practices by the provincial liquor boards against import of U.S. beer (Section 301 is a trade law that allows U.S. industries to petition the government to initiate trade action against foreign countries that are alleged to engage in unfair or protectionist policies). The United States also brought a case against these Canadian provincial practices to the GATT/WTO. In October 1991, the GATT/WTO Panel ruled against Canada's provincial beer practices. Canada “adopted” (agreed to) the Panel's findings at the February 1992 GATT/WTO Council Meeting. On March 31, 1992, Canada submitted a plan to act on the GATT/WTO ruling under which interprovincial barriers to domestic beer trade in six provinces would be removed by July 1992, although discriminatory provincial beer practices against *imported* beer would not be remedied until 1995.

Under threat of trade retaliation by the U.S. government, an Agreement in Principle was reached on April 25, 1992 between the two parties that would have eliminated discriminatory pricing (markups, general and administrative components of cost of service charge) and listing (package size restrictions in Ontario) by July 1992, and provided delivery and points of sale access by September 1993. The United States agreed to freeze its retaliatory actions once an acceptable agreement was concluded: it said it would rescind instructions to the U.S. Customs Service to withhold liquidation of imports of Canadian beer, and terminate Section 301 of U.S. trade law. (These actions had been initiated after the GATT/WTO Panel had ruled in favor of the United States, and Canada had not yet taken any action.) Such retaliatory threats are typical of such disputes and are frequently used as bargaining chips in order to convince countries to take remedial action in response to GATT/WTO Panel rulings.

The Environmental Can Levy

On April 26, 1993, however, the province of Ontario announced a \$.05 increase in its "environmental fee" on nonrefillable alcoholic beverage (but not soft drink) containers to \$.10 per container. The government presented this increase as just one element of Ontario's overall environmental program, and argued the increase was simply designed to discourage use of single-use disposable containers. The United States argued that Ontario's fee disadvantaged U.S. brewers (who ship predominately in cans) and that the new tax was an underhanded effort to limit U.S. beer sales in Canada, noting that even if U.S. brewers shipped in refillable glass containers argued the U.S. government, there was no system in place to provide access to Ontario's return system.

Canada said that a plan would be developed to provide U.S. brewers access to the system, but not until September 1993, and, because of peculiarities of Ontario's entire alcohol beverage control regime, U.S. brewers would not be granted access identical to Ontario brewers but would be treated in a 'parallel' fashion. (Because Canadian brewers own and operate retail beer outlets where bottles are returned, and provincial alcohol beverage control officials limit the number of available return sites, U.S. brewers would not be permitted to operate similar return points, partly because Canadian brewers were resistant to carrying U.S. products and accepting bottles of their U.S. competitors.) U.S. aluminum manufacturers joined the debate because they were concerned about sales north of the border. They claimed that aluminum cans were as environmentally responsible as glass bottles. In fact, producers claimed that cans could be recycled dozens of times and were therefore less environmentally damaging than bottles which could only be refilled 4-5 times and were then discarded as common solid waste (see table below).

Environmental groups, including the Sierra Club and Friends of the Earth, urged the USTR to reconsider its hard line position saying that refillable container systems were a preferred approach to limiting solid waste and protecting the environment. Moreover, such systems were used widely in the United States and Europe. In addition, the groups argued that the ability of the U.S. to negotiate tough environmental and labor side agreements to the NAFTA (negotiations which were at a very sensitive stage) would be compromised by the U.S. objecting to a legitimate environmental initiative in Canada. Further complicating the situation was the fact that the EC had taken the U.S. to the GATT/WTO over U.S. taxes that discriminated against automobiles with low gas mileage, a circumstance not entirely dissimilar to the Ontario/U.S. dispute, with the United States in the role of the defendant.

Discussions between the U.S. and the governments of Canada and Ontario to lessen the negative effects of the tax through either early access to the private retail beer store system or creation of a return system at the liquor control board retail stores were unsuccessful. On July 24, 1993, the United States imposed retaliatory import tariffs of 50 percent *ad valorem* (percentage) on Canadian beer brewed in Ontario.

Issue for Decision

Although the GATT/WTO had already ruled on many of Canada's restrictive practices, the United States considered bringing a new case to the GATT/WTO focusing solely on the can tax. If the U.S. had brought such a case, what arguments would be made by the parties in the dispute? How should/would the GATT/WTO have ruled on the question of whether or not the Ontario levy violates GATT/WTO rules?

Simulation Instructions

You will be assigned to one of six groups:

- (1) U.S. government;
- (2) Canadian/Ontario government;
- (3) U.S. brewers;
- (4) a coalition of U.S. and Canadian environmental groups, including Sierra Club and Friends of the Earth;
- (5) U.S./Canadian aluminum producers;
- (6) the GATT/WTO panel.

Participants should spend 20-30 minutes reviewing the case and formulating arguments that advance the agenda of the group. Refer to the "GATT/WTO Principles" below and the background material above for further guidance. After the initial session, groups whose interests may be similar may consult with each other for an additional 10-15 minutes to coordinate presentations/minimize duplication. These might include the Ontario/Canadian government group consulting with the environmental group, and the beer and aluminum producers consulting with each other and the U.S. government. The Panel is essentially composed of judges and should be respected accordingly. Each group should make an opening presentation of no more than 10 minutes to the GATT/WTO Panel. The presentation should summarize the main points of the argument and urge a particular decision on the part of the Panel. Panel members may then ask questions of the groups for an additional 15 minutes. After each group has presented its argument, the Panel will deliberate for 20 minutes and present its findings.

GATT/WTO Principles: General Obligations

The General Agreement on Tariffs and Trade (now the World Trade Organization or WTO) was founded after World War II to establish rules for international trade practices and resolve disputes among nations. Two fundamental principles govern most GATT/WTO provisions: most favored nation treatment and national treatment. National treatment refers to the obligations of the contracting parties to treat nationals of foreign countries no less favorably than they treat nationals of their own country. A more common term for this obligation is "non-discrimination." The GATT/WTO also requires that the parties extend most-favored nation treatment to other parties, so that some countries are not treated more favorably than others. Dispute settlement resolution (when one or more countries accuse another contracting party of violating GATT/WTO rules) is carried out by three to five member panels that render reports (decisions).

Exceptions

The GATT/WTO provides for limited exceptions to the above obligations. For example, preferential trade agreements such as the EU and NAFTA are permitted to extend better-than-most-favored-nation treatment to their members under certain conditions. There are also "general" exemptions which excuse otherwise illegal actions if they are designed to protect public morals, preserve national heritage, and limit commerce in goods made with prison labor. Although the word "environment" is never mentioned, the GATT/WTO does offer a basis for deviating from GATT/WTO principles in support of environmental protection. Specifically, Article XX holds that the GATT/WTO does not prevent contracting parties from taking actions: (1) necessary to the protection of human animal, or plant life or health; and (2) relating to the conservation of exhaustible natural resources -- provided trade measures affecting international commerce are joined by restrictions on domestic production or consumption.

Domestic environmental policies justified under Article XX would have to meet three criteria: (1) fit to the defined (limited) scope, (2) be necessary or be the least trade restrictive alternative available or “related to” conservation of exhaustible natural resources, and (3) be applied in a nondiscriminatory way. Limited scope is defined as follows. Article XX expressly covers only health issues relating to the conservation of exhaustible resources. Because they do not explicitly mention the environment, the GATT/WTO provisions do not cover environmental policies outside the “exhaustible natural resources” category. The “necessary test” requires that all less trade-distorting options must be tried before more trade-distorting options are considered. Regarding extra jurisdictional/extraterritorial measures (extension of domestic laws and practices to other countries) in the 1991 Tuna-Dolphin case the GATT/WTO Panel found Article XX could not be involved in defense of policies addressing environmental harms outside the country using the measures.

Energy Consumption per use for 12 oz. Beverage Containers

Studies have shown that energy use to produce beverage containers provides a conflicting picture of whether aluminum cans or bottles are preferable from an environmental standpoint. See Table 1.

Insert Table 1 Here

APPENDIX: ADDITIONAL BACKGROUND ON TRADE/ENVIRONMENT TENSIONS

Time permitting, instructors may wish to devote one class period in advance of the simulation to a brief review of other trade/environment issues and conflicts presented below. In addition, instructors in other countries or disciplines may find this material useful in developing simulations on other trade-environment disputes, following the model presented in the simulation described above.

Impact of Trade Liberalization on the Environment

Trade and trade liberalization may affect the environment in both positive and negatives ways. According to many economists, increased business activities create environmental impacts or negative “externalities.” This is because prices and markets don’t account fully for the environment costs they incur. Trade and investment liberalization may also put pressure on countries to lower environment standards (See Esty, 1994). This can happen in two related ways: (1) pressure is placed on countries to lower environmental standards in order to preserve/attract jobs; and (2) removal of trade barriers results in equalization of regulatory burdens toward the “lowest common denominator” (See Esty, 1994)

Trade can also have a positive impact on the environment. For example, some economists argue that trade can increase economic welfare and provide more resources for environmental protection. A World Bank Study showed that environmental quality decreases as GDP per capita grows (to approximately \$5000), but then *increases* as countries’ grow wealthier (See Dasgupta, Mody, Subhendu, & Wheeler, 1995). Elimination of trade barriers can result in a more efficient allocation of resources so that prices reflect true economic costs. For example, the removal of subsidies that support over-harvesting of timber or fish may lead to better resource management practices. This is one area in which environment and business groups have allied to urge continued progress under the WTO and other trade agreements.

In addition, the prospect of trade concessions may provide leverage for achieving environmental goals, such as the U.S. efforts during the NAFTA negotiations to use trade concessions as an enticement to encourage Mexico to improve its environmental protection (See Johnson & Beaulieu, 1996). Trade agreements may provide an opportunity to access the latest environmental remediation and prevention technologies by lowering tariffs and harmonizing standards and regulations that guide new product development. In addition, there may be positive externalities when early adopters take the first step towards legitimizing and standardizing environmentally sound business practices and technologies,

making it easier for other companies in the industry to implement similar technologies (See Nehrt, 1998).

Impact of Environmental Policies on Trade

In addition, environmental policies may affect trade flows. Many environmental agreements, such as the U.S. Endangered Species Act, use trade measures to penalize countries for not upholding environmental commitments. Environmental regulations can be perceived as disguised barriers to trade if countries use environmental protection as an excuse to limit imports. In this context, it is important to distinguish between regulations that apply to how a product is manufactured or harvested, versus those that focus on the final product's safety and quality (See Esty, 1994). Some countries have banned importation of products because they perceive the production methods in the exporting country to be environmentally harmful, however, most trade agreements prohibit countries from limiting imports of goods simply because they are produced in an environmentally damaging manner (versus those that pose a health risk once imported). This discrepancy is at the center of many of the trade-environmental disputes such as the tuna-dolphin case described below that has been among the most contentious in the international arena.

U.S.-Canada Dispute over Softwood Lumber

U.S. lumber producers have long alleged that Canadian provinces subsidize softwood lumber harvesting on provincial lands, and in so doing, contribute to unfair import competition to U.S. producers. In this dispute, however, U.S. environmental NGOs supported the U.S. complaints because of a belief that Canada's practices caused poor conservation practices, an interesting twist on the stakeholder roles assumed in the beer case (See Davey, 1996). This case has been ongoing for nearly two decades, and the persistent nature of the dispute makes for an interesting exploration of the entrenched nature of many cross-border disagreements that stem from different policies toward natural resources management. In this case, Canada's approach gives the federal and provincial governments significant control over the terms of timber harvesting, while in the U.S., the private sector is accorded greater influence, although it is the Canadian system that has been alleged to be more environmentally damaging.

North American Free Trade Agreement (NAFTA)

The North American Free Trade Agreement (NAFTA) served as a catalyst for the emergence of concerns about the impact of trade on the environment. Specifically, environmental NGOs criticized the U.S. Administration for pursuing the NAFTA, arguing that it would result in downward harmonization of standards, loss of sovereignty over environmental laws, and would legitimize the absence of public participation in environmental and other policies in Mexico. NAFTA's Supplemental Agreement on Environmental Cooperation calls for each country to work toward "high and improved levels of government protection of the environment," essentially promoting "upward harmonization" (See Johnson & Beaulieu, 1996; Menz, 1995). At the same time, the Agreement allowed a country or NGO to file a petition if a party exhibits a "persistent pattern of non-enforcement" of domestic environmental law (See NAFTA, 1994). The U.S. government argued this gave the agreement "teeth" because it would allow for trade sanctions if a country engages in a pattern of non-compliance, however, some NGOs criticized the final agreement because it failed to force more fundamental changes in environmental policies.

The Tuna-Dolphin and Shrimp-Turtle Cases

Under the 1994 Amendments to the Marine Mammal Protection Act (1972), the U.S. banned the importation of tuna from certain countries that permitted harvesting practices that resulted in dolphin mortality. The United States faced a GATT/WTO challenge from a number of the countries from which tuna imports had been banned over these restrictions, and is still unresolved (See Reinhardt & Vietor, 1996). This case revolved around *extraterritoriality* – the ability of one nation to impose its laws on another using trade restrictions as leverage – and represents one of the most important milestones in the history of trade-environment disputes. A similar dispute between the U.S. and several Asian countries surrounding the harm to turtles caused by shrimp harvesting was also brought before the WTO. In this case, a partial resolution was reached when the U.S. agreed to provide technical assistance to developing

countries through provision of turtle excluder devices (TEDs) that prevent turtles from getting caught in shrimp nets (See Kaczka, 1997).

Experience of the European Community (now European Union) and the Dispute over Genetically Modified Organisms

European experiences with trade-environment disputes have been consistently more supportive of environmental conservation. The development of European-wide environmental standards minimizes the problem of different levels of regulation affecting the costs of doing business across different jurisdictions, and this coordination of policies has resulted in a more integrated system of environmental laws and regulations (Esty, 1994). Most European countries have a progressive “packaging tax” that discourages excess use of packaging materials and greater sale of products in bulk. In addition, European regulators have severely limited the widespread adoption of genetically modified (GM) crop technology and the importation of GM foods, generating an ongoing dispute with the U.S., where GM technologies are used widely to enhance crops and animal production. In Europe, a concept known as the “precautionary principle” leads public policymakers to “assume the worst” when it comes to potential environmental threats, a qualitatively different approach than in the U.S. (See Aubert, 2000; Soule, 2003).

Reforming the WTO

Some have suggested that the GATT/WTO, the multilateral body that oversees trade disputes, be reformed to (1) require environmental assessments of trade agreements such as the report prepared by the Bush Administration on the environmental impacts of NAFTA (not a formal Environment Impact Statement); (2) allow for greater participation by nongovernmental environmental organizations in the trade agreement and dispute process; (3) change the burden of proof in a dispute resolution case over an environmental requirements so that burden would be on the party alleging that the practice was trade-restrictive rather than the one defending the practice; and (4) increase staff with environmental knowledge at the WTO (See Esty, 1994). More substantive proposals include: (1) creating a Global Environmental Organization to counter-balance the WTO and provide a forum for resolution of international environmental disputes; (2) negotiating a comprehensive global environmental code to provide more comprehensive participation in environmental obligations; (3) establishing that environmental treaties always take precedent over trade agreements (like NAFTA); and (4) allowing trade restrictions to target “process” in addition to final “product” characteristics (See Esty, 1994).

Recent Developments and the Rise of Nongovernmental Organizations

Environmental NGOs (ENGOs) have increasingly pushed to have greater access to the trade policy process, a system that has historically been limited to governments acting as agents of business, and, to a lesser degree, representatives of labor interests. One area in which NGOs expressed a great deal of interest is in the trade policy dispute settlement mechanism. The Uruguay Round agreement of the GATT/WTO explicitly makes provisions for cooperation with NGOs. In the Agreement, Article V(2) on *Relations with Other Organizations*, states that: “The General Council may make appropriate arrangements for consultation and cooperation with non-governmental organizations concerned with matters related to those of the WTO” (See WTO, 1995). The recognition of NGOs as influential actors is beginning to gain attention in the international relations and management fields (See Doh, 2003; Economist, 2000, 2001; Mathews, 1997; Simmons, 1998). Along with MNCs and international organizations, NGOs are increasingly viewed as significant actors in global affairs (See Keck & Sikkink, 1998). NGOs play a growing role in collecting and disseminating information, and working with governments, international organizations, other NGOs, and MNCs, in furthering environmental goals (See Doh, Newbury, & Teegen, 2003; Ottaway, 2001).

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Table 1

Energy Consumption per use for 12 oz. Beverage Containers

Container	Energy Use (BTUs)
Aluminum can used only once	7050
Steel can used only once	5950
Glass bottle used only once	3730
Recycled aluminum can	2550
Recycled steel can	3880
Recycled glass bottle	2530
Refillable glass bottle used 10 times	610

Source: Gaines, 1991