WRITTEN SUBMISSION OF THE DAIRY COMPANIES ASSOCIATION OF NEW ZEALAND (DCANZ)

19 MAY 2023

Introduction and overview

1. DCANZ makes this submission on behalf of its members with the aim of providing a practical perspective of how Canada's procedures for administering its dairy TRQs under CPTPP ('administration procedures' or 'procedures') are experienced by exporters. This perspective is informed by its members' interactions with importers in the Canadian market.

2. In explaining how Canada's administration procedures are experienced by its members, DCANZ will show in this submission that Canada fails to administer its TRQs in a manner that allows importers the opportunity to utilise TRQ quantities fully or to make allocations (to the maximum extent possible) in the amounts that importers request, and that its administration procedures are neither fair nor equitable. More specifically, it will show that Canada's administration procedures:

   2.1. impede development of the willing-buyer/willing-seller relationships that would otherwise enable Canadian importers and CPTPP exporters to take advantage of opportunities to achieve full quota utilisation;

   2.2. create additional and significant complexities that impede full quota utilisation; and

   2.3. are unfair and inequitable because they treat some importers more favourably than others, and lack predictability and consistency.

3. This submission is structured by first providing background on New Zealand's dairy trade with Canada and expectations for CPTPP market access. It then explains how Canada's administration procedures are experienced by its members. Finally, to further illustrate the issues, it provides a case study of trade conducted under the butter quota in 2021-2022.

Background – New Zealand dairy trade into Canada

4. Canada is an important dairy market for New Zealand, with imports of New Zealand dairy products dating back to 1893. Multiple DCANZ members have historical, current, and future interests in the Canadian market. These members differ in size, structure and product offerings, but overall represent a choice of willing sellers for Canadian dairy customers.

5. Canada incorrectly suggests in its Initial Written Submission (IWS) that New Zealand produces a limited portfolio of products suitable for exporting over long distances and further, that it restricts exports through licensing.[1] To the contrary, New Zealand has over 130 markets globally and exports the full range of dairy products covered by the CPTPP quotas. New

[1] At paragraphs 117 to 119. The export licensing system Canada refers to is designed only to allocate quota where other countries maintain quotas for access to their dairy markets under the WTO or certain free trade agreements. It does not apply to CPTPP trade.

Zealand dairy exports reflect the full 'bucket of milk'[2] and are not constrained by distance. In the 2020-22 period for example, New Zealand has exported UHT fluid milk with a shelf life of nine to 12 months and yoghurt with a shelf life 35-50 days to destinations with similar shipping timeframes as Canada.[3] More information on New Zealand's export profile can be supplied to the Panel on request.

6. DCANZ members are aware of significant interest in New Zealand dairy products in Canada within and beyond the better performing Butter, Cheese of all Types and Mozzarella quotas, and we reject Canada's claims that there is no demand for imports. In the past month alone, New Zealand Trade and Enterprise, an agency that works to support New Zealand companies' offshore commercial relationships, has approached DCANZ with a request from a Canadian distributor for companies that could build a range of New Zealand origin specialty dairy products including niche cheeses, yoghurt, and ice cream. Another request received in 2022 came directly from a Canadian consumer wanting access to 'a2' milk products for dietary reasons and citing lack of availability in the Canadian market. DCANZ can make relevant correspondence available to the panel on request. These examples reinforce previous experience of demand from within different segments of the Canadian market. Such demand is driven by various motivations, including consumer demand for niche and pasture-based provenance products.

7. Within Canada, CPTPP market access opening has been publicly welcomed by the foodservice[4] sector, while retailers have expressed concern over lack of access to quotas[5]. There is good reason to anticipate opportunity – the Dairy Farmers of Canada suggest that, based on a nationwide survey, one in five Canadians (i.e., over 7 million potential consumers) are not set in the view that dairy products must be Canadian-only[6].

8. Despite the difficulties discussed in this submission, DCANZ members have, since the first quota year, traded to some degree under CPTPP TRQs. This included some ingredient trade for processing of dairy products. Although, the experience of DCANZ's members is that *well over* half of their trade has been conducted with quota holders in the distributor category. This reinforces that it is distributors[7], further processors, retailers, and foodservice businesses who are the most natural commercial partners for New Zealand dairy exporters.

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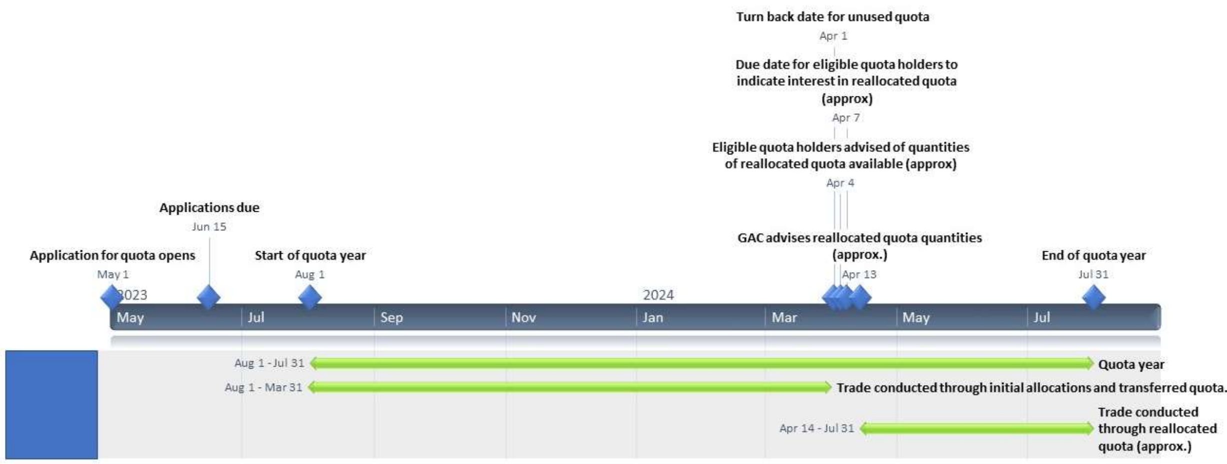
[2] That is, all milk components including butter, fat, protein, solids non-fat and whey.
[3] Includes UHT shipped to the Caribbean and yoghurt shipped to the US and UK. Source: Trade Data Monitor.
[4] https://www.restaurantscanada.org/industry-news/canadas-agricultural-sector-prepares-tpp-changes/ (accessed 17 May 2023).
[5] https://www.retailcouncil.org/tariffs-and-trade/ (accessed 17 May 2023)
[6] "77% of Canadians want to keep dairy Canadian" (source https://dairyfarmersofcanada.ca/en/blue-cow-logo/processors, date accessed 17 May 2023).
[7] An important point of clarification is that two types of entity seek quota in the 'distributor category': first, **trading desks** operate as 'match makers' between willing buyers and willing sellers but do not themselves use product; and second, **distributors** who operate a food distribution network and seek imports to put into their supply chains. The former category (trading desks) find demand with final end customers who may be processors, further processors, retailers or restauranteurs. New Zealand exports do significant business with this category of distributor.

9. Unfortunately, those importers (distributors) most likely to utilise the quotas are extremely limited in the quota they can access. They only receive small initial allocations, and we understand that to import they must either: (a) obtain **transfers** from the original quota holders (initial quota holders across all categories who do not wish to use it may transfer it) or (b) obtain allocations after unused quota is turned back and **reallocated** in the ninth month of the quota year. Regarding transfers, we understand that distributers often have to source multiple transfers of small allocations from a number of quota holders and consolidate them together so that they have quota of sufficient size to be commercially viable. We also understand (but have less visibility over) that some trade is conducted via quota that is 'rented' through buy-and-sell arrangements between processors and distributors.[8]

10. The following diagram provides an example timeline to show when reallocations occur for CPTPP quotas operating on a 1 August to 31 July quota year:



11. For the most part, trade conducted by DCANZ members occurs through quota that has been obtained through this system of transfers and reallocations. It is a system that is costly, burdensome, lacking in timeliness, and negatively impacts exporters and their import partners. Levels of trade remain suboptimal and exporters are unable to properly take advantage of the market access opportunities that ought to be available under CPTPP.

Development of willing-buyer/willing-seller relationships is impeded

12. To take advantage of potential demand for New Zealand product and fully utilise quotas, DCANZ members must be able to develop willing-Canadian-buyer-willing-New Zealand-seller relationships ('importer-exporter relationships'). But they are unable to do this because of the exclusive quota allocation of 80 to 85% for processors, and the resulting inability of business partners (such as distributors) to effectively and reliably access quota.

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[8] Where trade is arranged by one entity (usually a distributor) to be on-sold to another customer by using quota from a quota holder who has agreed to lease its quota but remains the 'importer of record'.

13. Importer-exporter relationships require a high degree of certainty of quota availability to allow commercial negotiation and contracting of supply. Having to rely on transfers and reallocations means that importers lack this certainty, and the development of commercial relationships with exporters is stymied for much of the twelve-month quota year.

14. The Canadian market participants for whom these procedures present obstacles are those whom, in DCANZ members' experience, have greater willingness to import and the capability to do so. Exporters are also denied the opportunity to build business directly with those entities who are not eligible for quota allocation at all, such as retailers or foodservice businesses.

15. We agree with Canada that processors are unlikely to operate against their own economic self-interest. It makes commercial sense that processors will, as compared to other entities, have limited interest in importing product that would compete with their own brands. Further, several processors have publicly stated their preference to use the Blue Cow 100% Canadian dairy label[9] for many of their products, which would prevent them from using imported product in those supply chains.

Additional and significant complexities impede full quota utilisation

16. When they apply for quota, distributors and further processors are not able to indicate the quantities they would like to receive or which best reflect their business objectives for the year; instead the application form seeks only an indication of the minimum quantity they would accept[10]. To secure initial quota holding and ensure eligibility for transfers and returned volumes later in the year applicants are incentivized to state the lowest amount possible (i.e. 1 kg). When Canada allocates the restricted volume in the pool across applicants, this has the effect of dicing the quota available to these participants into small equal volumes. Distributors and other importers who consequently cannot obtain sufficient quota volumes at the beginning of the quota year are reliant on obtaining quota through a system of transfers and reallocations. While we assume that Global Affairs Canada (GAC) compiles information on transfer activity and reallocation volumes, this is not made publicly available. This information would identify which quota holders are actually utilising their quota in comparison to those who were initially given quota, and would provide a full picture of where demand for quota lies and the burden imposed on importers who have to work through the transfer and reallocation system.

17. Importers reliant on transfers and reallocations do not know at the outset of the quota year what volumes of quota they might obtain or when. In these circumstances, it is extremely difficult, if not impossible, for importers to fully commit to a commercial contract for supply of product they may not be able to import and for exporters to manufacture product to meet market specifications for a market to which they may not otherwise be able to export.

18. Having information at the beginning of the quota year is important for exporters to plan their contracting, processing and shipping. Ability to successfully complete these processes

[9] See online at: https://dairyfarmersofcanada.ca/en/blue-cow-logo/processors (date accessed: 18 May 2023).
[10] https://www.international.gc.ca/trade-commerce/assets/pdfs/notices/2241E.pdf

diminishes as the quota year progresses. The reallocation system provides an extremely tight window for exports from New Zealand. By the time quotas are reallocated (typically up to two weeks after the turn back date) there are only three and a half months remaining in the quota year. This is a very short time in which to contract and ship product, let alone manufacture if customer specific tailoring is required. Our members report that the risks and costs associated with missing this window have a chilling effect on trade.

19. For New Zealand, with a pasture based and seasonal dairy system, peak production occurs in October and sharply tapers off in March/April. This is the very point of the quota year when reallocation occurs for many of the CPTPP TRQs. Having to wait until this point of the year to access quota puts a significant brake on planning a Canadian market strategy for New Zealand exporters of those products.

Canada's procedures are not fair and equitable

20. As experienced by exporters, the procedures are not fair and equitable.

    20.1. Processors have a significant advantage over other importers as the initial allocation of 80-85% they receive provides certainty they will obtain meaningful quota volumes and have the full quota year to plan their business. Other importers have no such certainty and must compete with each other to access and consolidate quota license from holders who have no plans to use it.

    20.2. It is unlikely that quota transfers occur at no additional cost, such that this routine 'clipping the ticket' could be viewed as a *de facto* tariff. The decision of some importers to make arrangements to build and consolidate quota is a commercial one, but the requirement to do so in order to build meaningful quota volumes is only imposed on some quota holders and not others.

    20.3. From an exporter's perspective, two hallmarks of a fair and equitable quota administration system are predictability and consistency. Canada's procedures lack both. DCANZ members do not know with certainty from one year to the next what quota volumes their importer partners will be able to access, or when, which as set out above, impedes trade. It is unfair and inequitable that some importers (and exporters) are doomed to rely on the transfers and reallocation process annually, while others who persistently transfer, turn back or otherwise do not use their allocation face no disincentive and continue to receive quota.

Case Study: the 2021-22 CPTPP Butter Quota (3,000 tonnes)

21. This case study summarises DCANZ members' experience with the butter quota[11] in 2021-22, demonstrating a lack of fairness and equity. The high quota fill rate for this year belies the effort and cost taken to achieve it, which comes at a impost on imports as well as unfair treatment of those importers willing to explore opportunities and risk penalty if reallocated

[11] The butter quota covers both butter and anhydrous milk fat (AMF)

quota cannot be used, or tariffs of 298.5% (or more[12]) if product lands after the end of the quota year, while importers who repeatedly hand back unused quota are not subject to penalties.

22. This quota year ran from 1 August to 31 July, with a turnback date for unused quota of 31 March. Eligible quota holders were advised of available reallocated quantities on 5 April and had to confirm their interest in receiving quota by 11 April. Reallocation quantities were confirmed in mid-April.

23. Initial allocation of volumes was as follows:

	Processor	**Further Processor**	**Distributor**
Share of quota	80%	10%	10%
Aggregate tonnes	2,400	300	300
No. of quota holders	9	3	20

24. The usage, reallocation, and fill rates were:

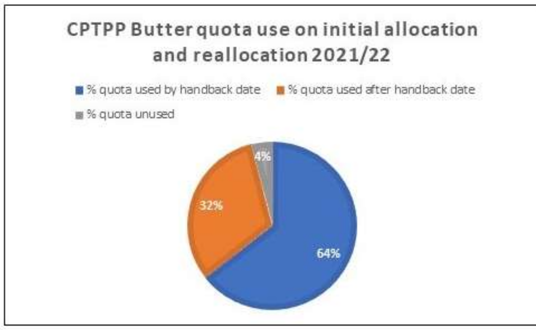
Volume made available to all eligible quota holders after turn back date	>1,100 tonnes
Percentage of initial quota used by original quota holder or transferred and used by other quota holders	63%
Percentage of initial quota allocation not used by original quota holder	37%
Final fill rate	96%

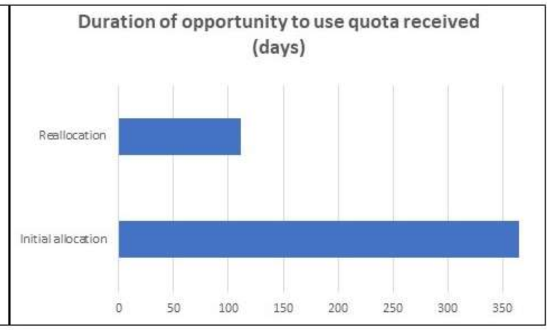
25. The approximate volume available after the turn-back date of 31 March was advised to DCANZ members by distributors who were assessing the viability of using the reallocated quota within the remaining four months of the quota year. We are not privy to the notices of reallocation, but our members' experience suggests that the original distributor and further processor quota allocations were likely almost fully used by the turn-back date, which suggests that processors **returned as much as 45% of their original allocation**. It is also not apparent to us how much of the initial quota trade was conducted by the quota holder themselves as opposed to being transferred (and therefore used by distributors or further processors).

26. As shown in the diagram below the initial allocation was not weighted to those motivated and with capacity to conduct the trade. The latter needed to work to consolidate volumes via transfers or wait till the last four months of the year to secure a business opportunity. Those importers reliant on reallocation volumes faced higher risks that product landing after the quota year would incur both a 298.5% out of quota tariff for butter and count as unused quota for which a penalty would apply on the following year's allocation. The result was less than full utilisation of a quota which would otherwise likely have been completely filled.

27. We expect that transparency from GAC on transfers and reallocation activity would confirm this picture.

[12] For AMF





Conclusion

28. This submission has shown how Canada's TRQ administration procedures negatively impact and distort the normal commercial, logistical and business drivers that would otherwise give rise to greater utilisation of the TRQs. Canada's procedures:

    28.1. favour Canadian processors whose exclusive initial allocation gives them a say in the import of products that compete directly with their own product;

    28.2. impede the development of the importer-exporter relationships required to pursue commercial opportunities;

    28.3. impose an unfair burden on non-processor importers (including further processors) who must engage in a complex and costly series of transfers to access and consolidate quota into commercially meaningful volumes;

    28.4. rely on a reallocation mechanism that unfairly concentrates much of the opportunity to trade into a short window at the end of the quota year; and

    28.5. create an unpredictable and uncertain business environment for exporters, resulting in a chilling effect on trade.

29. The experience of DCANZ's members shows an inherent bias in the system towards Canadian processors. This bias is at the core of the inequalities and inefficiencies in the system. It starts with the initial exclusive allocation of 80 to 85% of quota, and ripples through the system. Addressing this bias is critical if the system is to enable full quota utilisation. A decision that leaves open the opportunity for Canada to replace its current *de jure* allocation for processors with a *de facto* allocation (as is being litigated currently in the CUSMA dairy case) would generate additional concerns for us.

30. On behalf of its members, DCANZ thanks the panel for the opportunity to provide this written submission. We are at the panel's disposal to answer any further questions.

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