

**Report of  
The Commission of Inquiry  
Into Certain Allegations  
Concerning Commercial Practices of  
The Canadian Dairy Commission**

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# **The Commission of Inquiry Into Certain Allegations Concerning Commercial Practices of The Canadian Dairy Commission**

Commissioner

**The Honourable Mr. Justice Hugh F. Gibson**

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Commission of Inquiry into  
Certain Allegations Concerning  
Commercial Practices of the  
Canadian Dairy Commission



Commission d'enquête sur  
certaines allégations  
concernant des transactions de la  
Commission canadienne du lait

Commissioner/ Commissaire  
Honourable Mr. Justice Hugh F. Gibson

December 29, 1980.

TO HIS EXCELLENCY

THE GOVERNOR GENERAL IN COUNCIL,

May it Please Your Excellency,

By Order in Council P.C. 1979-1586 dated  
May 25, 1979, I was appointed the Commissioner  
to inquire into and report upon certain allega-  
tions concerning commercial practices of the  
Canadian Dairy Commission. I have completed  
the duties prescribed in the said Order in  
Council and now submit my Report.

A large, stylized handwritten signature in black ink, which appears to read "Hugh F. Gibson".



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## CHAPTER I

### OVERVIEW OF THE INQUIRY

This Inquiry was established under the Inquiries Act, R.S.C. 1970, Chapter I-13, by Order-in-Council P.C. 1979-1586 on the 25th day of May 1979. The particular matter connected with the good government of Canada, and the conduct of the particular part of the public business of Canada, into which the Commission of Inquiry was directed to inquire concerned certain allegations made by Schafer Bros. Ltd. as enunciated by Michel Choquette with respect to dealings of the Canadian Dairy Commission, its officers and employees with Schafer Bros. Ltd. during the years 1966 to 1977, relating to the export from Canada of skim milk powder.

In general terms, the allegations and complaints of Schafer Bros. Ltd. and Michel Choquette are of two types. First, they are complaints or allegations that, beginning in January 1968, the Canadian Dairy Commission was not even-handed or fair in the administration of its policies concerning the sale of skim milk powder and with respect to the public funds it controlled and could make available in the form of subsidies to private traders; that it took over the market or business developed by Schafer Bros. Ltd. with the Mexican government purchasing agency known as CONASUPO, that in connection with such taking over it favoured certain private traders who competed with Schafer Bros. Ltd.; and that in the process certain Canadian Dairy Commission officials received kickbacks from such private traders. Second, they are complaints and allegations that the Canadian Dairy Commission, a Crown agency, misconceived its role in respect of export sales of skim milk powder. Different and broader policy questions not exclusive to Schafer Bros. Ltd. are raised in this second general group of complaints and allegations.

The Canadian Dairy Commission is a marketing board with powers extending to export marketing, a Crown corporation created by the *Canadian Dairy Commission Act*, R.S.C. 1970, Chapter C-7. The statutory objects of the Canadian Dairy Commission are to provide efficient producers of milk and cream with the opportunity of obtaining a fair return for their labour and investment and to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality.

CONASUPO (Compania Nacional de Subsistencias Populares) superseded an earlier Mexican purchasing agency known as CEIMSA in 1959. The

Mexican Government assumed complete control over it in 1965. CONASUPO is, and was, the sole and exclusive authority for importing skim milk powder into Mexico. In addition to skim milk powder, it buys a wide variety of agricultural products and owns and operates several small stores, particularly in the poorer areas of Mexico City. With respect to the skim milk powder it buys, part is processed through its reconstitution plant for sale in its stores and part is sold to certain public corporations for processing into evaporated milk and similar types of products for resale by those corporations in Mexico.

The dairy product that this Commission of Inquiry is concerned with is skim milk powder.

Schafer Bros. Ltd. is a small exporter and importer dealing mainly in agricultural products and has its head office in the City of Montreal. Commencing in 1968, and from time to time thereafter, David Schafer, its President, and George Schafer, his son, complained to federal government officials about certain policies and practices of the Canadian Dairy Commission. The complaints were of the type set out above and had to do, insofar as Schafer Bros. Ltd. is concerned, with the treatment, or perceived treatment, of it by the Canadian Dairy Commission, its officers and employees in connection with the export sale of Canadian skim milk powder to Mexico and to a lesser extent to other foreign markets.

Beginning about 1976, these complaints and allegations were consolidated into voluminous detailed written accounts by Michel Choquette for David Schafer. These detailed written accounts were prepared apparently for the purpose of persuading senior government officials to cause compensation to be paid to Schafer Bros. Ltd., essentially based on its claim that the Canadian Dairy Commission in 1971 took over the business of exporting and selling Canadian skim milk powder to CONASUPO, which business prior thereto Schafer Bros. Ltd. had developed and built up by the expenditure of much time and monies, and also on other matters. In respect to these other matters, these written accounts of complaints and allegations prepared by Michel Choquette otherwise generally painted a disturbing picture of the Canadian Dairy Commission, agent of the Government of Canada, in acting narrowly and vindictively with respect to Schafer Bros. Ltd. and its officers David Schafer and George Schafer, and generally in conducting its business without any proper regard for the broad objects and public interest with which it was charged by its enabling statute, and further that it conducted its affairs without any effective system of accountability.

The Order-in-Council P.C. 1979-1586 directed me to define the issues raised by the allegations, to determine all relevant facts, to ascertain whether or not the Canadian Dairy Commission, its officers and

employees during the period 1966 to 1977 have acted lawfully and fairly in their dealings with Schafer Bros. Ltd., and to report with respect to these matters. In addition, it was directed that the report include a recommendation as to whether or not any compensation should be paid to Schafer Bros. Ltd., and such other recommendations as I might deem appropriate.

In order to obtain a general understanding at this stage of the essence of the allegations made by Schafer Bros. Ltd. as enunciated by Michel Choquette, of which, as stated, the principal ones relate to the export sales or potential sales of Canadian skim milk powder to CONASUPO, it should be stated that the evidence disclosed that during the 1960's David Schafer made certain efforts as a private exporter to develop a demand in Mexico for Canadian skim milk powder. He did this by seeking to encourage certain officials in the purchasing agency, CONASUPO, to buy Canadian skim milk powder.

At the time that David Schafer was making his efforts as a private exporter to develop a demand in Mexico for Canadian skim milk powder, he did not know (in fact he did not know until evidence was given at this Inquiry) that other private Canadian traders at the same time, and even prior to the time David Schafer commenced to do so, were and had been interested and active, during the 1960's, in attempting to develop a Mexican market for Canadian skim milk powder.

David Schafer apparently envisaged that Schafer Bros. Ltd., if successful in making export sales to CONASUPO, would obtain supplies of skim milk powder from the stocks or inventory of the Canadian Dairy Commission, which purchased skim milk powder under a price support program.

By the latter half of the 1960's CONASUPO began to purchase significant quantities of skim milk powder in the export market. From that time to date the purchases have progressively increased, and in recent years have been quite substantial.

In 1968, the Canadian Dairy Commission sought, itself, to make a direct sale to CONASUPO of Canadian skim milk powder in competition with Canadian private exporters, including Schafer Bros. Ltd. In 1971, the Canadian Dairy Commission discontinued the export subsidy it had previously made available and paid to private exporters in connection with sales of Canadian skim milk powder to CONASUPO. Since 1971, the Canadian Dairy Commission has been the exclusive Canadian supplier of skim milk powder to CONASUPO.

In order to put these complaints or allegations in a proper context for analysis and determination, it was necessary for this Commission to examine certain general aspects of the policies and programs of the

Canadian Dairy Commission during the relevant years. In doing so, it was necessary to review the powers conferred upon the Canadian Dairy Commission pursuant to its enabling statute and to consider, in relation to the acts which are the subject of the complaints or allegations, whether or not the policies, practices and controls employed by the Canadian Dairy Commission were within or beyond the powers granted to the Canadian Dairy Commission, whether they were consistent with the objects of the Commission as prescribed by Section 8 of the *Canadian Dairy Commission Act*, whether they were necessary to achieve those objects, and whether the powers of the Commission were exercised within the framework of any general policy or criteria adopted to achieve the objects of the Canadian Dairy Commission as prescribed by Section 8. For example, an export subsidy perhaps would not have been necessary at all were it not for the large Canadian surpluses of skim milk powder which existed from time to time during the relevant years and which in turn resulted from the price support programs implemented by the Canadian Dairy Commission. Because of the price support program for skim milk powder, the Canadian Dairy Commission had purchased the surplus skim milk powder at a price above the international price.

A further reason for examining certain general aspects of the policies and programs of the Canadian Dairy Commission during these relevant years so as to put the complaints or allegations in a proper context, was to avoid the risk that actions or policies of the Canadian Dairy Commission might be unfairly criticized if they were examined outside the perimeter of the statutory objects and purposes of the Canadian Dairy Commission. This is especially important because certain public policies require flexibility in their administration in order that they might be made effective.

Section 8 of the *Canadian Dairy Commission Act* defines the objects of the Canadian Dairy Commission as follows:

"8. The objects of the Commission are to provide efficient producers of milk and cream with the opportunity of obtaining a fair return for their labour and investment and to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality."

Section 9 sets out the powers of the Canadian Dairy Commission. "Subject to and in accordance with any regulations made under this Act", the Canadian Dairy Commission is, *inter alia* authorized to purchase any dairy product, to export or sell or otherwise dispose of any dairy product purchased by it, to make payments for the benefit of producers of milk and cream for the purpose of stabilizing the price of those products, and to do "all such acts and things as are

necessary or incidental to the exercise of any of its powers or the carrying out of any of its functions under this Act."

Section 11 requires the Commission to comply with any directions from time to time given to it by the Governor in Council or the Minister of Agriculture, but there have been no such directions.

Section 12 authorizes the Governor in Council to make regulations pertaining to various subjects, but there have been no relevant regulations.

In order to assess the relevant implications of Sections 8 and 9 of the *Canadian Dairy Commission Act*, evidence was sought and received from expert economists, from disinterested persons with long and thorough experience in the dairy industry in Canada, and from several officials past and present of the Canadian Dairy Commission. As to the latter, evidence was given by the three persons who have at various times been Chairman of the Canadian Dairy Commission at various times since its creation to the present time, namely, S.C. Barry (1966-1973), E.J. Powers (1973-1976) and G. Choquette (1976 to the present). Three other persons who have served as members of the Commission also testified, namely, H.M. Johnson (1973-1979), E.G. Hodgins, (1977 to date), and J. Thibaudeau (1967-1976), as well as did other marketing and policy personnel of the Canadian Dairy Commission.

Each particular allegation of fact made by Schafer Bros. Ltd. and enunciated by Michel Choquette was

examined carefully. David Schafer, George Schafer and Michel Choquette were the first witnesses regarding the facts in issue and they gave extensive evidence of what was being alleged. They also stated their interpretations of what the documentary evidence meant to them. They were cross-examined by various counsel, including counsel for the Canadian Dairy Commission. Certain officials of the Canadian Dairy Commission also gave evidence, stated their interpretations of the documentary evidence and were in like manner cross-examined by various counsel. Certain personnel of other private traders also gave evidence and they, in turn, stated their interpretations of the documentary evidence and also in like manner were cross-examined by various counsel.

All documentary evidence that was thought to be relevant in any way to the allegations was made part of the evidence of this Inquiry.

In addition, a number of officials of CONASUPO and of private traders or agents in Mexico were interviewed in Mexico-City in the presence of Michel Choquette and counsel for a number of the parties, all such parties and their counsel having been invited to be present.

All the evidence, both oral and documentary, was adduced in public at all times and a transcript of the oral testimony and copies of the documentary evidence were made available for public inspection at the Commission of Inquiry offices during all business hours.

## **CHAPTER II**

### **NATURE AND CONDUCT OF THE INQUIRY**

#### **(A) ORDER-IN-COUNCIL**

By Order-in-Council P.C.1979-1586, dated the 25th day of May 1979, the Honourable Mr. Justice Hugh F. Gibson was appointed a Commissioner, pursuant to the provisions of Part I of the Inquiries Act, Chapter I-13 of the Revised Statutes of Canada 1970, and was directed to inquire into certain allegations made by Schafer Bros. Ltd. as enunciated by Mr. Michel Choquette in respect of dealings of the Canadian Dairy Commission, its officers and employees with Schafer Bros. Ltd. of Montreal, Quebec, during the years 1966 to 1977, relating to the export from Canada of skim milk powder.

The Order-in-Council specifically directed that the issues raised by the said allegations be defined, that all facts relevant to the said issues and allegations be determined, and that it be ascertained whether the Canadian Dairy Commission, its officers and employees have acted "lawfully and fairly" in their dealings with Schafer Bros. Ltd.

The Order-in-Council directed that the report on these matters include a recommendation as to whether any compensation should be paid to Schafer Bros. Ltd. and, if so, the basis on which such compensation should be determined. It also invited such other recommendations as the Commissioner might deem appropriate.

The Order-in-Council is reproduced in full in Appendix 1 to this Report.

#### **(B) GENERAL NATURE AND ESSENCE OF THE ALLEGATIONS AND OF THE ISSUES RAISED**

The allegations are contained in voluminous written submissions made by Michel Choquette for David Schafer and to a lesser extent George Schafer to various Government of Canada officers and officials during 1976, 1977, and 1978. The role of Michel Choquette is discussed in part (E)3 of this Chapter, below.

The substance of the main allegations may be summarized as follows:

1. Schafer Bros. Ltd. alleged it had expended much time and money since the late 1950's attempting to develop an export market in Mexico for surplus Canadian skim milk powder. Regular trips

were made by David Schafer to Mexico, personal contacts were established with officials of CONASUPO, Mexican government officials were made aware of the merits of Canadian skim milk powder, and knowledge was gained about Mexican requirements and purchasing specifications. All this was done with the knowledge and approval of senior officials of the Agricultural Stabilization Board and, since the establishment of the Canadian Dairy Commission in 1966, with the same general encouragement of senior officials of the Canadian Dairy Commission. David Schafer says that he was led to understand by those government officials that in the event that Mexican demand for surplus Canadian skim milk powder materialized, he could count on the cooperation of the Agricultural Stabilization Board or the Canadian Dairy Commission, as the case may be.

2. In January, 1968, when the first major possibility arose that Schafer Bros. Ltd. might sell skim milk powder to Mexico, not only did the Canadian Dairy Commission refuse supplies to Schafer Bros. Ltd. but it bid to CONASUPO directly. David Schafer was advised of this at a meeting with the Canadian Dairy Commission on January 24, 1968, and from that date forward things seemed to go downhill, at least so far as David Schafer's trust in the officials of the Canadian Dairy Commission was concerned. For reasons that are more fully explained below in the Report, David Schafer felt that the Mexican market for surplus Canadian skim milk powder properly belonged to him in a proprietary way, and that he had been betrayed by a Canadian government agency that was acting beyond its proper scope and function.
3. David Schafer and his son, George Schafer, the owners and senior officers of Schafer Bros. Ltd., felt that on various occasions between 1968 and 1971 the senior officials of the Canadian Dairy Commission deliberately discriminated against Schafer Bros. Ltd. and gave favoured treatment to particular competitors of Schafer Bros. Ltd. The primary individual target for criticism by Schafer Bros. Ltd. was Dr. S.C. Barry, who was Chairman of the Canadian Dairy Commission during this period, although virtually every Canadian Dairy Commission official who had anything to do with Schafer Bros. Ltd. also came under attack. The principal incidents of alleged discrimination had to do (i) with the sale by the Canadian Dairy Commission of ageing skim milk powder at a very low price to another exporter in August 1968 for resale outside the western hemisphere; (ii) with misleading information and inflexible financial conditions in connection with a 770 ton sale in January 1969 (which was the

first-and-only-sale that Schafer Bros. Ltd. actually made to CONASUPO) which made performance of the contract more difficult and expensive than it should have been; (iii) with misrepresenting a key fact to David Schafer in March 1969 with the result that Schafer Bros. Ltd. lost out to one of its Canadian competitors on a large contract with CONASUPO at that time, and (iv) with providing confidential bidding information to competitors of Schafer Bros. Ltd. in 1969 and 1970.

4. In 1971 the Canadian Dairy Commission discontinued the payment of export subsidies to private exporters in connection with the sale of Canadian skim milk powder to CONASUPO, which was becoming Canada's single largest foreign customer for skim milk powder. This was the alleged explanation of the fact that all the CONASUPO business was thereafter handled directly by the Canadian Dairy Commission.
5. In 1976, at a time when Canadian Government surpluses of skim milk powder were abnormally large, Schafer Bros. Ltd. lost out in a bidding contest with suppliers from other countries to supply very substantial amounts of skim milk powder to the Philippines over a period of three years. Schafer Bros. Ltd. says that the Canadian Dairy Commission should have given better technical support in connection with that bidding contest, and that the Canadian Dairy Commission was not sufficiently aggressive in assisting private exporters.
6. In 1977 the Canadian Dairy Commission decided to appoint a Canadian exporter to act as its agent in connection with its sales to CONASUPO, and it appointed someone other than Schafer Bros. Ltd.

Other allegations are also made but they are of a much more minor nature. The statement of allegations is reproduced in full as Appendix 5 to this Report.

In addition also, Schafer Bros. Ltd. and Michel Choquette make certain allegations indirectly in the form of innuendo. It may be that the intent of these allegations was to convey the impression that allegations were being made when in form perhaps they were not; but the result of the form in which the statements were made was to convey the impression to third parties that there were illegal kick-backs from certain private traders in Canadian skim milk powder to officials of the Canadian Dairy Commission in return for favoured treatment afforded those private traders by Canadian Dairy Commission officials. An example of the form of these allegations is as follows:

"In addition, if it were to be proven that certain officials of the Canadian Dairy Commission received illegal "kickbacks" for their preferential treatment of Messrs. Gonzalez and Chisholm, or even extended favoured treatment to these traders without receiving supplementary remuneration, then this secretive transfer of the Mexican market for Canadian skim milk powder to these favoured individuals would surely constitute legal grounds for prosecution. "Furthermore, if, in spite of the Canadian Dairy Commission's "official" statements that by 1971 it had monopolized the Mexican market for skim milk powder and that consequently it was no longer giving export subsidies to private traders for sales of this commodity to Mexico, it could be shown that the same favoured Canadian exporters or any other traders received subsidies for sales to CONASUPO which the Dairy Commission refused to extend to Schafer Bros., it is probable that a court of law would find the past senior officials of the Commission guilty of fraud." (Exhibit 6, Vol. VI, p. 175)

In short, the gist of the allegations of Schafer Bros. Ltd. and Michel Choquette against the Canadian Dairy Commission, its officers and its employees, is that the Canadian Dairy Commission abused its powers over large stocks of skim milk powder and abused its power to determine the existence and amount of export subsidy by acting in a manner that was sometimes discriminatory against Schafer Bros. Ltd., that was unfair in view of the investment of time and money expended by Schafer Bros. Ltd. in developing the Mexican market for surplus Canadian skim milk powder, that may sometimes have been criminal, and that may sometimes have been outside the statutory powers of the Canadian Dairy Commission.

In addition, it is in substance alleged that the Canadian Dairy Commission during the subject period, 1966-77, did not competently and adequately discharge its statutory responsibilities. It is alleged that some of the general policies and practices of the Canadian Dairy Commission were shortsighted, of insufficient assistance to the private sector, and sometimes even harmful to the private sector. David Schafer and George Schafer both felt that the Canadian Dairy Commission was not working hard enough at what it should be doing, namely, helping the private sector to get rid of Canada's surplus skim milk powder, and that it was doing far too much in the nature of direct export sales itself.

Schafer Bros. Ltd. says that as a result of the acts of the Canadian Dairy Commission, which are alleged to be unlawful and unfair, Schafer Bros. Ltd.

has suffered a substantial loss of investment and profits for which it should be compensated.

David Schafer says that he chose not to sue in the courts, but instead chose to appeal to the Government on a "moral" basis. One result of his avoiding the courts was that until this Inquiry took place there was no proper forum for accomplishing an organized and complete disclosure of all relevant documents and information in such a way that the principal antagonists could properly confront each other.

### **(C) PRIOR INVESTIGATIONS OF THE ALLEGATIONS**

Beginning in late 1974 a series of assessments of one form or another were made of the allegations and claims of Schafer Bros. Ltd. by various persons in government. The Minister of Agriculture and the Privy Council Office both obtained assessments or opinions on aspects of the matter from members of their departmental staffs.

These assessments and opinions did not satisfy Schafer Bros. Ltd., Michel Choquette, or the Honourable Warren Allmand, who continued to press for a more comprehensive and independent investigation. In late 1977 or early 1978, the Department of Justice was asked to investigate and report on all aspects of the matter. It reported in writing in 1978.

By letter dated September 19, 1978, addressed to the Prime Minister, Michel Choquette was highly critical of the Department of Justice investigation and report. Excerpts from his lengthy letter, which was marked as Exhibit 6, Volume IX (G) in this Inquiry, are as follows:

"Although it is identified on its title page as an 'Inquiry', the report prepared by Mr. J.S. Milligan and signed by Mr. Hayim Calof could much more properly be called an outright defense of the Dairy Commission's position. Mr. Milligan often seems to be acting more as an attorney for Mr. Barry and the Dairy Commission than as an objective investigator. Certainly it is difficult to believe, in reading the report, that matters were approached openly and without bias by Mr. Milligan.

"Furthermore, the report contains serious errors of fact and orientation, and totally ignores many key questions raised in my formal presentation.

"What the Department of Justice has produced is, in my opinion, no more than a gilded, updated edition of the old Dairy Commission story, with all the contradictions and feeble arguments preserved. It is an insult to the intelligence of all of us who, for

several years now, have been asking for a truly objective and independent investigation...

"It is extremely disturbing to learn from the list provided at the back of the Justice Department's report that of 18 persons interviewed by Mr. Milligan, 14 have a direct connection with the Dairy Commission or with its predecessor, the Agricultural Stabilization Board, or with the Department of Agriculture. The only person openly critical of the Dairy Commission who was interviewed is myself. And it should be noted that I was contacted by Mr. Milligan only after I had written to Mr. Calof to point out that I had not been contacted.

"Moreover, although Mr. Milligan told me when we first spoke that he would be coming to Montreal to spend as much time as would be necessary to go over everything with me in detail, he later chose, for reasons better known to himself, not to pursue his discussions with me beyond one or two preliminary meetings in Ottawa. At these meetings, matters relating to Mexico were barely touched upon. I was consulted almost exclusively about a potential milk powder sale to the Philippines, which is only a small side issue in the Schafer Bros. case, and one upon which my written presentations had already made it quite clear no moral or legal claim is based.

"Not only does the report concentrate very heavily on information obtained from individuals with an interest in the Canadian Dairy Commission; it also invariably takes these individuals at their word without the slightest trace of skepticism...

"More than anything else, it is the general attitude which I feel must change if this whole matter is ever to see the light of day. Until now the tendency in Ottawa has been to treat the Schafer case as an attack at the civil service rather than as an opportunity to right a possible wrong.

"It seems clear to me that what is required now more than ever is a truly objective third party prepared to approach this unusual case with an open mind and to probe as deeply as necessary.

"I believe that the terms of reference may have to be wider than those which were set out as guidelines for Mr. Milligan to follow, and that the investigator's mandate should make it easier for him to obtain documents from the private sector and should enable him to question witnesses with the advantage



of being able to inform them that whatever they say will officially go on record.

"What I am suggesting, of course, is an investigation set up under the *Inquiries Act*.

"However, at the same time as the questions of civil, administrative and possibly criminal liability are being looked into, the commissioner or commissioners should be asked quite specifically to consider the moral side of the case as well, since this has never really been given proper attention."

None of the reports of the previous assessments or investigations were made part of the record of this Inquiry and I did not refer to them in any way. This Inquiry was an inquiry *de novo*.

#### (D) METHOD OF CONDUCTING THE INQUIRY

A Commission appointed under the *Inquiries Act* has a duty to investigate and search out the facts and to avail itself of all reasonable or apparent sources of information, giving a wide scope to the inquiry, in order to report fully on the facts. It is not a trial, and there is no prescribed practice or procedure that must be followed; a Commissioner is free, indeed duty-bound, to obtain all reliable information by whatever means appear to be necessary or appropriate. The principal requirement is that the inquiry, and the report, be honest, fair and impartial.

The Inquiry provides a forum in which any member of the public may give any information concerning the subject matter of the inquiry. As a consequence it is essential that the inquiry be conducted in public as far as possible, with all interested persons having the opportunity to present evidence and with others having the opportunity to confront them with questions or to present conflicting or differing evidence.

It was important to conduct the entirety of this particular inquiry openly and in public, and this was done from beginning to end. There were no *in camera* sessions to take evidence, no private telephone calls and no communications conveying relevant subject matter that were not marked as exhibits or otherwise communicated to all interested persons. Where inquiries by Commission staff turned up relevant information, that information was made available to all interested persons in such a manner that it could be openly challenged and assessed.

All of the oral evidence, except for the interviews held in Mexico, was given under oath at public hearings, with transcripts taken. In order to assist all interested persons and to obtain as much reliable evidence as possible, without any impairment of anyone's opportunity to present his case in full, most of the voluminous documentary evidence filed in an

organized, chronological way at the commencement of the public hearings, and, near the end of the inquiry, certain unsworn interviews were held in Mexico in the presence of counsel or representatives of all interested persons who wished to attend. These latter procedures are appropriate in public inquiries so long as basic public interests of openness and fairness are observed (see, for example, *Re the Ontario Crime Commission, Ex parte Feeley and McDermott*, [1962] O.R. 872 (C.A.); *R. v. Deputy Industrial Injuries Commissioner, Ex parte Moore*, [1965] 1 Q.B. 456 (C.A.); and *Selvarajan v. Race Relations Board*, [1976] 1 All E.R. 12 (C.A.).) These cases review the principles prescribing that a Commissioner under the *Inquiries Act* is entitled, and obliged, to adopt the most effective and expeditious procedures consistent with fairness and reliability.

The Order-in-Council establishing this Commission of Inquiry specifically authorized the Commissioner "to adopt such procedures and methods as he may from time to time deem expedient for the proper conduct of his duties".

One of the first steps was to formulate and make available to the public the *Rules of Practice and Procedure* that would be followed. These Rules, reproduced as Appendix 4 to this Report, were prepared in order to facilitate an organized presentation of all evidence in a manner that would minimize the risk of surprise at public hearings, that would enable everyone to decide in advance whether he wished to be in attendance when certain evidence was given, and that would facilitate advance preparation of questions to be directed to the witnesses giving such evidence. The key requirement was that detailed written evidence statements be filed sufficiently in advance of the hearing where the evidence was to be given in order to meet these objectives. The *Rules of Practice and Procedure* also notified all interested persons and members of the public of the way the inquiry would be conducted, where documents could be inspected and information obtained, and so on.

The existence of the *Rules of Practice and Procedure*, the general nature of the Inquiry, and the date of the public Organizational Hearing were communicated widely to the Canadian public across Canada by means of a Public Notice (see Appendix 2) published in newspapers, broadcast by radio, and sent to a large number of industry organizations, governmental bodies, universities, and individuals who were thought to have a possible interest in one or more aspects of the inquiry. Anyone who wished to receive notices of the specific dates of subsequent hearings was invited to advise the Registrar of that wish, a special mailing list was maintained for that purpose, and advance notices of all hearings held throughout the inquiry were given to all persons who indicated a wish to be so advised. (See Appendix 7)

Since the Order-in-Council had directed the Commissioner to inquire into the allegations made by Schafer Bros. Ltd. and Michel Choquette, it was essential at an early stage to study the voluminous writings of Michel Choquette and the documents he referred to (Exhibit 6, vols. I to IX — over 2300 pages in total), in order to distill the precise allegations and to define the issues so as to provide a framework which would ensure a thorough and efficient inquiry, while giving full opportunity to all interested persons to submit any relevant evidence.

On the basis of this documentation Commission counsel prepared a suggested statement of the allegations, together with a further document setting out their suggested definition of the issues raised by such allegations. These two documents were deposited for public inspection at the Commission's offices and were filed at the public Organizational Hearing which was held on November 23, 1979 at Ottawa.

In addition, formal requests were made, directed to a number of other possible sources of documents, including individuals, private corporations, government agencies and departments, to produce such relevant documents as they had in their possession or control. Such additional documents, when received, were studied in light of the allegations and issues. Such documents as were deemed relevant or possibly relevant by Commission counsel, including certain classified government documents for which declassification was sought and obtained, were bound in six volumes and were also filed at the Organizational Hearing (Exhibit 12, Vols. 1 to 6 — 1211 pages). Approximately 600 pages of further relevant documents were filed as exhibits by Commission counsel after the commencement of public hearings as other documents came into the possession of the Commission of Inquiry.

Finally, certain Commission advisors, as requested by me, prepared and filed extensive statements and expert opinions describing the operations of the Canadian Dairy Commission during the years 1966 to 1977 relating to the export from Canada of skim milk powder; and providing an outline of the economic aspects of the inquiry.

After hearing all representations from counsel for all interested parties and those others who wished to make representations, I determined what the allegations were and defined the issues raised by the said allegations; and I then pronounced a statement of the allegations and of the issues raised by the allegations in accordance with Rule V(3) of the *Rules of Practice and Procedure*. The *Statement of Allegations* and the *Issues raised by the Allegations* as so settled appear as Appendices 5 and 6 to this Report.

Evidence statements were filed by witnesses, and the Registrar of the Commission of Inquiry having

duly notified the interested parties prior to each hearing, I as Commissioner held public hearings in Montreal, Hull and Ottawa on the following dates: December 4,5,6 & 7, 1979; January 14,15,16,17 & 18, 1980; February 4,5,6,7,8,14 & 15, 1980; March 10,11,12,13 & 14, 1980; May 28, 29 & 30, 1980; June 25, 1980; and July 2, 1980 (for details, see Appendices 8 and 9.)

The evidence of David Schafer, George Schafer and Michel Choquette was heard first, and in Montreal where they reside. Many other witnesses were heard and cross-examined by counsel for all parties who wished to do so. Many documents were filed, either by witnesses or by Commission counsel, and were made available for public inspection at the Commission's offices.

Counsel for interested parties submitted written arguments on different occasions regarding the allegations and the issues based on the evidence presented to me.

## **(E) GENERAL COMMENTS ON THE EVIDENCE**

### **1. David Schafer**

David Schafer was about 82 years of age at the time the hearings commenced. Because of this fact, and because he was the principal complainant, he was the first witness to be heard regarding the allegations of fact. Previous investigations had apparently not heard any evidence from him directly. Because of his age, he was unable to testify for any long period in any day. His memory of events was not as clear as it probably was some years ago. His suspicion of the Canadian Dairy Commission and its officers and officials was evident in his testimony. Many of the answers he gave in response to questions on cross-examination by various counsel were not really responsive to the questions. The reason for this was a combination of the adverse effects of his age on his memory, and his suspicion of the Canadian Dairy Commission and its officers and employees.

As a consequence, in the determinations made in this report account is taken of these frailties and any consequent deficiencies in his evidence so as to not in any way detract from the position he was submitting in respect to the allegations and issues of this inquiry.

### **2. George Schafer**

George Schafer, son of David Schafer, was the other officer of Schafer Bros. Ltd., during the years 1966 to 1977. He was 42 years of age at the time of the commencement of the hearings. He is not and never was the businessman that his father was. He has an unfortunate manner which manifests itself in the irritation of most persons with whom he deals, and especially any Government officials. His conduct

and attitude towards such officials, on many occasions, cannot be categorized other than as abusive.

He is not well, suffering from diabetes. He was not truthful on certain minor collateral matters having nothing to do with the subject of this Inquiry. He did not demonstrate any substantial or outstanding knowledge of the milk industry, unlike many of the other private traders such as the Bishops of Eastern Townships Produce Ltd., Mr. Pariseault of the Granby Co-op and currently with la Coopérative Fédérée du Québec, Messrs. T.A. Chisholm and W.I. Pelley of Ronald A. Chisholm Ltd. and Mr. Samuel Ault.

George Schafer has certain beliefs, and certain views arising out of them, which he expressed in correspondence and orally which are irrelevant to the subject matter of the Inquiry but, because he expressed them, did not assist in giving credence to the complaints and allegations of Schafer Bros. Ltd.

### 3. *Michel Choquette*

Michel Choquette is a 42-year old writer, entertainer and filmmaker from Montreal. He is no relation to Gilles Choquette, who has been the Chairman of the Canadian Dairy Commission since 1976.

Michel Choquette was the author of the documents which form the basis of the statements of the allegations and issues. He is an articulate, intense person. He obviously believes in the worthiness of the cause of David Schafer. He conceived his function as being to enunciate, and he did enunciate, the beliefs and position of David Schafer. His sources of information in the main were David Schafer and, to a lesser extent, George Schafer, his interpretation of certain documents, (all of which documents are before the Commission of Inquiry) and certain conversations he had with Gilles Choquette when the latter was Executive Assistant to the then Minister of Agriculture. He had no personal interest in the cause he espoused. Instead, what he did was marshal the facts for David Schafer.

In early 1974, Michel Choquette was told by a mutual friend of his and the Schafers of the difficulties that Schafer Bros. Ltd. believed it was having with the Canadian Dairy Commission. This mutual friend knew that Michel Choquette had a strong general interest in the control and supervision of discretionary power exercised by government bureaucracy. Michel Choquette was introduced to David Schafer and George Schafer, heard their side of the story, and reviewed various documents shown to him by the Schafers. He apparently concluded that there were important issues involved and that Schafer Bros. Ltd. probably had a legitimate complaint. He was also upset by what appeared to him to be the inability of Schafer Bros. Ltd. to secure, through

three successive Ministers of Agriculture (Messrs. Greene, Olson, and Whelan), a fair and independent assessment of its complaints. It seemed to him that the Ministers of Agriculture relied to too great an extent on the senior officials of the Canadian Dairy Commission itself to make their assessments of the facts.

Michel Choquette then made a substantial personal commitment to the complicated and arduous work he felt was necessary to obtain a satisfactory hearing of the entire matter. He set about to preparing comprehensive and detailed chronological accounts of the facts as he understood them from the Schafers and reviewed such documents as the Schafers possessed. He also made certain inquiries in Mexico and of the Canadian Dairy Commission, and had conversations with Gilles Choquette when the latter was Executive Assistant to the Minister of Agriculture and, later, Chairman of the Canadian Dairy Commission. It turned out to be his principal occupation for four years, all of which work he performed voluntarily without remuneration and on a disbursements-only basis. He produced a much more coherent account of the facts than the Schafers could have done by themselves. It appears that without his efforts this Commission of Inquiry would not have been established.

Michel Choquette was also present at many of the public hearings of the Commission of Inquiry, testified himself before the Commission of Inquiry, and was present during the interviews held in Mexico City in October, 1980.

The voluminous documentation prepared and assembled by Michel Choquette between 1974 and 1977 was the raw material on which the *Statement of Allegations*, which formed the basic subject matter of the Inquiry, was based. That documentation, all of which was marked as Exhibits 6 and 6A in this Inquiry, is listed in Appendix 10 to this Report. Michel Choquette's evidence statement, which in essence sets out the nature and evolution of the documentation, is reproduced as Appendix 16 to this Report.

For most purposes the key document prepared by Michel Choquette is a 182-page letter or report dated July 25, 1977, which he wrote to Gilles Choquette, "definitively stating Schafer Bros.' case", as he put it in his evidence. In evidence he stated that "it is all in here anything that is relevant". This long letter had, as Appendix I to it, a 120-page "condensed version" of a longer 323-page chronological account of the facts he had prepared, as well as copies of what he considered to be the key documents which were attached as Appendices 2 to 78. He subsequently prepared a memorandum dated August 15, 1977 by way of an addendum to the document dated July 25, 1977.

Copies of all these documents were submitted to various government officials.

It is worth noting that in the preparation of all this documentation, and apart from a minor first-hand involvement in the Philippines incident, Michel Choquette only really had access to the Schafers' side of the matter. He did not contact other private Canadian exporters. The Canadian Dairy Commission did not appear to be cooperative in answering questions he submitted to it seeking information. Perhaps this is understandable, but it did lead to a situation where he became an advocate for the Schafer understanding and interpretation of the facts, based largely on circumstantial evidence and on the suspicions of the Schafers. It also led to his raising questions in a manner certain to cause anguish (and hostility) on the part of the Canadian Dairy Commission officials and others. For example, at page 6 of his memorandum of August 15, 1977, referred to above, he stated:

"What we are dealing with is not a question of agency, but of unfair competition, unjust enrichment, inducement, quasi contract, misuse of delegated administrative power, etc. We may also be dealing with fraud, discrimination and the transferring of business to favoured individuals."

(As was the case with David Schafer and George Schafer, the testimony and documents given and filed before this Commission of Inquiry must certainly have added to the prior knowledge and understanding Michel Choquette had of the subject matter of the Inquiry.)

#### 4. *Canadian Dairy Commission*

All past and present officials of the Canadian Dairy Commission who appeared at any time to have had any contact with or possible responsibility for any of the facts alleged by Schafer Bros. Ltd., excepting Mr. D.B. Goodwillie who is deceased, were called to testify by either counsel for the Canadian Dairy Commission or counsel to the Commission of Inquiry, and were made available for cross-examination. These persons included: Dr. S.C. Barry (Chairman, 1966-1973); Mr. E.J. Powers (Chairman, 1973-1976); Mr. Gilles Choquette (Chairman, 1976 to present); Mr. H.M. Johnson (Member, 1973-1979); Mr. E.G. Hodgins (Member, 1977 to present); and Mr. J. Thibaudeau (Member, 1967-1976).

Other marketing and policy personnel of the Canadian Dairy Commission who testified were Mr. Richard Tudor Price, Mr. L.J. Marcellus, Mr. J.R. Sherk and Mr. Raymond Cloutier. They testified not only regarding the operations of the Canadian Dairy Commission, but also with respect to the particular allegations and issues which were the subject matter of this Inquiry.

Commission counsel, on various occasions, requested and obtained from the Canadian Dairy Commission documents which were relevant to the Inquiry.

#### 5. *Private Canadian Traders*

During the course of the Inquiry certain Canadian private traders gave evidence and expressed their views regarding the operations of the Canadian Dairy Commission, of skim milk powder markets and of the export trade business. The testimony of these traders was particularly valuable to me in view of their extensive experience as traders of dairy products including skim milk powder.

Mr. Timothy A. Chisholm and Mr. Walter I. Pelley, both of Ronald A. Chisholm Ltd., appeared as witnesses. Mr. Chisholm is the President of Ronald A. Chisholm Ltd. and has been employed by the company since 1957, while Mr. Pelley is its Vice-President and has also been in its employ since 1957.

Ronald A. Chisholm was founded in 1938 and is an international commodity merchant trading in food and industrial commodities domestically and internationally. On average, Ronald A. Chisholm Ltd. currently trades 3 million (and up to 4 million) pounds of agricultural products daily, and was involved in large sales of skim milk powder to CONASUPO in 1969-1970, after it had made a sale of skim milk powder to CONASUPO in 1968.

Ronald A. Chisholm Ltd. had a special interest in the Inquiry as a result of allegations by Schafer Bros. Ltd. that it had engaged in "irregular behaviour" in connection with its sales to CONASUPO in 1969 and 1970.

Mr. D. Curtis Bishop and Mr. Ronald B. Bishop also gave evidence before this Inquiry. Both are officers, directors and shareholders of Eastern Townships Produce Ltd. (hereinafter referred to as ETP), which was founded in 1941. They stated in their joint evidence statement:

"That ETP by December 31, 1945, was already engaged in the export and domestic distribution of milk powder.

"That from 1949 to the present, the export and domestic distribution of manufactured milk products (principally skim milk powder) has been the major area of business activity of ETP.

"That an officer of ETP has at one time or another personally visited almost every country in the world which has imported Canadian milk powder. The only business purpose of these visits was to sell manufactured milk products.

"Dean R. Bishop, our father and President of ETP, first visited Mexico in 1952. By about 1953 we were making sales and shipping Canadian Milk Powder to Mexico.

"Dean R. Bishop first visited Cuba in 1954. No sales of milk powder were concluded at that time. Between 1954 and 1961, ETP purchased surplus Cuban milk powder which was shipped to Venezuela and Canada.

"Dean R. Bishop first visited the Philippines in about 1965. ETP had already sold to this market prior to his visit.

"Subsequent visits were made to Mexico and the Philippines on several occasions and to Cuba on at least 2 occasions.

"ETP has made sales of Canadian manufactured milk products to: Argentina, Aruba, Bahamas, Belgium, Brazil, British Honduras, Canal Zone, Chile, Colombia, Cuba, Curacao, Denmark, Dominican Republic, Greece, Grenada, Guatemala, British Guiana, Holland, Honduras, Hong Kong, India, Iran, Iraq, Israel, Italy, Jamaica, Japan, Korea, Lebanon, Madagascar, Malaysia, Mexico, Nicaragua, Nigeria, Pakistan, Panama, Peru, Philippines, Rhodesia, St. Lucia, St. Vincent, El Salvador, Singapore, Spain, Sweden, Taiwan, Thailand, Trinidad, Union of South Africa, U.S.A., Venezuela.

"In several of the above countries, ETP was (and is) represented by an appointed agent. "In Mexico, from 1961 to the present, ETP's agent has been Walter E. McAllister, Rio Lerma 339-2, Mexico 5, D.F. As ETP agent, Mr. McAllister maintained regular contact with private businesses, CEIMSA, and subsequently CONASUPO.

"Between 1961 and 1966 Dean R. Bishop personally visited CONASUPO in Mexico and met with Hector Rodriguez Licea, the purchasing manager of CONASUPO. Mr. McAllister and his wife were also present at this meeting. Dean R. Bishop has also met personally with Hank Gonzalez, former General Manager of CONASUPO.

"ETP has always maintained a close liaison with officials of the Agricultural Stabilization Board and Canadian Dairy Commission, providing them on a regular basis with information pertaining to any world market.

"In August 1968 ETP contracted with the Canadian Dairy Commission to purchase approximately 35,000 metric tons of Canada First Grade Spray Process Skim Milk Powder, 1967/1968 production...

"In 1970, ETP sold Canadian skim milk powder to CONASUPO."

Mr. Philippe Pariseault, Director of the milk industry division of La Coopérative Fédérée du Québec, gave evidence and stated that:

"From 1941 to 1955, I was employed by Laurentide Dairy Products Corp., first as a technical director and subsequently as its director and general manager;

"From 1955 to 1976, I worked as general director of Cooperative Agricole de Granby;

"From 1966 until now, I have also acted as director of the Dairy division of La Coopérative Fédérée du Québec;

"During that period, namely from 1968 to 1978, I was also the President and General Manager of Québec-Lait;

"More than 8,000 farmers are members of La Coopérative Agricole de Granby and we are producing more than 40% of all the milk of the province of Quebec;

"The Coopérative Agricole de Granby, by 1940, was already engaged in the processing and in the export and domestic distribution of manufactured milk products including skim milk powder;

"From 1950 to the present, the processing, the export and domestic distribution of manufactured milk products including skim milk powder, have been the major area of business activity of our society;

"In fact, from 1955 to 1960, I visited Mexico and most of the importing foreign countries, in order to sell manufactured milk products, principally skim milk powder;

"After 1960, Mr. F. Brunet, our director of export-marketing, visited Mexico regularly to maintain regular contact with our agents, private businesses, CEIMSA and subsequently CONASUPO;

"Before the Cuban revolution in 1959, we visited Cuba in order to sell them skim milk powder;

"We also visited this country after 1959 and we have made sales of skim milk powder to them;

"Our Coop has made sales of Canadian manufactured milk products including skim milk powder to about 40 countries of which Mexico [sic];

"From 1950 to 1953, our agent in Mexico was Rafmex S.A., from 1954 to 1967 our

agent was Wygard Alex, A.A.B. Centro, and from 1967 to the present, our agent was and still is Sr. Alberto Benelol, Lopez 82-18, Mexico, D.F.;

"Our agents had our instructions to maintain regular contacts with the proper authorities;...

"From 1950 to 1953, we sold regularly skim milk powder to Mexico; in fact we were controlling at the time 70% of the private Mexican market;

"From 1953 to 1971, we sold skim milk powder to Mexico and more particularly we sold 3 million pounds — of skim milk powder in 1965 to CONASUPO."

Mr. Samuel G.K. Ault, former President of Ault Foods (1975) Ltd. which had a special interest in the Inquiry by virtue of two of the allegations, also gave evidence and stated:

"The Ault Company has been in existence in Dundas County in the Province of Ontario producing dairy products of all kinds since 1891.

"The company was initially incorporated as Ault Creamery Ltd. As our operation diversified, new companies were incorporated such as Ault Milk Products Ltd. and Ault Cheese Company Ltd. In 1975, Ault Foods (1975) Ltd. was incorporated federally and the majority of dealings take place under the name of Ault Foods Ltd. presently. "In 1939, I entered the employment of the Ault Company, and between 1946 and 1960 held the position of General Manager. In 1960, my brother, Ken Ault, retired as President and I was President from 1960 until 1978 and am currently Chairman and Chief Executive Officer.

"Until 1950, the Ault Company was a family business. At that time, my brother Ralph, sold his shares to Ogilvy Flour Mills, a publicly traded company. In 1968 John Labatt Ltd. purchased the controlling shares of Ogilvy Flour Mills and consequently acquired Ault Creamery Ltd. and Ault Milk Products Ltd.

"In November of 1975, Ault Foods (1975) Ltd. purchased the assets of Cow and Gate (Canada) Ltd., a subsidiary of the British Company, Unigate Ltd...

"In 1973 the Ault Company developed a powdered baby formula to meet the requirements of the Mexican Government and this is now sold to Compania Nacional de Subs-

tencias Populares (CONASUPO). Through development of the infant baby formula, Ault Foods Ltd., became very familiar with the technical requirements of the Mexican market. Mexican technicians would be sent to our plants and laboratories in Montreal and Winchester.

"As well, Ault Foods Ltd. developed a bar composed of dairy based powder which is used for school lunches in Mexico, specialty dairy based powders for use in the nutritional food programs in Mexico, and conducted a research project on behalf of Mexico with respect to turning milk powder into lactose and cosein.

"Through our research contracts and marketing of powdered infant formula and other specialty dairy based powders, we had continual communications with officials at CONASUPO. We also had frequent communication with the Canadian Dairy Commission. For example, CONASUPO officials would want to schedule C.D.C. visits at the same time as Ault's."

## 6. *Expert Witnesses*

In order to carry out my mandate adequately and to deal exhaustively with the subject matter of this Inquiry, I retained technical advisers who submitted reports and testified regarding the general aspects of the dairy industry, certain aspects of the operations of the Canadian Dairy Commission, and the policy aspects of this Inquiry. Their contributions to this Inquiry were most useful because of their experience and qualifications. Their evidence assisted me greatly in understanding the factual and policy context of the allegations and issues.

Dr. L.A. Skeoch prepared a statement entitled *An Outline of Some of the Economic Aspects of the Inquiry*, which was marked as Exhibit 11 and which is reproduced as Appendix 12 to this Report. Dr. Skeoch is a Professor Emeritus of Economics at Queen's University. He received his Master of Arts degree in Economics at the University of Toronto and his Ph.D. in Economics at the University of California at Berkeley. Following graduation he lectured in Economics at the University of Manitoba and at the University of Toronto, and was senior Economist for the Canadian Wheat Board during the years 1941 to 1946. He was the Agriculture Rehabilitation Specialist and the acting Chief of the United National Relief and Rehabilitation Mission to the Ukraine in 1946 and 1947, and subsequently, until 1957, served as Senior Economist in the Combines Branch of the Department of Justice in Ottawa. Dr. Skeoch was the first to be appointed as the Skelton-Clark Visiting Professor, Queen's University, and was a Professor of

Economics at Queen's University from 1957 to 1975. He has served as a consultant on competition policy to UNCTAD and to the Governments of Canada, Sweden and West Germany, and has appeared as an expert witness before various Canadian Parliamentary Committees and before the Antitrust Subcommittee of the United States Senate. He has written widely in the fields of industrial organization and agricultural policy, and is widely acclaimed as an outstanding scholar in those fields.

**Mr. George R. McLaughlin** prepared a statement, with supporting documents, entitled *The Evolution of Organization and Regulation in the Ontario and Canadian Dairy Industries*, which was marked as Exhibit 78 and which is reproduced as Appendix 13 to this Report. Mr. McLaughlin graduated in 1946 with High Honours from the Ontario Agricultural College at the University of Guelph with a Bachelor of Science degree in Agriculture, specializing in animal husbandry. Mr. McLaughlin has spent his lifetime since then as a dairy farmer. He built up a breeding herd of Holstein Friesian cattle in Canada that enjoyed a substantial reputation not only nationally but internationally. In August 1965, Mr. McLaughlin was appointed by the Ontario government as Chairman of the newly-created Ontario Milk Marketing Board. He remained as Chairman until 1976. He was a member of the Consultative Committee of the Canadian Dairy Commission from its inception in 1966 until 1976, and was a member of the Canadian Milk Supply Management Committee from 1971 to 1976. In 1974, Mr. McLaughlin was awarded the H.R. McMillan Laureate in Agriculture, which is awarded every five years to the individual judged to have made the most outstanding contribution to Canadian agriculture during the period. Mr. McLaughlin is highly knowledgeable and thoroughly experienced in every aspect of the dairy industry, and its regulation.

**Mr. P. Pariseault**, who has equally extensive experience in the dairy industry, particularly in the Province of Quebec and at the national level, as was shown above, has been the Chairman of the Consultative Committee of the Canadian Dairy Commission from 1966 to 1977. He submitted a memorandum to me providing detailed explanations regarding aspects of the production and disposal of dairy products in Canada, together with general comments about the Canadian dairy industry and the operation of both fluid milk quotas and industrial milk quotas. The memorandum was marked as Exhibit 146 and is reproduced as Appendix 14 to this Report.

**Dr. G.A. Hiscocks** and **Mr. L. Stephens** jointly prepared a general background paper entitled *Review of the Canadian Dairy Commission, Background, Creation, Policy and Operations*, which was marked as Exhibit 9 and which is reproduced as Appendix 15 to this Report.

Dr. Hiscocks obtained his doctoral degree in Agricultural Economics from the University of Illinois. Since 1965 he has studied many sectors of agriculture in Canada, of which the dairy sector is a major sector. He has written several articles, a number of which relate to the marketing of agricultural products and to marketing boards of one kind or another involving the dairy industry.

Mr. Stephens graduated from the Ontario Agricultural College at the University of Guelph in 1936. He was employed by Canada Packers Limited from 1936 until 1960. He was then employed for two years by the Pet Milk Company of St. Louis, serving in Canada as manager of the cheese division of the Cherry Hill Cheese House. From 1962 until his retirement in 1979, Mr. Stephens was employed by Gay Lea Foods of Weston, Ontario, in various capacities, starting as production manager and ending up as Vice-President and Assistant General Manager. He has been interested in industry affairs from the processing side of the industry and has served both as a director and as president of the Ontario Dairy Council. He also served for a time as a Director of the National Dairy Council, the national association of dairy processors in Canada.

## **7. Mexican Witnesses**

Prior to the establishment of this Commission of Inquiry, when Schafer Bros. Ltd. submitted its allegations to Government officials, it relied heavily upon written statements supplied to it in 1975 by three Mexican nationals, namely, Mr. Guiseppe Rocchi, sometime General Manager of Sociedad General Mexicana de Control S.A.; Mr. Baltazar Rodriguez Ayala, former Assistant Purchasing Manager at CONASUPO, and Mr. Alejandro Carillo, a Mexican Senator.

At the beginning of this Inquiry the same three persons, as well as Mr. Hector Rodriguez Licea who was the Purchasing Manager of CONASUPO until 1970, submitted and filed evidence statements.

During the Inquiry, written interrogatories suggested by various counsel were sent to the above Mexican nationals and to CONASUPO. They were answered by Messrs. Rodriguez Ayala and Rocchi in writing.

In order to confirm or further my understanding regarding certain general matters pertaining to the subject matter of the Inquiry, invitations were sent to certain Mexican nationals to meet with me in Mexico City on October 16 and 17, 1980. Counsel for all interested parties were invited to attend and in fact, many of them including Mr. Michel Choquette attended the meetings and participated in the discussions with the Mexican witnesses.

Eight Mexican nationals were interviewed at that time, including past and present officials of CONASUPO (Mr. Enrique Rios Velazquez, Mr. Baltazar Rodriguez Ayala and Mr. Eduardo de la Torre), persons from the private sector who act as agents in Mexico for foreign suppliers (Mr. Ben Nordermann, Mr. Jose Luis Uriarte, Mr. Alberto J. Benolol and Mr. Guiseppe Rocchi), and Mr. Fidenzio

Arguelles, who has served in the Commercial Section of the Canadian Embassy in Mexico for many years with responsibility for agriculture.

The interviews so conducted in Mexico were of very considerable assistance to me, as is evident elsewhere in this Report, and the cooperation of those interviewed was much appreciated.



## CHAPTER III

### THE FACTUAL SETTING

#### (A) THE CANADIAN DAIRY COMMISSION

##### 1. *Brief Historical Background*

Particularly after World War II the production of milk grew more rapidly than did demand, both domestically and internationally. This led to extreme downward pressures on producer incomes which added to the usual difficulties created by fluctuations in production costs and the weather, and by seasonal production peaks.

By the early 1960's the Federal Government's price support program for butter, given continually rising productivity and the growing popularity of margarine, had resulted in huge government surpluses of butter in Canada.

Although the production and marketing of fluid milk within the provinces had been the subject of regulation for many years, there was little coordination of policy between the provinces and between federal and provincial programs. Two prior experiences with a federal regulatory authority in the dairy industry, namely the ill-fated Natural Products Marketing Act, 1934, which had been declared unconstitutional by the courts, and the Wartime Prices and Trade Board, had not led to a permanent authority.

Various producer organizations cooperated to convene the Canadian Dairy Conference in February 1963 in order to deal with their concerns and to discuss their interests in achieving increased stabilization and policy coordination. Representatives of the principal dairy organizations, and of the Federal and Provincial Governments, attended the Conference on invitation. It was from this Conference that the pressure and organization developed to establish a national agency for the dairy industry.

The bill to establish the Canadian Dairy Commission was introduced and given First Reading in Parliament on June 16, 1966. It received Third Reading one week later and Royal Assent on July 11, 1966. The Act came into force October 31, 1966, and the Canadian Dairy Commission was fully operative by the time the new dairy year began on April 1, 1967.

##### 2. *The Commission*

The Canadian Dairy Commission is a statutory corporation established by Section 3 of the *Canadian Dairy Commission Act*. It consists of three members

appointed by the Governor in Council, one of whom is designated as the Chairman (and Chief Executive Officer) and one as Vice-Chairman. The three members hold office during pleasure of the Governor in Council.

The Commission employs approximately 60 persons, all of whom work at the Head Office which, by statute, is required to be in Ottawa.

By virtue of Section 4 of the Act, the Commission is constituted an agent of Her Majesty and may act only in that capacity. It may enter into contracts, and property acquired by it may vest, in the name of Her Majesty or in the name of the Canadian Dairy Commission.

By Section 4(4) of the Act, legal proceedings in respect of any right or obligation acquired or incurred by the Commission on behalf of Her Majesty may be brought or taken by or against the Commission in the name of the Commission in any court that would have jurisdiction if the Commission were not an agent of Her Majesty.

##### 3. *Outline of Powers*

Section 8 of the Act sets out the objects of the Canadian Dairy Commission:

"8. The objects of the Commission are to provide efficient producers of milk and cream with the opportunity of obtaining a fair return for their labour and investment and to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality."

"Dairy product" is defined by Section 2 to mean "milk, cream, butter, cheese, condensed milk, evaporated milk, milk powder, dry milk, ice-cream, malted milk, sherbet, or any other product manufactured wholly or mainly from milk."

Section 9(1) of the Act sets out the principal powers of the Commission. It is difficult to summarize and is now reproduced in full:

"9(1). Subject to and in accordance with any regulations made (a) under this Act, the Commission may

(a) purchase any dairy product and package, process, store, ship, insure, import, export, or sell or otherwise dispose of any dairy product purchased by it;

(b) make payments for the benefit of producers of milk and cream for the purpose of stabilizing the price of those products, which payments may be made on the basis of volume, quality or on such other basis as the Commission deems appropriate;

- (c) make investigations into any matter relating to the production, processing or marketing of any dairy product, including the cost of producing, processing or marketing that product;
- (d) undertake and assist in the promotion of the use of dairy products, the improvement of the quality and variety thereof and the publication of information in relation thereto; and
- (e) do all such acts and things as are necessary or incidental to the exercise of any of its powers or the carrying out of any of its functions under this Act."

The word "marketing", which appears in Section 9(1)(c), above, also appears in certain other sections of the Act that will be referred to. Section 2 defines "market" as meaning "to market in interprovincial or export trade".

No regulations relevant to the subject matter of this Inquiry have been made under the Canadian Dairy Commission Act, but the scope of the regulation-making power may be relevant to the construction of Section 9(1) and to an assessment of the powers that can be exercised by the Canadian Dairy Commission in the absence of regulation. The principal regulation-making power is set out in Section 12(1) of the Act:

"12(1). The Governor in Council may make regulations regulating the marketing of any dairy product, including regulations

- (a) providing for the marketing of any dairy product on a quota basis;
- (b) designating the agencies through which any regulated product shall be marketed;
- (c) providing for the issue of licences to persons engaged in the production or processing of a regulated product for market, prescribing the fees therefor and providing for cancellation or suspension of licences;
- (d) prohibiting persons from engaging in the marketing of any dairy product, or any class, variety or grade thereof, in whole or in part except under the authority of a licence;
- (e) prescribing the books and records to be kept by persons engaged in the production or processing of a regulated product for market and the information to be furnished by such persons;
- (f) authorizing the Commission to fix, impose and collect levies or charges from

persons engaged in the marketing of any dairy product or the production or processing of a regulated product for market and for such purposes to classify such persons into groups, fix the levies or charges payable by the members of the different groups and to use such levies or charges for the purpose of carrying out its functions under this Act;

- (g) providing for the seizure and disposal of any regulated product marketed in contravention of any regulation made under this section; and
- (h) generally, for carrying out the purposes and provisions of this Act."

Two further statutory provisions should be noted, although they appear not in fact to have been used:

"9(3). The Commission may make such rules as it deems necessary for the regulation of its proceedings, for the fixing of a quorum for any of its meetings and generally for the conduct of its activities under this Act."

"11. In exercising its powers under this Act or the regulations in relation to the importation or exportation of any dairy product, the Commission shall comply with any directions from time to time given to it by the Governor in Council or the Minister."

#### 4. *Funding*

The Canadian Dairy Commission administers very substantial public funds. It has an annual budget of approximately \$300 million. Deducting the export levies recovered from producers, from the amount paid in the form of direct producer subsidies, it appears that over half of the budget is paid as direct subsidies to producers in connection with milk and cream that is used for industrial purposes, and approximately one third of the budget is devoted to covering the cost of export sales of surplus products.

Virtually all the funding for these activities derives from Parliamentary appropriations for the work of the Canadian Dairy Commission, paid to the Commission through the Agricultural Stabilization Board for the purpose of stabilizing the price of milk and cream.

Flexibility in funding is achieved when necessary by loans to the Commission out of the Consolidated Revenue Fund on approval by the Governor in Council. Section 16(2) of the Act provides that the outstanding loans at any time shall not exceed \$100 million.

## 5. Consultative Committee

There are, of course, certain general mechanisms whereby Parliament and the Minister of Agriculture can require the Canadian Dairy Commission to answer for or to explain its policies and their administration. In addition to the members of the Commission holding office during pleasure of the Governor in Council, the Commission is required to report formally every year to the Minister, which Report must be laid before Parliament. Also, Parliament votes the appropriations for the work of the Canadian Dairy Commission, and each year the Commission is required (Section 10(1)) to submit to the Minister an outline of the program by which it proposes to carry out its functions under the Act for the forthcoming year.

There is, however, a further mechanism provided for in the Act that appears to have been intended to assist the Commission in matters pertaining to the formulation of policy relating to production of dairy products and their marketing in interprovincial or export trade. This mechanism is the Consultative Committee, and since one of the allegations made by Schafer Bros. Ltd. (Allegation B.8, in part) concerns the Consultative Committee, a brief account of its general nature and operations will be helpful.

Sections 5 and 6 of the *Canadian Dairy Commission Act* provide for the Consultative Committee as follows:

"5.(1) The Minister shall appoint a Consultative Committee consisting of a chairman and eight other members.

(2) Each of the members of the Consultative Committee shall be appointed for a term not exceeding three years, except that of those members first appointed three shall be appointed for a term of two years, three shall be appointed for a term of three years and three shall be appointed for a term of four years.

"6.(1) The Consultative Committee shall meet at such times as are fixed by the Commission and shall advise the Commission on such matters relating to the production and marketing of dairy products as are referred to it by the Commission.

(2) The members of the Consultative Committee may be paid for their services such remuneration and expenses as are fixed by the Governor in Council."

Several witnesses testified regarding the membership and nature of the Consultative Committee during the years which were examined by this Commission of Inquiry, which also happened to be the first ten years

of the existence of the Canadian Dairy Commission. Throughout the tenure as Chairman of Dr. S.C. Barry, and continuing through most of the tenure of Mr. E.J. Powers, the Consultative Committee appears to have served a very useful advisory function to the Canadian Dairy Commission, meeting monthly except for the summer months and acting, in effect, like a board of directors without authority. Ultimately, the influence of the Consultative Committee appears to have derived from the fact that it was composed of knowledgeable and experienced individuals from different parts of the dairy industry. Mr. P. Pariseault was Chairman of the Committee from the inception of the Commission, and the Committee, in 1966 until late 1976 or early 1977. Mr. George R. McLaughlin was also a member throughout this same period. Until 1970, six of the members of the Committee were in essence producers, and three were processors. With the appointment of Mr. Samuel Ault in 1970, five of the members were producers and four were processors.

The statutory provisions relating to the Consultative Committee are sufficiently general that much depends on the particular chairman of the Commission, and the abilities of the individuals on the Consultative Committee, in determining exactly how and to what extent the Committee is used by the Commission.

It appears that increasingly, after the establishment of the Canadian Milk Supply Management Committee in 1970-71, the activity and usefulness of the Consultative Committee with respect to advice on production policies began to diminish, and by 1975 the Committee was being convened only approximately every two months in order to review statistics that were presented to it. This lack of input into policy formation resulted in a growing dissatisfaction among members of the Consultative Committee, with the result that a Special Committee of the Consultative Committee was established in 1976 to consider the proper role of the Consultative Committee. The Report of this Special Committee was marked as Exhibit 109 in this Inquiry. Its first recommendation reads in part as follows:

"(1) Purpose: The purpose should be to review with the C.D.C. industry strategy and problems well in advance of the time of making these decisions. For example: To advise on the development of marketing philosophy and strategy. Particularly in the export field, as well as for domestic products. For instance, the need to clear up a long standing question of whether the C.D.C. should handle all exports and/or imports. At least there should be a clear understanding of what the role will be of the various segments of the industry."

The Special Committee further recommended that four meetings per year should be adequate provided that proper documentation was submitted to the members in advance of the meetings.

As of the the conclusion of the evidence given before this Commission of Inquiry no appointments to the Consultative Committee had been made after 1975. The result of this was that by the end of 1976 the membership of the Committee was being depleted. The last meeting of the Consultative Committee was in February 1977, and despite the depleted membership of the Committee there is some evidence that one of the reasons for these being no further meetings was that at the meeting in February 1977 the members of the Committee disagreed with the Chairman of the Canadian Dairy Commission on certain policy matters, as a result of which he chose not to summon them to further meetings. This may or may not have been one of the reasons. In any event, the Annual Report of the Canadian Dairy Commission to the Minister of Agriculture for the year ended March 31, 1977, states as follows, regarding the Consultative Committee:

"During the past years the Committee was consulted on major policy decisions and members advised the Commission throughout the year on various aspects of the Dairy Program.

Regarding the frequency of meetings, the Committee reviewed its manner of operation with the Commission and it was decided to discontinue the regular monthly meeting in favour of fewer meetings. These will be scheduled prior to important decisions being taken to maximize the effectiveness of the contributions of the Consultative Committee to the Commission's operations."

As stated above, the Chairman of the Commission did not summon any further meetings of the Committee after February 1977.

All appointments to the Consultative Committee had expired by the end of 1978.\*

# Reportedly, in November 1980, the Minister of Agriculture announced nine new appointments to the Consultative Committee.

## **(B) THE GENERAL SYSTEM**

### **1. *The Regulatory Structure\****

\* In this section I have relied to a considerable extent upon the evidence given by Mr. McLaughlin and Mr. Pariseault. In addition to the background papers and the evidence of this Inquiry, see generally D.P. Stonehouse, "Government Policies for the Canadian Dairy Industry", (1979) 14 Canadian Farm Economics 1-11 (Agriculture Canada).

The Canadian dairy industry is an important sector of Canadian agriculture. The production of milk and cream as a source of Canadian farm cash receipts is exceeded only by the production of beef and grain. Consumer expenditures in Canada for milk and dairy products account for about one dollar out of every six that Canadians spend for food. The production and processing sectors of the dairy industry taken together account for approximately one per cent of Canada's gross national product. Canada is largely self-sufficient with respect to dairy products.

There are also other important social realities about the Canadian dairy industry. Approximately three-quarters of Canadian milk production occurs in Quebec and Ontario, with Quebec being the larger of the two. This means that in those two provinces, and particularly in Quebec, dairying and dairy farmers tend to be more important factors for policy making than they tend to be in other provinces.

Although consumer demand for milk and dairy products is probably the portion of consumer food needs that is least likely to decrease as a result of price increases, per capita demand in Canada for dairy products other than fluid milk decreased significantly in the 1970's. This decline was probably, at least in part, attributable to substantial increases in the prices of such products in Canada, which increases exceeded increases in the consumer price index and were also, at least since 1974, more than double comparable increases in the United States.

Total milk production in Canada also decreased slowly but steadily throughout the 1970's.

Production and price levels of dairy products in Canada are significantly influenced, and to an extent determined, by Government policies and regulations pertaining to the dairy industry.

The different uses for milk, together with requirements of Canadian constitutional law, have led to the existence of two sectors in the Canadian dairy industry, namely, fluid milk and industrial milk. Fluid milk has been loosely described as the milk we drink, and industrial milk as the milk we eat.

Fluid milk is consumed in fresh fluid form, is relatively perishable and is costly to transport due to its bulk. Fluid milk commands a higher price for producers than does industrial milk because of a greater need to maintain rigorous sanitation standards in production and to assure daily supply.

Industrial milk, sometimes called "manufacturing milk", refers to milk and cream that is processed or used to manufacture a wide variety of dairy products including cheese, butter, milk powder, condensed milk and evaporated milk. These products are not as perishable as fluid milk, are relatively easily transported, and are not required on a fresh daily basis.

Skim milk powder is a by-product of the manufacture of butter. A hundred pounds of "standard" raw milk, namely, milk with a 3.5% butterfat content, yields approximately 4.2 pounds of butter and 8.0 pounds of skim milk powder.

In the past, the market for industrial milk was mainly supplied by farmers whose output was destined solely for that market, and the market for fluid milk was filled by other dairy farmers. Today, due largely to similar production standards and coordination in Federal and Provincial Government policies and administration, most dairy farmers fill both fluid and industrial milk quotas. Production standards for industrial milk have risen. Indeed, the same provincial government tank truck typically picks up each farmer's production at his farm and the distribution of that milk is handled by the Provincial marketing bodies.

Essentially, provincial governments have jurisdiction to pass laws relating to the production, marketing and prices of fluid milk, while the Federal Government has jurisdiction to pass laws relating to the production, marketing and prices of industrial milk. Little fluid milk crosses provincial boundaries, whereas most processed dairy products move readily into interprovincial and export markets.

Both levels of government have adopted policies, rules and mechanisms for the control of supplies and the determination of prices, in order to seek to ensure what is determined to be a fair return to producers and adequate supplies for consumers.

### **Fluid Milk**

The marketing of fluid milk is controlled by provincial boards or agencies in every province except Newfoundland.

According to Mr. Pariseault and Mr. McLaughlin, the control and maintenance of supply is accomplished at the provincial level by the allocation of quotas to producers. Individual quotas are allocated within the framework of the total provincial fluid milk requirements, as calculated, and represent for each quota holder his amount or share of the total production of his province or region. The quotas provide for some tolerance in order to take account of unforeseen circumstances that may arise. Quotas may be acquired, increased or decreased in accordance with such methods as may be permitted or prescribed by regulation. These normally include purchase from another farmer, purchase from a quota exchange and transfer.

Quotas may be reduced or lost because of a failure to produce to the quota level. In Ontario, according to Mr. McLaughlin, instead of being subject to a variation in individual quota because of individual changes in sales, producers have agreed that the same

individual quota will be retained with a change in the percentage of their milk entitled to the fluid milk price.

Production within his quota guarantees a producer the payment of the price set for fluid milk by the competent provincial authority. As put by Mr. McLaughlin:

"It is in fact a contract which requires him to supply a certain daily volume of milk, usually with some tolerance allowed for unseen circumstances, and which guarantees him a certain level of payment for the quota milk, based upon compositional and hygienic quality."

Production which exceeds the fluid milk quota will be diverted to manufacturing use paid for on the basis of current world prices for butter and skim milk powder. The producer can protect himself from this effect of over-quota fluid milk production by acquiring a quota for industrial milk to cover the excess volume, and he will then receive such benefits as are enjoyed by industrial milk quota holders for his surplus. In the words of Mr. Pariseault:

"The surpluses of milk produced under fluid milk quotas, but not required by the fluid milk market, have to be produced under the market sharing quota (MSQ) released by the Canadian Dairy Commission (CDC). This "surplus milk" will then cause no harm to the supply management of industrial milk and will be eligible to the CDC subsidy on industrial milk..."

Any farmer who produces altogether outside of quota can only expect to receive the world market price, through the central provincial buyers, for his milk shipments. This is a price at which, Mr. McLaughlin said, "he could not survive under Canadian cost conditions". In fact, over-quota production is effectively discouraged by the absence of the subsidy and by special penalty levies. Accordingly, levels of output are controlled.

Mr. McLaughlin stated that the price to be paid to producers for their fluid milk is fixed by some compulsory process, depending upon the province:

"Such prices are generally established through negotiation and, if necessary, by arbitration. In some provinces prices to farmers are established by government regulation after public hearings. In Ontario, prices are established by regulation of the producer marketing board, and are then subject to appeal to a government tribunal. Some provinces also regulate prices which processors and retailers may charge consumers."

Formulae are generally used to guide the setting of the levels of prices to dairy farmers. The formulae seek to take into account production costs (labour, invested capital and equipment, and feed) and market conditions.

The procedure for payment varies from province to province. In Ontario, the farmer sells his milk directly to a Provincial board, which pays him after making deductions for costs of administration, promotion, advertising and transport. As stated by Mr. McLaughlin:

"Once in production, he will sell his milk to his marketing board, the OMMB, to market it for him. In fact the OMMB buys the milk from him at his farm, and sells it to the processors. It contracts with milk transporters as agents to pick up the milk at the farm and deliver it to a designated processing plant. The farmer may not know the plant destination of his milk, and he may not care for he is paid the same wherever it goes. The processor pays the OMMB on the basis of the end use of the milk. Prices vary from fluid milk use (the highest priced category, called Class 1) to that used for the manufacturing of butter and skim milk powder (called Class 5). The returns from Classes 1 and 2, which are fluid uses, are pooled and the pooled or average price is paid to each producer in relation to his fluid quota, modified by factors for hygienic and compositional quality, less OMMB costs for administration of the Board and for promotion and advertising, and less a pooled transportation charge. Classes 3 to 5 are industrial use categories, and returns from the sale of milk used in these categories are pooled, and this pooled price is paid to each producer in relation to his MSQ, modified by factors for hygienic and compositional quality, less OMMB costs, and less a pooled transportation charge."

In Quebec, according to Mr. Pariseault, the fluid milk is delivered directly to dairies, who pay the Federation of Fluid Milk Producers, which in turn pays the producers a predetermined price less the costs for advertising and so on.

As stated, in the case of the typical dairy farmer who has both fluid and industrial milk quotas, shipments in excess of his fluid quota are allocated to his industrial quota.

### **Industrial Milk**

The Canadian Dairy Commission is the key agency in the administration, and in many respects the formulation, of the Federal Government's dairy policy.

The Canadian Dairy Commission administers a number of programs that are, together, intended to stabilize producers' returns at a satisfactory level. The two principal policies adopted to this end are the price support programs and payment of a direct subsidy to producers of industrial milk and cream. By these policy instruments, both of which were instituted by the Agricultural Stabilization Board and carried on by the Canadian Dairy Commission, the Commission seeks to help producers achieve a "target support price" or "target return".

The two main price support programs for this purpose are those for butter and skim milk powder. Under these programs the Canadian Dairy Commission offers to purchase all butter and skim milk powder produced (by processors) in Canada, and that meets prescribed specifications, at a stated price per pound. The support prices give a calculable value to standard milk (3.5% butterfat content) and thus convert to a market price guarantee for the milk. By then deducting an "assumed processors' margin" to cover costs of and profit for the processor, an estimated market return to the producer for the sale of his industrial milk is arrived at, calculated on a hundred-weight basis. The support prices are designed to enable processors to pay this basic market price for industrial milk.

To this market return for the producer's milk is added the subsidy paid directly by the Canadian Dairy Commission, from public funds, to the producer for his industrial milk shipments. This subsidy is also calculated at so much per hundredweight of standard milk, sometimes also expressed in terms of so much per pound of butterfat. For example, the current direct producer subsidy of \$2.66/cwt is 76 cents per pound of butterfat. (Since the metric system was put into effect the calculations are now done in terms of hectolitres, but the principles and steps are the same. To avoid confusion for purposes of comparison, the pre-metric calculations are still in common use.)

These two income sources, namely, the market return through the support price (paid ultimately by consumers), and the subsidy (paid ultimately by taxpayers), make up the target support price per hundredweight of milk to the producer. From this amount the producer must pay an export levy, discussed below in this Chapter.

The Canadian Dairy Commission had to fix individual quotas for industrial milk, initially called "subsidy eligibility quotas", in order to limit the amount of its subsidy payments. This initial system of quotas was replaced, beginning in 1971, pursuant to an exercise in federal-provincial cooperation apparently inspired by the Dairy Farmers of Canada. This was the Interim Comprehensive Milk Marketing

Plan, administered by a federal-provincial body called the Canadian Milk Supply Management Committee.

The Interim Comprehensive Milk Marketing Plan resulted in part from a growing degree of interdependence between the fluid milk and industrial milk sectors. Similarities in production between the two have been referred to above. In addition, restrictions on producer entry into or expansion in one sector, by means of changes in quota limitations or subsidy eligibility rules, can affect the quantity of production and the prices in the other sector. A shift in consumer demand to 2% fluid milk, and from butter to margarine, affects the butterfat surpluses that have to be coped with.

All provinces except Newfoundland, which has no dairy industry to speak of, signed the Interim Comprehensive Milk Marketing Plan (see Appendix 13, Schedule 19, to this Report). Quebec and Ontario signed in December 1970, Prince Edward Island in 1971, the three prairie provinces in 1972, British Columbia in 1973, and Nova Scotia and New Brunswick in 1974. In 1974 the Comprehensive Milk Marketing Plan was signed, in effect continuing the Interim plan.

The Canadian Milk Supply Management Committee is made up of two producer representatives and one government board representative from each participating province, plus three representatives from the Canadian Dairy Commission. Representatives of the Dairy Farmers of Canada also attend. One of the Canadian Dairy Commission representatives serves as chairman.

The central feature of the Comprehensive Milk Marketing Plan is the Market Sharing Quota ("MSQ") Program. The way this works is that the Canadian Milk Supply Management Committee makes an estimate each year of Canada's butterfat "requirements" for the forthcoming year, and converts this estimate to a volume of standard milk. It then adds 5% as a so-called "sleeve" to ensure against errors in the estimate, and thus arrives at a global MSQ figure. This global figure is then allocated by the Committee among the provinces. (For example, as of 1979, 48% of the total was allocated to Quebec and 31.3% to Ontario) The further allocation of each province's share among the individual producers in each province is done by the provincial regulatory agency.

It is not intended in this section of the Report to attempt anything other than a general description of what is in some respects rather complicated, but an excerpt from Mr. Pariseault's evidence relating to MSQ transfers may be helpful:

"In Quebec, MSQ are sold and purchased at public auctions. In Ontario, bids and offers

for MSQ are channelled by an exchange quota system working by telex. Elsewhere, MSQ are sold to and bought from the provincial marketing board at a nominal price.

These MSQ removed from the producer are put in reserve. Whenever a producer sells his quotas, the Federation takes 25% of the MSQ for the reserve. This reserve is used either to be distributed equally amongst actual producers or to attenuate an eventual decrease of MSQ decided by the Canadian Management Supply Committee. A producer can lend to another producer a maximum of 20% of this MSQ for a period not exceeding two years, etc."

The Canadian Dairy Commission ties its subsidy and levy programs to the MSQ shares allocated to each individual producer as set out above. The direct producer subsidy, paid monthly by Canadian Dairy Commission cheque to each producer on the basis of his prior month's shipments, is paid only on the 95% of the MSQ that reflects the nation's requirements as estimated. It is not paid on shipments made within the 5% sleeve portion unless and until, at the end of the year, it materializes that some or all of the sleeve portion was required for domestic use, in which event the subsidy is then paid on such portion. Similarly, a "contingency levy" is collected during the year on all MSQ shipments by producers, in order to build up a fund to defray the costs of export disposal in the event that the sleeve production turns out to be surplus to actual Canadian requirements. Contingency levy funds are subject to refund to the extent that sleeve production is used domestically.

The sleeve is something that exists in national terms. If some provinces have a good dairy year and others have problems with herd sickness, pasture quality, or some such thing, it may be that a disproportionate amount of the sleeve production for that year will come from certain provinces. This can have the result, in terms of an individual producer, of his having no sleeve production in a given year and therefore obtaining a full refund of the contingency levy collected from him during the year.

In addition to the contingency levy imposed on all MSQ shipments to help defray the possible costs of disposing of sleeve production on export markets, a separate export levy is assessed on all MSQ shipments to cover the export costs of skim milk powder produced from within-quota milk. Both these levies, together with any penalty levies for over-quota production, are now collected for the Canadian Dairy Commission by provincial authorities by means of deductions from the payments for milk that are received from the processors. In the 1978-79 dairy year the contingency levy was 20¢ per hundred-

weight, the export levy \$1.00 per hundredweight, and the over-quota levy \$7.50 per hundredweight. Before remitting the net market returns, after levy deductions, to each producer, the provincial agency makes a further deduction to defray its own general administrative costs.

Adoption of the supply management MSQ program had a positive effect on producer returns (and a corresponding effect on consumer prices). As to the general effect of restricting supply, the Canadian Dairy Commission Annual Report for 1969 stated:

The stabilization of producer's returns is dependent in considerable measure on the maintenance of a reasonable balance between the supply of dairy products and the effective demand. It is for this reason that a limitation is placed on the total quantity of milk and cream on which subsidy will be paid....

As to the effects of the adoption by Quebec and Ontario of the MSQ Program, the Canadian Dairy Commission stated as follows in its 1971 Annual Report:

The adoption of this program, with its safeguards against excessive production, in the two provinces supplying 80 per cent of Canadian manufacturing milk and cream, made possible the increase in product support prices on February 8, with the resultant increase in prices for manufacturing milk to producers in all provinces.

The next significant development in Federal Government dairy policy, as far as direct impact on prices and returns is concerned, was the long term dairy policy adopted in 1975. A central feature of that policy was implementation of an "Industrial Milk Returns Adjustment Formula", as the basis for adjusting target returns to dairy farmers for their production of industrial milk and cream, referred to earlier in this section of this Report.

The Canadian Dairy Commission regards the Returns Adjustment Formula as its main mechanism for providing efficient producers with the opportunity of obtaining a fair return for their labour and investment. The effects of changing statistical components of the Formula are regularly calculated, and if changes to the target support price of more than a certain small percentage are indicated, the target support price can be adjusted as frequently as every three months.

The Returns Adjustment Formula has three components, weighted as follows:

1. A cost of production index (45%). This index accords weights internally to a variety of cash and capital input costs that are, in effect, the costs of production. The items include feed, breeding fees,

veterinary and similar expenses, machinery and automobile expenses, gasoline and oil, machinery rental, fertilizer, crop expenses, land and building repairs, taxes and insurance, hydro and telephone, and hired labour. Mr. Cloutier stated in evidence that investment costs of herds, buildings and quotas were also taken into account.

2. A family labour earnings index (35%). The consumer price index is applied here to measure changes in earnings.
3. A judgement factor (20%). Mr. Cloutier referred to this as a Ministerial discretion. The 1978 Annual Report of the C.D.C. states that factors considered are significant changes occurring in levels of dairy product stocks, changes occurring in other countries to dairy producer returns, and major changes in competitive processing costs.

Finally, it should be noted that the Federal Government's target support price or target return is just that, a target. Variations in production from quota levels, and surplus disposal problems, result in certain levies that frequently make the actual return less than the target. Further, the actual processor margins are set by provincial authorities and variations as between provinces occur. Mr. Cloutier observed that usually producers in Quebec and Ontario are, in fact, able to achieve higher actual returns than are producers in other provinces.

Further elaboration of the background, context and details of the regulatory structure outlined in this Section of the Report are set out in the background papers prepared for the Commission of Inquiry by Messrs. McLaughlin, Pariseault and Hiscocks and Stephens, which are reproduced as Appendices 13, 14 and 15 respectively to this Report. The article by Stonehouse, referred to at the commencement of this section, also contains a useful and readable summary of the policies.

In illustrating the general description that has been set out in this section of the Report, the following two charts and table of reference data may be helpful.

## **2. *International Trade in Skim Milk Powder***

The major producers and exporters of skim milk powder are the European Economic Community, New Zealand, Australia, the United States and Canada. These countries maintain some form of support programs for their dairy farmers and restrict imports into their own domestic markets.

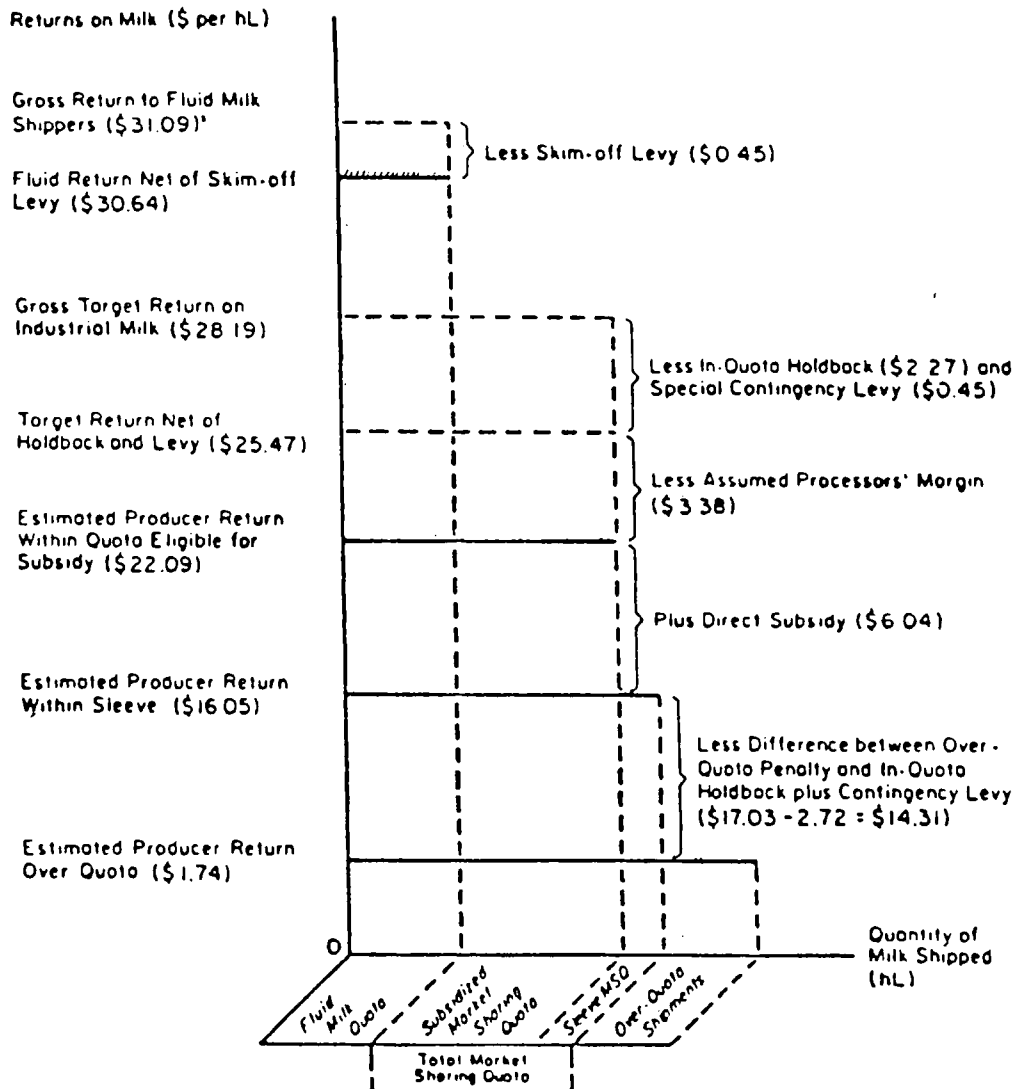
The principal importers of skim milk powder have been Japan, Spain, Indonesia, Thailand, the Philippines, and the larger, more developed countries of Latin America including Mexico and Cuba.

Canada is a small exporter of skim milk powder compared, particularly, to the European Economic



# IMPACT OF DAIRY POLICIES ON MILK PRODUCERS' RETURNS

(April 1, 1978 Values\* Used as an Illustration)

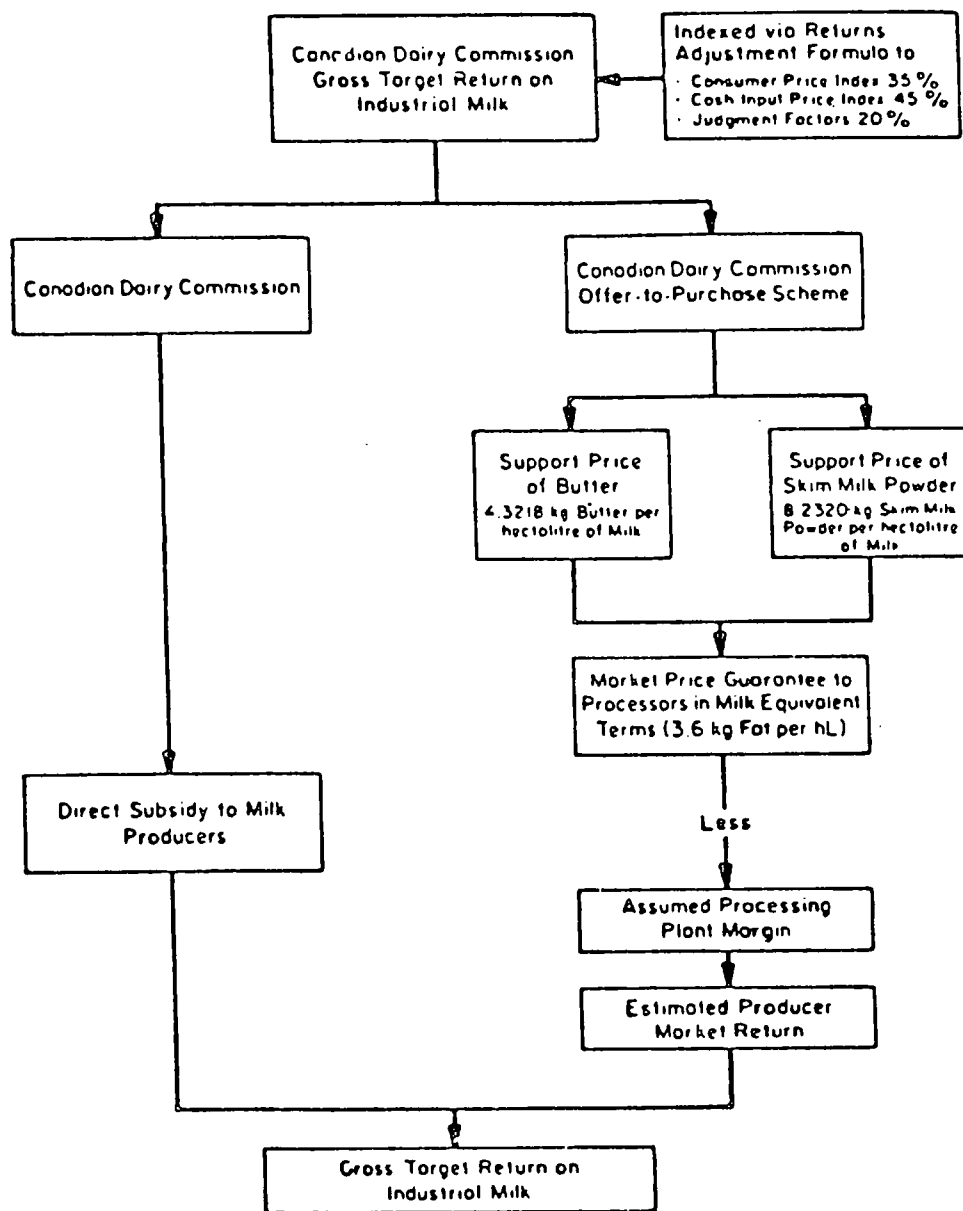


\* Source: Dairy Farmers of Canada, *Cow's For Us and Us For Cows*, 1978, Ottawa, 1978

<sup>a</sup> National average minimum price paid to fluid producers, f.o.b. processing plant - Source: Agriculture Canada, *Dairy Product Market Report*, Vol. 53, No. 11, Ottawa, April 1978

Source: D.P. Stonehouse, "Government Policies for the Canadian Dairy Industry", (1979) 14 *Canadian Farm Economics*, 1 at p. 9

## UNIT RETURNS-SETTING MECHANISM FOR INDUSTRIAL MILK



Source: D.P. Stonehouse, "Government Policies for the Canadian Dairy Industry",  
(1979) 14 *Canadian Farm Economics*, 1 at p. 5

# REFERENCE DATA FOR 1966-1977

Date	Target Support Price (\$/100 Lbs. milk)	Direct Producer Subsidy (\$/100 lbs. milk)	Support Price Skim Milk Powder (\$/lb.)	Export Levy (\$/100 lbs. milk)
1966-67	4.10	0.85	—	0.10
1967-68	4.75	1.21	0.20	0.11
1968-69	4.85	1.31	0.20	0.15
1969-70	4.85	1.25	0.20	0.26
1970-71	4.85	1.25	0.20	0.26
1971-72 (Apr. 71)	5.24	1.25	0.24(Feb/71)	(0.26)
Aug. 16, 71	5.49	1.25	0.26	0.20
Oct. 1, 71	5.49	1.25	0.26	0.10
1972-73	5.69	1.25	0.29	0.10
1973-74	6.55	1.45	0.35	0.30
1973-74 (Aug. 73)	6.70	1.45	0.38	0.10
1974-75 (Apr. 74)	8.50	2.30	0.50	0.15
June. 74	8.76	2.56	0.50	0.15
Aug. 1, 74	9.41	2.56	0.54	0.15
Jan. 24, 75	10.02	2.56	0.59	0.15
1975-76 (Apr. 75)	11.02	2.66	0.64	0.45
July. 75	11.02	2.66	0.64	0.90
Oct. 75	11.02	2.66	0.64	0.65
1976-77 (Apr. 76)	11.45	2.66	0.68	1.35
1977-78 (Apr. 77)	11.86	2.66	0.70	1.20

Source: *Canadian Dairy Commission Annual Report*, 1978.

NOTE: The above data covers only the years which were the subject of this Commission of Inquiry. As of August, 1979, the figures for the above were:

Target Support Price: \$13.67/cwt.  
 direct Producer Subsidy: \$2.66/cwt.  
 Support Price, Skim Milk Powder: 83.5 cents per pound  
 Export Levy: \$1.00/cwt.

Community. Due to transportation costs, however, Canada has certain advantages competing for export sales to Latin America and the Caribbean.

Fresh skim milk powder is used for home consumption (both for reconstituting as fluid milk and in baking), for commercial baking, for making other dairy products such as evaporated milk, condensed milk, yogurt and ice-cream, for food mixes and soups, and the like. Older skim milk powder, sold at a lower price, is used in animal feed to improve the yield from livestock.

International trade in skim milk powder is vitally affected by the quantities of existing surpluses in exporting countries from time to time, by changes in the export assistance granted by these countries to the exporters of those surpluses, by changes of various types in demand patterns, and by the existence of certain trading agreements.

Competition in the international supply of skim milk powder intensified in the 1960's as surpluses resulting in part from domestic agricultural support programs increased.

In 1970, in an attempt to introduce more order into international trade in skim milk powder and to protect established trading relationships, the major exporting countries concluded an International Arrangement on Skim Milk Powder under the General Agreement on Tariffs and Trade. This arrangement set a minimum price for export sales of skim milk powder destined for human consumption and provided for control procedures to ensure that skim milk powder sold for animal feed, which was not subject to the same minimum price provision, was not used for human consumption. The Arrangement was for one year, renewable on a yearly basis, and provided for adjustment of the minimum price from time to time as might be considered desirable. The Arrangement was renewed from year to year throughout the 1970's. The minimum price set in 1970 under the GATT Arrangement was US\$200 per metric ton. International market conditions during the first half of the 1970's, however, were such that the minimum price was increased first to US\$250 and then to US\$350 per metric ton.

International prices for skim milk powder more than doubled during the years 1972 to 1974 from the levels that had obtained in 1970-71. Exports by major producing countries increased by some 30% in 1973 and continued at a high level into 1974. The stocks held by these countries as surplus declined markedly.

Apparently, the major contributing factor to the relatively strong world demand for skim milk powder in these years was the emergence of a world-wide scarcity of animal feeds. For some of this time the United States embargoed the export of soybean products, which put a strong upwards pressure on the

demand for, and the price of, skim milk powder as a substitute animal feed. As well, in 1973/4 the United States substantially increased its own import quota for skim milk powder.

Following a slump in 1974-75, international shipments of skim milk powder have continued to increase, but at a slower pace, with growing markets in Japan, Mexico and certain developing countries. This increase has not solved the problem of surpluses in exporting countries because many importing countries have expanded their own domestic production of skim milk powder, and overall production has continued to increase at a greater rate than demand.

From 1975 to 1977 international prices of skim milk powder moved sharply downward towards the GATT minimum price of US\$350 per metric ton set in the peak year of 1974. This trend reversed, however, in early 1977 and since that time the human food price internationally has increased continuously to 1980 so that by May 1980 it was US\$950 to US\$1000 per metric ton f.o.b. country of origin (see Exhibit 165).

#### Canada

Canadian price support programs affecting skim milk powder were expanded in the latter half of the 1960's at the same time as international competition in the supply of skim milk powder was intensifying, with the result that Canada experienced serious problems at that time in the disposal of its surplus skim milk powder.

Canada, in dealing with its surplus, imposed import restrictions and granted export subsidies. The export subsidy was paid to an exporter on evidence that the powder had been exported. Until 1969, if a private exporter purchased the skim milk powder from the Canadian Dairy Commission, he would first pay the Canadian support price for it and later, after exporting it and furnishing the Canadian Dairy Commission with proof of export, he would be paid the export subsidy by the Canadian Dairy Commission. An exporter who sourced his skim milk powder from the private sector (including processors who might export their own powder) would claim the subsidy in the same way, namely, upon proof of export. In January 1969 the Canadian Dairy Commission instituted the practice of allowing purchases from its stocks at 2 cents per pound above the subsidized price for export sales and later refunding the 2 cents upon receiving satisfactory proof of export. The cost to the exporter of financing the difference between the domestic price of the powder and the subsidized price, until such time as he could furnish proof of export, could have an important affect on the profitability of an export transaction in a competitive environment. It was essential that this financial guarantee of export be reduced to the lowest effective level.

The Canadian Dairy Commission's Annual Reports chronicle the fluctuations that have occurred in the production and disposal of Canada's skim milk powder since 1966. In 1967, as stated above, the Commission accumulated substantial stocks of skim milk powder which were surplus both to Canadian demand and to export sales negotiated for commercially-owned stocks. Production of skim milk powder had, in fact, increased from 120 million pounds in 1957 to 316 million pounds in 1967. Canadian consumption in 1967 was 160 million pounds.

This situation persisted in 1968, as evidenced by the Canadian Dairy Commission Annual Report for 1968-69 which stated as follows:

"There was a substantial increase in supplies of dry skim milk during the year, resulting in a surplus of over 200 million pounds, which was either purchased by the Commission or for which the Commission provided export assistance. This quantity was approximately double that of two years earlier.

...Since world prices during 1968-69 were well below the Canadian support level... the resale value of Commission stocks for export was well below the Commission's cost...

Skim milk production from April 1, 1968 to March 31, 1969, was 365 million pounds, compared to 319 million pounds in 1967-68 and 270 million in 1966-67."

At the same time, seriously depressed prices on the international market reflected heavy world over-supply. During the fall and winter of 1971 the international market price of skim milk powder advanced above the Canadian support level and, by March 31, 1972, the Canadian Dairy Commission was able to report a zero inventory from total stocks for the year of 108.7 million pounds. The average cost of the 108.7 million pounds, according to the Canadian Dairy Commission, had been 24.2 cents per pound, while the average price realized on sale for export was 20.4 cents.

Beginning in 1972, the situation began to deteriorate again as a result of a falling international price and a rising domestic support price in Canada. Mr. Ellard Powers, Chairman of the Canadian Dairy Commission from 1973 to 1976, stated in evidence that:

"Part of the surplus problem in Canada at that time came about because the supply management system... was not restrictive enough in terms of the maximum amount of milk which could be produced under the system. In 1974 or '75 milk production increased sharply. In fact [it] increased

above the levels required for Canadian consumption which gave us an even greater surplus of skim milk powder" (Transcript, p. 4501).

Certain steps were taken to attempt to deal with the serious Canadian surplus problem. Domestic production was cut by reducing the market share quotas. In addition, in 1975 the Canadian Dairy Commission hired an official to be responsible for export marketing, in the person of Mr. Richard Tudor Price. Prior to that time, export marketing had not been the responsibility of a specific official; it would appear that the Canadian Dairy Commission recognized at that time the need to extend its efforts in the face of tough international competition.

In his testimony, Mr. Tudor Price described the situation that faced him when he joined the Canadian Dairy Commission, and the steps he took to improve it. He said:

"By the time that I joined the CDC in September of 1975 a substantial inventory build-up of skim milk powder had occurred in Canada with the CDC and at the same time a large buildup of inventories had occurred in other countries. The situation at the CDC was that in the period between April and September, 1975 the CDC had purchased 201 million pounds of skim milk powder and sold only 20 million... By the 30th of September the CDC stock had reached 269 million pounds and there were very few immediate sales opportunities in sight. Furthermore, the domestic production of skim milk powder was increasing rapidly and I found that although the CDC had budgeted for purchases of 216 million pounds in that fiscal year it had in fact on a moving year basis already purchased in the latest 12 months to the end of that quarter some 250 million and my projection at that point was that they would purchase in the full year some 290 million; in the event it was 328....[under the] open-ended offer to purchase program."

Mr. Tudor Price stated that the difficulty in disposing of the surplus was compounded as a result of high prices in the previous year which had the effect of reducing demand on the world market by virtually cutting it in half, in fact. He continued:

"At the same time a similar situation was arising in other countries that production was rising and demand falling both domestically and for export purposes, so that there was really in all of the major producing countries of skim milk powder a major imbalance developing.

During 1975 we had delays on shipments to Mexico at the Mexicans' request and we had also during the period of shortage in the previous years had our share of the Cuban market reduced very substantially."

He stated further:

"... that there was no short-term solution to this problem and that the problem had to be attacked on a worldwide basis by achieving market expansion in any way in which it was possible...[The CDC, through the Trade Commission Service, approached] the countries where we felt that there could be an opportunity to market skim milk powder, either for regular human uses or for new uses, even including stock-feed uses and to see whether we could first of all expand the market in general and, secondly, whether we could take a larger share of Asian markets which were not traditionally ours... During periods of relatively high prices the use of skim milk powder for animal feed is effectively limited to calf-starter and foal rearing but at a certain point skim milk powder does become competitive with alternative products and a much wider range of stock-feed uses and we immediately started to look at the opportunities for market expansion and also for re-entering the Japanese market which Canada had not supplied for a considerable period of time."

As a result of a relaxation in the provisions of the GATT Arrangement in 1976 pertaining to animal feed, there were dramatic increases in international shipments of skim milk powder for animal feed purposes, and stockpiles began to reduce. However, as Mr. Tudor Price pointed out:

"One of the less welcome consequences of this policy was that we were achieving very low returns. In order to take the world market down to levels where we felt that the market could continue to expand and to allow us to compete with other sources of protein and feed stocks we were making extremely low returns on skim milk powder and this led us to look at alternative strategies which would have a long-term effect of reducing the quantities of skim milk powder that were sold to the CDC and which the CDC would have to export and this led us to look into a series of opportunities such as evaporated milk, such as whole milk powder, the export of products which were mixes of skim milk powder and other products and even such products as ultra high temperature treated milk."

The Canadian Dairy Commission was, however, able to report as follows in its 1978 Annual Report:

"The disposal of excess skim milk powder from Canadian Dairy Commission inventories by export sales for animal feed use was completed during the year; improved export demand for skim milk powder for human food use resulted in the Canadian Dairy Commission closing inventory at March 31, 1978 being only 60.9 million pounds compared with 194.8 million pounds at the same date in 1977 and 282.5 million pounds in 1976. All skim milk powder produced in 1977/78 was sold as human grade powder and all stocks as of March 31, 1978 had been committed. Total export sales of skim milk powder were 381.3 million pounds compared with 326.8 million pounds in the previous dairy year."

A word might be said about the general nature of export sales transactions for skim milk powder. A person wishing to purchase, who may be a government agency in a foreign country, will usually prepare specifications of what he wishes to buy in terms of amounts, future delivery dates, bacteria count, age, heat treatment characteristics and so on depending on the particular nature of his need. He will then invite offers from suppliers, based on those specifications, and may also require what is, in effect, an option on some additional supply. For example, he may request 25,000 tons of skim milk powder with a tolerance of 10% on the quantity, so that according to the way in which his requirements actually materialize he may only take 22,500 tons under the contract or may instead insist upon 27,500 tons at the contract price per pound. The bidders usually bid on a price-per-pound basis with the result that, in view of the contract quantities involved, a difference of a few hundredths of a cent per pound on a tender can amount to quite a significant difference for the total contract price. Bidders must also do their best to line up their supplies, and in a case where, for example, 90-day old powder must be delivered at a date four months in the future, the particular powder would not even be in existence when the contract is entered into.

### 3. *The Export Subsidy*

When the price in a price support program exceeds the international price for a product, in this case skim milk powder, the producer of the powder will not sell on the export market unless he receives a subsidy making up at least the difference between the domestic price and the international price. Likewise, in the event that the producer of the powder elects to sell to the Canadian Dairy Commission under the offer to purchase program at the support price, private exporters will only buy the product from the Canadi-

an Dairy Commission if they receive a sufficient subsidy to permit them to make a satisfactory profit on the export transaction.

Accordingly, it was not realistic to expect that Canadian skim milk powder in any significant volumes would be sold in Mexico in the 1960's until such time as an export subsidy was instituted and raised to the level where Canadian exporters could be competitive. For example, a 6.5¢ per pound subsidy in January 1968, given the Canadian support price of 20¢ per pound, placed a 13.5¢ per pound floor on the price that could be offered by the Canadian private sector on foreign sales. In fact in January 1968 CONASUPO purchased from the United States at a price below 9¢ per pound.

Inasmuch as the Canadian Dairy Commission determines the level of subsidy that applies in each case, it has a substantial influence over export sales regardless of whether the Canadian exporter sources privately or from the Canadian Dairy Commission. As put by Dr. Barry:

There were two forms of financial assistance relating to skim milk powder: either a subsidy on privately-procured or privately-produced product or a selling price of the Canadian Dairy Commission product which would have given the same net cost too, whichever route was taken. In other words, if our support price was 20 cents and we paid an export subsidy of ten cents for privately-produced powder then our powder would be available at ten cents." (Transcript 3773)

In the event that the Canadian Dairy Commission sold skim milk powder from its own stocks directly in an export transaction, it would of course not, even in form, pay itself a subsidy. It would simply absorb the loss and finance it from the revenues it received from the Government through the Agricultural Stabilization Board.

As for whether the prevailing level or levels of export subsidy to private exporters would influence the Canadian Dairy Commission's own pricing, as a matter of general principle, Dr. Barry stated in evidence that the amount of the export subsidy "... would I presume have been the basis for our pricing as well. ... out of a sense of fairness to Canadian exporters" (Transcript p. 3814). (In the only instance disclosed in the evidence when the Canadian Dairy Commission actually bid on a tender call in which the private sector was also interested, which was the January 1968 tender call referred to above, the Canadian Dairy Commission bid a price of 10.24¢, which does not appear to be reconcilable with Dr. Barry's general statement in view of the prevailing support price and export subsidy at the time.)

It appears that an export subsidy for skim milk powder was first established in Canada in late 1964 or in 1965. This was a very low subsidy that was increased to 3¢ per pound subsequently in 1965, was later raised to 5¢ in April 1967, and to 7¢ in September 1967. These subsidy levels were varied from time to time according to what the Canadian Dairy Commission felt was necessary for a satisfactory level of marketing of Canadian skim milk powder, although international marketing conditions did not change so quickly that the general levels of export subsidy were changed more than every few months. As stated by Dr. Barry in evidence:

"On April 17th, of the C.D.C. first year of operation (1967) a policy circular was prepared for the trade. It stated that the Dairy Commission would pay an export subsidy of five cents per pound subject to specified terms and conditions.

"On September 15th, another circular was prepared changing the subsidy to seven cents per pound. Further such circulars were prepared over the years, reflecting changing market conditions."

The general level of export subsidy from time to time reflects in part the difference between the international price and the domestic support price. Subject to the effects of any cartel-like agreements entered into by sellers or buyers, the international price is a free market price resulting from supply and demand conditions. The Canadian domestic support price, on the other hand, is a fixed price subject to periodic government review. For example, it was raised every six months or so throughout the 1970's, as the target support price for industrial milk was raised, so that it increased from 20 cents per pound at the start of the decade to 81 cents per pound as of April 1979.

As indicated above, there were no written guidelines used by the Canadian Dairy Commission with respect to deciding whether a change should be made in the general level of export subsidy and, if so, how much of a change. It was just a judgement that was made from time to time on the basis of all relevant facts as to what subsidy level would be effective.

By 1969, it had apparently become evident that the Mexican demand for skim milk powder, and the potential Canadian sales to Mexico, had assumed such dimensions that it was a particularly important export market for Canadian skim milk powder. Accordingly, the Canadian Dairy Commission established special terms and conditions relating to CONASUPO in particular, which terms were communicated generally to the trade by letter or telex (See documents 325 and 1364 of Exhibit 12 & 12A# for the general telex of February 11, 1969, and documents 479 and 1392 and the same exhibit for the

general communication by letter dated April 24, 1970).

The evidence was clear that although the Canadian Dairy Commission sought to retain maximum flexibility in setting and adjusting its export subsidy from time to time to meet competitive pressures as they materialized, it also made a conscientious effort to ensure that with respect to similar quantities going to the same market at the same time, all Canadian traders or prospective traders would be treated equally. Dr. Barry stated that if the Canadian Dairy Commission was going to adjust the level of subsidy for a particular transaction "the normal procedure was to send notices to the various people that we knew were interested in that particular market, any particular market... That subsidy announcement would have been sent to everybody who got the earlier announcement as to the earlier price." (Transcript pp. 3778-79). A similar point was made by Mr. Tudor-Price in a memorandum prepared for the Commission of Inquiry and marked as Exhibit 165:

"At various times in this period C.D.C. operated different prices and conditions for different countries simultaneously and gave different prices for large volumes than for small volumes to the same market. In March 1977, 10,000 m.t. of animal feed s.m.p. was sold by what amounted to a tender. In some cases C.D.C. normal selling terms of cash before release from warehouse were relaxed and payment against documents accepted.

"Prices were changed extremely frequently to reflect (a) changes in the competitive situation with other s.m.p. exporters (b) changes in competitive product prices particularly the Chicago 44% protein soybean meal price and (c) pressure of inventory and product age on C.D.C. commercial policy.

It would be impractical at this time to retrieve from C.D.C. files all the quotes, price indications, bids, counteroffers etc. made for animal feed s.m.p. by C.D.C. to the trade in the period.

I am not aware however of any situation where C.D.C. departed from the principle of treating Canadian traders equally when pricing similar quantities to the same market at the same time."

It was not as likely that such adjustments would be made with respect to potential transactions with CONASUPO because the special subsidy and conditions of sale applicable to exports to CONASUPO were specially considered and established in each of 1969 and 1970 and announced in advance to the trade.

One fundamental problem arising from the Canadian Dairy Commission's wish to retain maximum flexibility in determining the export subsidy from time to time and with respect to the particular competitive pressures in each case is that it is extremely difficult for any trader who distrusts the officials of the Canadian Dairy Commission to be assured that he is being treated fairly and equally with other exporters. The Canadian Dairy Commission has the power to respond to competitive pressures from abroad with respect to a particular sale possibility. The question may be asked as to why and on what basis the Canadian Dairy Commission should refuse to grant a sufficient subsidy to enable a particular exporter who might be interested in a particular transaction to be successful as against his foreign competitors? This question exists even where the best of good faith obtains among Canadian Dairy Commission officials. The system only operates fairly when the responsible officials are able to blot altogether out of their minds any feelings of antagonism or favouritism they might have towards any particular trader for whatever reason. Plainly, too, such a system is wide open to abuse. It is not a very persuasive justification to a suspicious mind for the Canadian Dairy Commission to assert that its decision as to the appropriate subsidy level was made solely on the basis of "our understanding of market conditions", to use Dr. Barry's words. (Transcript 3768).

Dr. Barry agreed in evidence that, as indicated by document 127, Exhibit 12, in the fall of 1967 the Canadian Dairy Commission essentially offered to the Granby Co-op to increase the export assistance to it to 8¢, for reasons particular to the Granby Co-op. It should be added that apparently nothing came from this proposal to either benefit the Granby Co-op or prejudice any of its competitors.

The ad hoc way in which the Canadian Dairy Commission administered its export subsidy policy, in the name of flexibility, is also illustrated by a telex sent by Mr. Gilles Choquette, Chairman of the Canadian Dairy Commission, to George Schafer on April 22, 1980, a copy of which was supplied by Mr. Choquette to the Commission of Inquiry and marked as an exhibit. In the telex, and in reply to a request by George Schafer for Canadian Dairy Commission "price announcement circulars", Mr. Choquette stated:

"The C.D.C. has not publicly announced the prices for products for export since 1976. It has been the practice of the C.D.C. to indicate prices to the trade in response to specific inquiries. We do this in response to constantly changing market conditions, changing levels of export restitution in the E.E.C., etc., in particular. This practice of not announcing



prices publicly has been of assistance to the Canadian trade: because it makes it more difficult for other countries to know Canadian prices when Canadian traders are bidding against them."

A note should be added regarding the funding of export assistance costs, by which I include the export subsidy and the storage, financing and marketing costs of exporting the surpluses that accumulate under the price support program.

Officials of the Canadian Dairy Commission speak in terms of the costs of export assistance being financed by the producers by means of a special levy made upon them for this purpose.

The levy on producers, which was instituted during the first year of the Canadian Dairy Commission's operation at the rate of 10 cents per hundredweight, began as a pro-rata holdback from the direct producer subsidy that was given by the Federal Government to producers of manufacturing milk and cream. It was not really a "levy" at all except in form and on paper. The producer never saw the money.

When the Interim Comprehensive Milk Marketing Plan and the Market Sharing Quota program were instituted in 1970, and as the provinces joined that program one by one over the next four years, producers in those provinces received the direct producer subsidy without the holdback. A levy to defray costs of disposing of surpluses on export market was and is, however, deducted monthly from the market payments to producers. The amounts so collected are remitted to the Canadian Dairy Commission by the administering provincial milk marketing agency.

When the levy was instituted at the ten cent level in 1966-67, the direct producer subsidy was 85 cents per hundredweight. Although the amount of the levy was adjusted from time to time, it did not change significantly until 1975 when it was raised first to 45 cents and then to 90 cents per hundredweight. The following year it rose to \$1.35. It has since been reduced to \$1.00 per hundredweight (\$2.27 per hectolitre), which is slightly more than one-third of the current direct producer subsidy of \$2.66 per hundredweight (\$6.04 per hectolitre). The levy applies to all within-quota production; there is an additional deduction made with respect to deliveries by particular producers that are in excess of their quotas.

It should also be noted that the "export levy" has not, except on an occasional temporary basis, usually funded the entire cost of export assistance for skim milk powder. Dr. Barry testified that during the fiscal years 1967 to 1972, as a period, the levy covered approximately seventy-five percent of the cost of export assistance for skim milk powder. The other

twenty-five percent was simply paid for by other funds the Canadian Dairy Commission received from the Government.

As of July 1, 1975, ostensibly to even out the large fluctuations in the amount of the export levy that appeared imminent as a result of the drop in the international price, an "Export Equalization Facility" was established. This was in essence a special loan account under which the Canadian Dairy Commission was authorized to average out the export levy over a five year period so as to minimize the impact on producer returns and yet recover export "equalization" costs and interest over the five year period. A forty million dollar cash deficit or surplus was authorized for the Facility for this purpose.

The Export Equalization Facility was not a success. By March 31, 1977, it had a deficit of \$159.7 million. The government decided the taxpayers would absorb the loss, and terminated the experiment. It was then decided, after hearing representations made by the producers, that the liability of producers of manufacturing milk and cream to pay for export assistance would be limited in absolute amount by limiting the amount of the levy. The rest would be made up by a special annual Government contribution and by a levy on fluid milk production.

#### (C) SCHAFER BROS. LTD.

In 1925, in Hungary, Mr. David Schafer and his two brothers, began exporting commodities to various countries. According to Mr. Schafer, their firm soon became one of the largest privately-owned grain firms in Hungary.

As to his general background and experience David Schafer stated that in 1919 he worked as a commissioner in merchandising at the Anglo-Hungarian Bank, sold agricultural products and became a member of the Budapest Grain and Stock Exchange. He stated that in 1928 he was elected a member of a Hungarian Legislature, and that in 1930 and 1934 he was elected president of the Hungarian Provincial Exporters Association. He was also elected a Council member of the Budapest Grain and Stock Exchange, which, according to him, was one of the largest such exchanges in the world at that time.

During World War II David Schafer was interned in a Nazi concentration camp, but he said he was taken out of the camp several times to be consulted about trade matters.

Although World War II interfered with his business, Mr. Schafer stated that after the War he built up the business once again.

At the end of World War II, he said that he was sent by the Hungarian Government as a one-man

mission to every major city in Europe in order to help to reorganize Hungary's export business.

Mr. Schafer said that he refused to become one of the permanent directors of the Hungarian Government grain and seeds organization because the Hungarian Government nationalized his business in Hungary without any form of compensation. He left Hungary in 1948, abandoning large sums of money, and came to Canada.

Mr. Schafer said that through the business firm he established in Montreal, he began exporting Canadian agricultural products to customers he had served in Europe. He said that in the 1960's he made several business trips to Cuba and Mexico for the purpose of discussing the possibilities of selling Canadian skim milk powder and developing markets for that commodity; that during that period, he met or corresponded with officials of the Cuban purchasing agency (Bancec) and the Mexican agency (CONASUPO); that he also had business relations with PROQUI, a Mexican firm involved in the sales of skim milk powder; that he exchanged information with them regarding their requirements and specifications for skim milk powder and the quality of Canadian skim milk powder; that he kept Canadian government officials (at the Agricultural Stabilization Board and at the Canadian Dairy Commission) informed about his efforts in those countries; that in 1961, Schafer Bros. Ltd. sold 5,500,000 pounds of skim milk powder to Cuba; and that in 1969 Schafer Bros. Ltd. sold and shipped to CONASUPO, without using agents, 770 tons of skim milk powder.

Mr. George Schafer is 42 years old. He said that he had worked in the family business since he was 7, but that he had no formal education in the dairy industry, in the export business or in agriculture. He said that between 1963 and 1967 he spent long periods of time in Europe and Asia, especially Hong Kong, trying to create markets for Schafer Bros. Ltd., but that he did not involve himself in seeking to develop markets in Latin America and specifically in Mexico until 1969.

Mr. David Schafer said that he was the president of Schafer Bros. Ltd. and that his son George and George's wife were the only other directors and shareholders. Schafer Bros. Ltd. is located in the Board of Trade Building, 300 St. Sacrement Street, Montreal, Province of Quebec.

Mr. David Schafer said that he and his son George owned certain other inactive family companies and also St. Lawrence Seeds Ltd. St. Lawrence Seeds Ltd. was mainly involved in the export and import of seeds and cotton and, according to Mr. George Schafer, had exported seeds to European countries and imported raw cotton from Mexico, acting as agents for Mexican companies.

Mr. David Schafer said that while St. Lawrence Seeds Ltd. sometimes made a small profit, Schafer Bros. Ltd. has not made a profit for the last 15 years.

Mr. David Schafer had two basic concepts of or relating to the rights of Schafer Bros. Ltd. to the CONASUPO market for Canadian skim milk powder:

1. In his view the Canadian Dairy Commission had been created not to compete with private traders, but that one of its functions was to help them to export Canadian surpluses "for the benefit of Canada";
2. Since, in his belief, Schafer Bros. Ltd. had alone created the CONASUPO market, he claimed it had an exclusive and monopolistic right to sell to CONASUPO Canadian skim milk powder for as long as it wished to do so.

These two basic concepts of David Schafer, and also of George Schafer, are illustrated by the following few excerpts from some of their letters. On February 19, 1969, George Schafer wrote to the Honourable H.A. Olson, then Minister of Agriculture (Exhibit 12, p. 332) stating:

"... it is up to the C.D.C. to facilitate the business in every way possible!!! The C.D.C. should not try to be an export sales organization but try to do the best possible job as a service organization."

And on May 5, 1969 (Exhibit 12, p. 389):

"We understand that this year again the C.D.C. is bidding direct in competition with us. This is not the function of the C.D.C."

In a letter to Mr. George C. Lachance, M.P., dated February 10, 1971 (Exhibit 12, p. 532), David Schafer said:

"In our opinion, an Agency of the government whose employees are paid from the taxes on private business, should not be allowed to take away private business. Their job is to provide accurate information and possibly regulate the market but NOT to transact business.

"Canada NEEDS its entrepreneur exporters who create new markets for the country. The government should not allow them to be exterminated."

David Schafer, in a letter to the Honourable H.A. Olson, dated May 17, 1971 (Exhibit 12, pp. 598, 600-01) wrote:

"JUSTIFICATION & POLICY. How can a Liberal government justify the further expansion into the export sales field of a State

Enterprise such as the Canadian Dairy Commission, depriving private firms of their livelihood? This is the case when the Dairy Commission takes away Mexico as it had done with Cuba (our firm's two principal customers) making government to government sales. In my opinion, under a Liberal government, state enterprise must refuse to enter into business negotiations, and categorically tell the interested buyer that he must deal with private concerns. The state organization should be there to regulate the market, and assist the exporter in every possible way, including credit and performance guarantees, market information, etc."

"RECOMMENDATIONS. In order to help Canada achieve economic independence, it must give every possible assistance to EXPORTS and to its QUALIFIED EXPORTERS, to build a group of Canadian citizen exporters (including Agents and Brokers) serving exclusively the Canadian interest. Including, but without limitation by enumeration: Incentives and Commissions must honour their work, along with all facilities they require, much better coordination for using combination deals as leverage and more flexible trading and services. As regards to the Canadian Dairy Commission, we would suggest the following. IT should

- a. regulate the market
- b. be deprived of all export sales powers
- c. provide export financing, (or financing and performance guarantees) wherever necessary
- d. provide world production, market, and price INFORMATION to EXPORTERS."

On December 16, 1971 (Exhibit 12, p. 675) David Schafer wrote to the Honourable H.A. Olson as follows:

"... tell us if you don't agree that it is fair, equitable, in the national (EXPORT SALES STRENGTH) interest, and in the realm of possibility:

1. that we receive a reasonable normal commission of 2% after all the milk powder the CDC sold direct to CONASUPO, Mexico
2. the Canadian Dairy Commission be prohibited to enter into any export sales agreement
3. that the CDC's activities be restricted to regulate the market and to ASSISTING private exporters through providing information

on world production, prices, and market conditions as well as to meet foreign requirements, export credit, etc. (together with EDC at competitive rates tolerable for low markup agricultural commodities)."

With respect to their concept that Schafer Bros. Ltd. should have monopolistic control of the skim milk powder market between CONASUPO and Canada for as long as Canadian skim milk powder was being sold to CONASUPO, or until such time as Schafer Bros. Ltd. informed the Canadian Dairy Commission that it was no longer interested in that business, George Schafer had the following exchange:

"George Schafer: Schafer Bros., in the case of Mexico, should have had the support of the Canadian Dairy Commission, to continue to do the business which it had informed the Canadian Dairy Commission it was trying to get, which it did get and it was continuing to pursue. In this case after having worked for a long time, I believe that Schafer Bros. should have had the support of the Canadian Dairy Commission to do...

Q. Should it have had a monopolistic interest in the Mexican market?

A. Not necessarily a monopolistic interest with all the Mexican market, but with CONASUPO yes.

Q. It should have had a monopolistic interest in?

A. With that one customer.

Q. For how long?

A. For as long as the business was going on. For as long as Canada was doing business or for as long or until such time as Schafer Bros. Ltd. informed the Canadian Dairy Commission that it was no longer interested in pursuing business.

THE CHAIRMAN: Why?

George Schafer: This is the way we would have operated with our —

THE CHAIRMAN: But why should they have that monopolistic control of that market? Why should Schafer Bros. for evermore or until they decided they did not want it. Why?

George Schafer: This is the way I have been brought up to think. My father who has been in- a member of the Arbitration Council of the Budapest Grain & Stock Exchange would have brought this kind of a ruling in an arbitration case. He has brought me up in this belief. . . (transcript pp. 2349-51)

Mr. David Schafer, after having read the evidence given by his son regarding this concept, said that he agreed with the statements made by George, but not with the conclusions. David Schafer's conclusion was that Schafer Bros. Ltd. should be paid a 3% commission, as compensation, on all Canadian skim milk powder sales to CONASUPO from 1968 until now. He said he based the percentage figure on the particular commission paid to Ault Foods (1975) Ltd. under its August 1977 contract with the Canadian Dairy Commission. David Schafer also said that from now on the CONASUPO business in Canadian skim milk powder should be split among Schafer Bros. Ltd. and the firms which were in that market in, or prior to, 1968, or which had sold Canadian skim milk powder to CONASUPO directly or through Mexican agents, namely: Ronald A. Chisholm Ltd., Eastern Townships Produce Ltd. and maybe Granby Co-op.

Essentially the views of both David Schafer and George Schafer which appears from their oral evidence and their correspondence is that once Schafer Bros. Ltd. has attracted a customer, it is entitled to have the customer deal exclusively with Schafer Bros. Ltd., which is entitled to be shielded from competition.

Although their views displayed some divergence — in that George Schafer demanded a monopoly of trade between the Canadian Dairy Commission and CONASUPO "as long as Schafer Bros. wishes to continue in that market", whereas David Schafer was prepared to share the trade in Canadian skim milk powder with CONASUPO with those other traders who participated in this market in the 1960's (in other words an exclusive oligopoly), the difference is one of degree and not of principle.

There is nothing novel in such views; indeed, they reflect the ancient guild tradition built up through thousands of years, reaching its most comprehensive expression in the restrictive mercantilist policy of France in the 18th century. The guilds which were organizations for the defense of the trade interests of those who belonged to them, adopted regulations for the conduct of business transactions and to suppress competition.

The guild had a policy to reduce, if it could not eliminate, competition and to protect its members against entry by third parties to its markets, trades and professions.

It is interesting to compare the concepts of the Schafers with various rules of conduct adopted by guilds:

"Again, it was forbidden to monopolize customers, to invite into your own shop the people who had stopped before a neighbour's display of goods, to call in the passers-by, or to send a piece of cloth on approbation to a

customer's house. All individual advertisement was looked on as tending to the detriment of others. The Florentine innkeeper who gave wine or food to a stranger with the object of attracting him to his hostelry was liable to fine. Equally open to punishment was the merchant who obtained possession of another man's shop by offering the landlord a higher rent. Any bonus offered to a buyer was considered an unlawful and dishonest bait."

Georges Renard, *Guilds in the Middle Ages* (London: G. Sell and Sons Ltd.) p. 42.

"In the market 'good form' must be observed between members of the same gild. One member must not intrude before a sale is consummated. 'If anyone is in front of the stall or window of a cook to buy or bargain with the said cook, and if any of the other cooks call him before he has left the stall or window of his own will,' the fine would be 5 sous."

F.B. Millett, *Craft Guilds of the Thirteenth Century* (Kingston: The Jackson Press, 1915).

"The real regulation of competitive practices during the early part of the middle ages was by the guilds themselves. Trade was largely localized in towns. The guilds dominated the trade and the usual lack of a strong central government made these organizations very powerful within their own towns. Guild regulations prohibited various methods of competition and imposed fines and other severe penalties for their violation. The enticement of employees was prohibited by many guilds. The plumbers in London in 1365 provided that 'no one of the said trade shall oust another from his work undertaken or begun'. Interference with a competitor while making a sale to a customer or disparagement of a competitor's goods were likewise condemned. For example, the Merchant Adventurers of Newcastle-upon-Tyne in 1669 enacted the following ordinance:

"...it is ordered &c. That noe brother or sister shall, either by themselves, their servants, or anie other person whatsoever, call too, or invite anie person, either by word or anie signe, to come to their shopps or sellars, while such person is either speaking with another of this Fellowship or his servants, against their owne shopps, sellar, or houses, or goeing with them to shew them anie commodity, or be present with them or anie of them; but shall dilligently attende their cus-

tomers, comeing to theire owne shopps and sellars. And that in theire selling they shall not undervalue or disgrace their neighbours goods, but leaveing every chapman to his owne discretion in buying the goods he is to buy, and hath presented to him. Upon paine that every brother or sister soe offending shall forfeite, for the first offence, twenty shellings, for the second forty shillings, and for the third five pounds."

Jones, Franklin D., "Historical Development of the Law of Business Competition", (1926-27) 36 Yale L.J. 351 at 368-69.

"Their ordinances were framed for the 'better relief and comoditie of the porer sorte'. No Gild-associate was to entice away a brother's customers nor a brother's servant."

*English Gilds*, Edited with notes by Toulmin Smith, (London: N. Trubner & Co., 1870) p. cxxxi

"The ambitious aim of the ordinances, according to the *Book*, was to ensure 'that the human race may be governed fittingly and no person may injure his fellow.' There was a high degree of division of labor, and each man must keep within his own bounds. The weaver could not be a merchant, the spinner could sell only yarn. Victualers must not encroach on the preserves of the perfumer, soapmaker, linen merchant, tavern keeper, or butcher 'even in the slightest degree,' under pain of the customary flogging, shearing of locks and beard, loss of goods, and banishment." (p. 198)

"While seeking to protect its members against outsiders, the guild protected them against each other. Unfair competitive methods were forbidden." (p. 201)

**"Craft Guild Policies.** Guild ordinances touched the guildsman's relations with fellow members, non-members, members of other guilds, future members, dependent workers, and consumers. The spirit that animated them was one of comprehensive protectiveness; the group was to be protected from competition or injury by outsiders, the individual member was to be protected from the destructive, unfair, or fraudulent competition of his brethren, while both he and the consumer were to be protected from defective workmanship and poor or dishonest products." (p. 203)

"Many ordinances sought to secure fair play and equal competitive conditions between rivals. Masters must not try to steal one another's workmen or customers or strive to gain an advantage in securing raw materials. Goods must not be hawked through the streets, but be offered only in shop or market. At St. Omer the seller was forbidden to attract attention by blowing his nose or sneezing when customers were

around. The boatman bringing beer to Bruges must not display any signboards singing the praises of his cargo. The professional ethics of medical and legal practitioners are a survival (or revival) of these rules against blatant solicitation or advertisement." (p. 207)

"How far guild opposition actually retarded technical advances we cannot say, but the attitude certainly was cautious and suspicious. The ideal was 'stability of conditions in a stable industrial organization' (Pirenne), 'order rather than progress, stability rather than expansion' (Lipson). Free competition, if such an idea was conceived, seemed to be a dangerous disruptive notion, the enemy of the existing order." (p. 207-8) Heaton, Herbert, *Economic History of Europe* (New York: Harper & Brothers)

From these references it should be noted at this point, before reviewing the evidence concerning the objects and purposes of the Canadian Dairy Commission and concerning the allegations and issues, that the Schafers' concepts of the role of the Canadian Dairy Commission and of competition in the market are not in accord with Canadian public policies.

#### (D) CONASUPO (MEXICO)

As stated, Compania Nacional de Subsistencias Populares ("CONASUPO") is the sole and exclusive authority for importing skim milk powder into Mexico. At least in the late 1960's, large purchase orders placed by CONASUPO, and the selection of the vendor, were done at the senior levels. Smaller orders apparently were handled at the level of the Purchasing Department. For the big orders, however, everyone on the register was invited to submit a tender. The Director General made all the final decisions with respect to the larger orders where price appears to have been the major factor in selecting the vendor. Confidence in the performance capability and reliability of the supplier was also taken into account in some manner.

Mexico elects a new President every six years. Apparently, although there is one dominant political party, with the election of a new President there is usually an extensive change-over and shift in senior and decision-making personnel and administrators, because that is the prerogative of the new President. The new administration takes office at the end of the year in which the presidential election is held. This frequent change-over of government personnel affects CONASUPO as well, so that several new key people, including the Director General, changed as of 1965, 1971 and 1977. These dates may have some significance to this Inquiry, as certain important events occurred at those times, i.e.:

1965 — David Schafer first met CONASUPO officials, introduced by Mr. Rocchi;

1971 — (a) Messrs. Rodriguez Ayala and Rodriguez Licea and the Director General, whom David Schafer knew, left CONASUPO;

(b) CONASUPO entered into an exclusive buying arrangement with the Canadian Dairy Commission with respect to Canada. (This was part of an overall policy of the Mexican government, which also extended to a number of other products).

1977 — The Canadian Dairy Commission decided it needed an agent for its business with CONASUPO.

Mexican demand for skim milk powder began to escalate in 1968. By 1973, Mexico was importing over 41 million pounds of skim milk powder annually, and in 1980, the annual demand is approximately 90 million pounds.

#### (E) PHILIPPINES, ALGERIA, PERU AND CHILE

Schafer Bros. Ltd. does not make any claim for compensation regarding the matters raised in the allegations concerning the Philippines, but made those allegations to seek to demonstrate the Canadian Dairy Commission's lack of cooperation and attitude towards the Schafers, and to seek to demonstrate that the Canadian Dairy Commission should be more aggressive in assisting export sales of Canadian skim milk powder.

As for Peru, Chile and Algeria, the matters raised in the allegations, either by their nature or by the circumstances surrounding them, have little significance and were made in order to raise questions which Schafer Bros. Ltd. felt should be answered regarding the extent of the Canadian Dairy Commission's willingness to cooperate with Schafer Bros. Ltd.

## CHAPTER IV

### EVIDENCE CONCERNING THE OBJECTS AND POLICIES OF THE CANADIAN DAIRY COMMISSION

Two basic objects are set by Parliament for the Canadian Dairy Commission in Section 8 of the *Canadian Dairy Commission Act*. The first object of the Commission is "to provide efficient producers of milk and cream with the opportunity of obtaining a fair return for their labour and investment". The second object of the Commission is "to provide consumers of dairy products with a continuous and adequate supply of dairy products of high quality."

The only directive given by Parliament as to the manner in which the Commission must carry out its functions are that the Commission shall carry out its functions under the Act in a manner that will achieve its objects and meet its obligations from the monies available to it under the *Canadian Dairy Commission Act*.

It should be noted that Section 8 of the *Canadian Dairy Commission Act* is directed to provide for efficient producers of milk and cream and to provide for consumers of dairy products. It is not directed to all producers, nor is it directed to processors, to private traders or to any other persons.

Because the Order-in-Council directed, *inter alia*, that there be an Inquiry into whether or not the Canadian Dairy Commission, its officers and employees acted lawfully and fairly (in one aspect of the meaning of that word) in respect of certain of its commercial practices, it has been necessary to consider the meaning of Section 8 and to hear evidence as to the manner in which the Canadian Dairy Commission by its policies has sought to implement the objects of the Commission as laid down by Parliament in Section 8.

Any body created by Statute may only exercise the powers conferred upon it by or pursuant to the enabling statute or any other relevant statute. In addition, those powers are only lawfully exercised if they are exercised in order to implement the purposes for which the body was created (see *Re Doctors Hospital and Minister of Health et al* (1976), 12 O.R. (2d) 164 at 174-176; and *The Agricultural Stabilization Board v. Jacobs Farms Limited et al* (Federal Court of Appeal, File A-432-79, April 25 1980 unreported).

It was therefore important that evidence be adduced in respect to these matters. This was made

especially apparent because of the fact that one of the principal threads underlying and running through most of the evidence adduced before the Commission was the question of the process for holding the Canadian Dairy Commission accountable for the exercise of its very considerable powers. Perhaps this Inquiry would not have been necessary had an adequate system existed for measuring and checking all aspects of the performance of the Canadian Dairy Commission.

Directed to determining the issues of lawfully and fairly, evidence was given at the Inquiry by Dr. Lawrence Skeoch, by Dr. S.C. Barry, Chairman of the Canadian Dairy Commission from 1966-1973, and by R.M. Cloutier, Director of the Economic Study Section of the Canadian Dairy Commission. The remainder of this Chapter sets out their evidence.

The legal implications are considered in Chapter VII.

#### *Evidence of Dr. Lawrence A. Skeoch*

Dr. Skeoch was not asked to undertake any special study of the Canadian Dairy Commission or of any particular allegations made by Schafer Bros. Ltd. Instead, because of his background as a senior Canadian economist of very considerable stature, particularly in the fields of agriculture and industrial organization, he was asked to give opinion evidence regarding the policies of the Canadian Dairy Commission in carrying out the intent and meaning of Section 8 of the *Canadian Dairy Commission Act*, whether such policies were in fact carrying out the intent of Parliament when Parliament enacted the section, and whether or not such intent could not be better implemented by different policies.

It is convenient, if somewhat arbitrary, to summarize Dr. Skeoch's evidence first under seven headings: general comments, "efficient producers", "fair return", "adequate supply", cost justification, price support programs, and general proposals; and second, regarding matters of accountability for the adequacy of policy and programs.

#### 1. General Comments

The fundamental concern that Dr. Skeoch stated he had in the field of public policy, including that relating to agriculture, is that measures be adopted that preserve or maximize the long run flexibility and adaptability of an industry, and its ability to change over the long run to take account of new technological and organizational developments. In his words "economic progress depends, as much as on any other factor, on the energy, inventiveness and creative imagination of particular men, attributes which are more likely to be developed and maintained by opportunities for independent action and the relatively

unconfined exercise of initiative. The consequences of excessive centralization [i.e. of decision-making power] may be more serious in the long run than in the short run."

It is this perspective that leads Dr. Skeoch to the view that concepts such as "efficient production", "fair return", and "adequate supply" are essentially long run in nature and are incapable of meaningful definition apart from a market context. To him they implicitly impose some requirement of market effectiveness. Dr. Skeoch stated that there was no way that one could tell whether producers or others were operating efficiently, or whether the prices were fair, or whether the output was adequate except by a relationship to market pressures and market criteria. In the absence of such criteria, one's judgments could be nothing but arbitrary or political.

As to the general utility of preserving as much of an open market economy as is compatible with other statutory objectives, Dr. Skeoch stated:

"The unavoidable reality is that outside an effective dynamic market economy, our society has no way to deter or penalize the wasteful use of resources, to compel technological innovation, or to direct production toward the satisfaction of consumer wants. Indeed, without competitive challenge, or the threat of such challenge, we cannot even measure waste, inefficiency, or technological stagnation."

In Dr. Skeoch's view one of the great long-run advantages of maximizing market forces, so far as these may be compatible with the statutory objectives, is that one thereby maximizes the economic usefulness of prices to signal the relative scarcity of different resources and commodities, and to serve as indicators of change in demand, supply and technological conditions. The price system in the market economy cannot be duplicated by a centrally controlled, administered system. It is the key to the incomparable ability of a market economy to transmit and utilize information. In Dr. Skeoch's words, "the market-induced search by thousands of individual minds for maximum efficiency, for opportunities for experimentation and innovation, creates a productive and optimizing effect of great force".

The great danger of administrative intervention in an industry, said Dr. Skeoch, is that it will not be a tool for adjustment but instead will turn out to be a device for supporting an existing system of production and existing cost-price relationships:

"The forces of economic progress are not self-perpetuating but tend to come to rest through the entrenchment of existing interests. The search for stability too often becomes a search for pseudo-security, secu-

rity, that is, that is based on the inhibition of change, and the avoidance of dynamic change. The fact that these considerations are incapable of precise quantification is no reason for doubting their basic importance."

It is, of course, unfortunate if the response to the short-run problem, in agriculture or anywhere else, takes the form of defending the status quo through the entrenchment of existing interests. Dr. Skeoch's overall assessment of government policy with respect to agriculture was expressed as follows:

"Government policy with respect to agriculture appears. . . to assume that the time-scale is unimportant, that innovation and dynamic change can be largely left to take care of themselves, and that its major focus should be limited to achieving some defensible level of 'government guaranteed profitability'."

Dr. Skeoch was generally critical of government price support programs, for the reason that by masking market signals they may inhibit continuous improvements in efficiency at substantial economic cost to taxpayers, and in particular to farmers and consumers over the long run. Dr. Skeoch generally took a dim view of comprehensive supply management schemes, while at the same time being of opinion that some intervention by government was essential in the case of agriculture, especially in the dairy industry sector of it. He felt that it was an exercise in self-deception to seek to control "market information" by imposing production quotas, by arbitrary allocation devices, and "by deriving prices from a cost-justification base frequently determined by formula rather than from the pressure of market forces..." He put it this way:

"Since thorough-going market controls create their own market 'information' by allocative decisions which severely limit the scope for individual producers and sellers to respond to the imposed market signals, there is a tendency for the planning authority to consider the result as representing an equilibrium situation, and any departure from it as representing 'instability'."

This problem of distorted market information is even more acute in a case where one person, such as the Canadian Dairy Commission, whether by virtue of the Government price support program and export subsidies, or otherwise, has such a large degree of power on both the buying and the selling sides of the market as to be substantially insulated from market pressures. The Canadian Dairy Commission being such a person can in large part settle both the supply and the demand sides of the equation, so that there is no standard for the measurement of efficiency, fairness or adequacy of anything. The limitations imposed upon production and entry create artificial



value attaching to the (quota) restrictions, with "consequences for the movement of resources, for investment valuation, and for producer management initiative that are difficult to quantify and appraise".

## 2. "Efficient Producers"

Dr. Skeoch testified that it was extremely important that consumer prices should be at the lowest level attainable. He further stated that consumers and producers of food require, in their own best interest, maximum efficiency of production in both the short and the long term, together with minimization of the costs of processing and marketing.

"Efficiency" to Dr. Skeoch is a word that can only be given substantive content in long-run terms of openness of an industry to market pressures and to change. As he put it:

"Efficiency is one of those words that everybody believes in until he has to adjust in order to make some contribution to it. The difficulty with efficiency is of course, that efficiency is a forward looking concept. It is not a static concept. It isn't a matter of static allocation of facts. It has very important dynamic dimensions..."

Dr. Skeoch, far from taking the view that he or anyone else could predict change or effectively utilize all relevant market information, said that nobody could possibly know what is going to be "efficient" five years from now in static terms. He was very firm in his view, however, that if the ends tend to be short-run, then there must inevitably be a conflict between the "efficiency" goal and the ends, "because you cannot talk of an efficient industry simply in terms of short-run results. You have to look to whether the industry is flexible and adaptable..." Production control, for example in Dr. Skeoch's view inevitably conflicts with the goal of "efficiency".

Dr. Skeoch did make clear that his comments regarding efficiency were not to be taken as any endorsement of the private sector over the public sector. He stated that there was no basis for assuming that the private sector was more effective than the public sector in achieving long-run efficiency. The difficulty, however, was that the private sector is generally forced to change and adapt according to market pressures, whereas the greatest care must be taken to ensure that proper incentives and opportunities for change exist in the public sector to the extent that it is insulated from the market pressures.

In answer to a question by counsel for Schafer Bros. Ltd. Dr. Skeoch expressly repudiated any suggestion that it would in some way be inefficient for a marketing board such as the Canadian Dairy Commission to compete with exporters to whom it sells product. In his words: "Competition is competi-

tion and it shouldn't be soft competition. Soft competition is not really what we are trying to get..."

## 3. "Fair Return"

"Fair return", like "efficient production", is a concept which, in Dr. Skeoch's view, is essentially long-run in nature and incapable of meaningful definition apart from a market context. It is something that can only be defined in terms of alternatives, and whether the market would actually yield that sort of return. In his words:

"The fair return is the long-run return that you can earn in a reasonably competitive market. It is nothing more than that and there is no other way to give it economic content. You may be able to give it other types of content but you can't give it economic content in any other way of defining it."

## 4. "Adequate Supply"

"Adequate supply" is a long-run, market-oriented concept for the same reason as are the concepts of "efficient producers" and "fair return".

Dr. Skeoch testified that if production restrictions are imposed, consumer preferences cannot possibly be effectively registered: "There is no way you can register a preference for something that you are not presented with. You have to have an alternative..."

Dr. Skeoch was asked certain questions relating to statistics outlined in Exhibit 145, which was a Canadian Dairy Commission pamphlet entitled "The National Dairy Program, 1979-1980". Apart from observing that the decline in Canadian requirements for industrial milk during the 1970's was understated by the Canadian Dairy Commission pamphlet, in the sense that by ignoring the population increase it only reflected about one half of the actual decline in per capita consumption, Dr. Skeoch testified that the reasons for the steady decline of per capita consumption of industrial milk in Canada might not have been fully explored by the Canadian Dairy Commission:

"There is also the other possibility, and you can't rule it out, and that is that there was a very substantial increase in price. The normal response to an increase in price is of course a decline in consumption. You can't say that a decline in consumption was not in any sense due to an increase in price since a reduction in price was not tried so far as I am aware."

Dr. Skeoch put the same proposition elsewhere in his evidence as follows, on cross-examination by counsel for the Canadian Dairy Commission:

"You can always get an adequate supply by putting the price so high that very few people want to buy. An adequate supply has no

meaning without reference to price. It is just a meaningless concept. You can say, well, if I am charged \$10.00 a dozen for oranges there will be very few oranges consumed and that would be an adequate supply of oranges. If you look at the production, the production now, a decline of 22% or more in industrial milk over a period of — that relatively short time — it would at least give you a *prima facie*, raise a *prima facie* question as to whether an adequate supply was provided. It doesn't prove it but it does raise a *prima facie* question."

And elsewhere:

"What is an adequate supply depends upon the price you fix, you see. You can always get an adequate supply. If you are going to charge \$2.00 a pound then, an adequate supply would be one amount. If the price were going to be \$1.00 a pound, an adequate supply would have been altogether different, so there is no formula that you can simply adopt to say, 'This is an adequate supply because we fixed the price at such and such a level and this amount is taken at that price.' The question is: Is that price a reasonably competitive price? Is that price arrived at by pressures of the market and by incentives to invest and so on? Otherwise, you are simply saying, 'Well, the supply always equals demand.' You know that is one of those irrelevancies that some ponderous people tell us. Supply and demand determine price. They look as if they had said something. The question is: What determines supply and what determines demand? If you have an international cartel, they can make supply and demand equal. Supply and demand will determine price quite easily. They just control the supply and it is a relatively simple matter so there is no way that you can determine what is an adequate supply and so on apart from such market tests. . . . Once you depart from that sort of test you are simply saying, 'Well, we fixed the price at so and so and so much butter or so much cheese or so many tires or so many gallons of gasoline were taken at that price', and that's obvious but that is not what we mean in economics by efficient production, by an adequate supply or by a fair price."

In answers to further questions addressed to him by counsel for the Canadian Dairy Commission, Dr. Skeoch observed that if one were going to restrict output in the first place, it could virtually be assumed that the controlled output would not be adequate in the sense that producers would be willing to provide

more to the consumer at that price than they are permitted to provide. The existence of production controls, in other words, creates a *prima facie* case of inadequacy.

##### 5. "Cost Justification"

The use of retrospective and static cost justification formulae is an aspect of the broader question of "fair return" with respect to which Dr. Skeoch was highly critical. In his view such a basis for prices and returns was incompatible with the limitation of the statutory goal to "efficient" producers.

The basis of Dr. Skeoch's criticism is reflected in a quotation which he adopted from the writings of an authority in the field:

"Among the most popular of the notions about fairness and pricing is the idea that a seller is entitled to a price which will cover his cost plus a reasonable profit. Few propositions gain readier acceptance particularly among persons supposedly sophisticated among business matters. It seems reasonable that a fair price should reflect the cost of production, that no one should be required to do business at a loss, that everyone should receive suitable compensation for his efforts. The weakness of the argument, often surprisingly obscure, lies in the fact that what it costs to do a job is not necessarily related to what it is worth to have it done. Yet, despite its unsoundness, the argument is widely employed and surprisingly persuasive. Sellers explain their costs must be raised because their costs have gone up. So often the explanation is patently absurd. Most utility regulation embraces the theory that cost must be reflected in prices. Legislatures are readily persuaded that price controls must not compel sales below cost. It is extremely dangerous to assume that the existence of a cost justifies the establishment of a price. What encouragement would there be for efficiency and economy if every excess cost could and should be readily passed on to the buyer? The deplorable condition of the whole building industry presents striking evidence of the exploitation which might become general if all groups in a community were permitted to practice extortion (as he puts it) through make work, output restriction and other cost maximizing devices applied with sanction by the public and the constituted authority."

A short-run cost justification approach, according to Dr. Skeoch, effectively denies a role for demand in the setting of prices. It weakens the forces working for the introduction of new technology and new forms of business organization over time, insulates people

from market pressures and is inconsistent with the fundamental principles of long-run dynamic change. In reality it provides no protection to the producers who are or can be efficient and effective in the longer run.

As to price support programs, Dr. Skeoch pointed out that they typically require production controls, and benefits to farmers become capitalized into the cost structure, usually through the factor with the more inelastic supply (e.g. land). Entry by new producers or expansion by producers already in the industry becomes more difficult and prices do not perform their proper signalling function.

In the longer run the combination of cost-justification pricing and quota controls results in substantial windfall gains to the "first generation" holders of quotas, which discourages entry and creates an upward ratchet effect on "costs" as the quota holders attempt to amortize their investment and, if at all possible, to emulate their predecessors in enhancing quota valuations.

In summary, it was Dr. Skeoch's view that it was absolutely essential, if one wished to maintain the flexibility and adaptability that is necessary in an economy that will achieve the objectives set out in Section 8 of the *Canadian Dairy Commission Act*, that a retrospective cost justification formula not be adopted or utilized.

## 6. Price Support Programs

Dr. Skeoch's general views regarding price support programs have already been referred to. In essence, Dr. Skeoch testified that price support programs obscure market signals and over the long run they may inhibit continuous improvements in efficiency at substantial economic cost. He felt that they relieved the distributors and processors from essential market pressures, and, in general, "that the public in the sense of consumer plus taxpayer... is always better off" with a direct subsidy to producers instead of a price support program.

I take Dr. Skeoch's view as applying equally to the extent that a price support program might supplement a direct subsidy to producers, as is in fact the case with the Canadian Dairy Commission.

Dr. Skeoch referred to a price support program as "a high price line" in that supports are fixed for processed products that are traded internationally, such as butter, cheese and skim milk powder, with the home market prices being kept above world prices by means of protection at the border. This protection at the border applies to the processed products and not to the raw material such as, in this case, the producer's milk. What Dr. Skeoch referred to as the "low price line" policy, or in other words the direct subsidy

to the producers, involved domestic acceptance of world market prices, with the price seeking its own competitive level in the market. With the low price line, farmers would be given subsidies on products produced by them in order to bring their incomes up to the level that was determined by government to be socially acceptable.

Dr. Skeoch testified that the high price line, or price support programs, had the disadvantage of extending the shelter from competition beyond agricultural production to the food processing and distributing industries, thereby lessening the pressure on the processing and distributing sectors of the industry to reduce their costs. Price support programs therefore, over the long run, tend naturally to interfere with the achievement of real cost economies or higher levels of efficiency throughout the relevant part of the agricultural industry.

With the low price line (which involves direct subsidies to the producer) a producer is free to adjust his output from time to time as he sees fit. In Dr. Skeoch's view the reason why the high price line is so popular is because it is easier politically, in that it serves to diffuse and disguise the amount of the real subsidy being given to producers. I understood that Dr. Skeoch would have no objection to this per se if it did not have the other adverse implications that he identified.

## 7. General Proposals

Dr. Skeoch stated that it was of fundamental importance that the means not conflict with the ends. In his view, about all one can do as a practical matter is to question whether there are not less interventionist and less restrictive practices which can be used to achieve a higher level of market effectiveness, particularly in the long run, and at the same time achieve the broad objects of the Canadian Dairy Commission Act as set out in Section 8. Dr. Skeoch would seek to introduce incentives and pressures to adapt, and to discontinue the use of any "direct-and-control" methods that might be used to support a form of security based on the inhibition of change.

In general, Dr. Skeoch said that the search should be for more simplified tools where you use decentralized market decision processes and then supplement them by other measures to establish reasonable stability in the market.

Dr. Skeoch did not in any sense suggest that the problem was an easy one, or that any failings by the Canadian Dairy Commission were somehow unique to it. It was in fact an extremely intractable problem requiring a sophisticated long-term perspective. Further, Dr. Skeoch said there was no painless formula or technique that would solve the problems of agricultural adjustment. The fact that the solutions were not

simple or clear-cut, however, did not lessen the fundamental importance of the long run perspective and the longer run programs that attempt to facilitate adjustment and change.

In Dr. Skeoch's view, as difficult and as complex as it might be to introduce a longer-run perspective into the regulation of Canadian agriculture, it would be less complicated than the existing policy programs in terms of figuring out their long-term consequences.

Dr. Skeoch was of opinion that agricultural policy must draw a balance between facilitating dynamic change and achieving a socially desired level of stability. Some sort of assistance to producers to reduce the short-run effects of severe fluctuations would be necessary. In fact he stated that for too long the agricultural sector of the economy at the producer level had been the forgotten sector, and had been left to take all the buffets of international fluctuations. It would cost something to build in an element of security for the producers, but that cost would be a good deal less than the loss which would and did heretofore occur to producers by leaving the producers to cope with unrestrained market forces.

By way of general critique of the policies of the Canadian Dairy Commission, Dr. Skeoch felt that it was clear that the objectives of Section 8 could be achieved with a much lower and less comprehensive level of intervention than has in fact been employed. In particular, he felt that the quota control and price support programs, and the cost-justification-based formula utilized by the Commission, were in "serious conflict" with the requirements of Section 8.

Dr. Skeoch therefore was of opinion that there is a need for government intervention in the Canadian dairy industry. This need results from the fact that there are a large number of producers, that the planning and production period is long, that there is a very substantial fluctuation in the cost side, and that on the production side, producers and sellers are frequently faced with an inelastic short-run demand on the part of buyers, with the result that there is a considerable likelihood of extreme price fluctuations. In such circumstances the individual can do relatively little to protect himself, and government intervention is required to eliminate the wasteful and inefficient effect of the extreme short-term fluctuations upon productive capacity, and on the ability of producers to perform effectively. Short-run stability, however, must not be achieved by methods that result in an inefficient industry from the longer run point of view.

In Dr. Skeoch's view it was not that the producers have lost the willingness to take risks and to adjust, but that the cost of change today is sometimes too great for the individual producer to bear unassisted. This is the source of the obligation upon the government to assist the producer in accommodating

change. The "trick" is to make this accommodation while in the longer run ensuring and preserving incentives and pressures.

In summary therefore Dr. Skeoch was of opinion that despite the nebulous formulation of the Canadian Dairy Commission's purposes and objects, the economic implications of its activities are considerable, particularly for consumers, for taxpayers and for producers. He was of opinion that it is imperative for bodies such as the Canadian Dairy Commission to have sophisticated and tough-minded policy leadership that will seek to maximize the play of market forces, to decentralize decision-making and to minimize the extent of centralist intervention, so far as is compatible with statutory responsibilities, in order to inspire over the long run the best delivery from the system as a whole at the best price. This advice relates to the general direction, or an attitude of mind, and is more basic and important than any particular suggestion or *modus operandi* that might be tested or implemented by the Canadian Dairy Commission.

Dr. Skeoch made some particular suggestions to illustrate his general comments, in addition to his opinion that it was important that the Canadian Dairy Commission avoid adopting formulae or setting targets or supports on a cost justification, or cost recovery, basis. His principal suggestion is that serious consideration should be given to eliminating the support prices for processed products such as skim milk powder and butter and, instead, to simply have a target price for producers for their industrial milk together with a direct subsidy to producers and that the subsidy be related to social considerations rather than directly to volume of production. Dr. Skeoch would eliminate the quotas for the production of industrial milk and he would use the direct subsidy to producers to the extent that it appeared necessary in order to push the producers towards the target price and to make up what the market failed to provide in terms of a socially acceptable family income level. His suggestion was that the target price be adjusted over time if necessary in order to achieve greater or lesser total production, the timing of the adjustments to take account of the planning and production period involved in dairy production.

Dr. Skeoch was of opinion that there would have to be a transition period if quotas were to be eliminated, in order not to be unreasonable with respect to the investment that people had made in quotas. Public policy, after all, instituted the quota system, and the producers should be given a period of time to work off the costs and the various investments they have undertaken in relation thereto. Dr. Skeoch suggested as one possibility that some system of quotas, gradually diminishing over a period of, say, five to seven years, might be considered.

In Dr. Skeoch's view it is in the long-run interest of both the producers and the economy as a whole to adopt the perspective he recommended.

#### ***Evidence of Dr. S.C. Barry***

Dr. Barry stated that, in general terms, the way the Canadian Dairy Commission attempted to come to grips with the generalities of the objects set out in Section 8 during the years he was Chairman of the Canadian Dairy Commission was to adjust the target support price to the level where the Canadian Dairy Commission thought it would produce enough to meet what had been determined to be the national requirements.

With respect to the concepts of "efficient producers" and "fair return", Dr. Barry stated as follows:

"Basically I suppose the measure of efficiency is whether a given producer is capable of operating under the price that has been established as the basis of support. . . . the end result as to whether a given price brings out the product required I think demonstrates whether it is being done by efficient producers."

"... if the deliveries start to go down then obviously whether it is expressed as fair or expressed as productive is a matter I suppose that would make an indication of a need for adjustment. Basically we had a formula as I recall it relating to changes in prices, changes in target prices in relation to certain input costs which I suppose is the common practice used in many price negotiation matters."

Dr. Barry explained the nature of the support program that was implemented under the *Canadian Dairy Commission Act*, as has been referred to above. In terms of the tabular or graphic description of the support program (see this Report, Chapter III(B)1), Dr. Barry said that the process of setting the support price really began with an original calculation or estimation of what was required in order to maintain a level of production of dairy products that was determined to be the national requirement. Taking this, together with the target support price, the other calculations including that of the support price for butter and skim milk powder were made. The first decision made in terms of prices was the Canadian Dairy Commission target support price. He stated that "our fundamental purpose in establishing what we regarded as the final target support price was to set it at a level which would equate the total milk production with Canadian demand, Canadian needs."

#### ***Evidence of R.M. Cloutier***

Mr. Cloutier is the Director of Economic Studies section of the Canadian Dairy Commission, which

section gathers statistics that are used to forecast milk supply, forecast demand, estimate Canadian requirements and the size of market quota, and also calculates processing costs and so on. He said that these figures are used by the Canadian Dairy Commission, the Canadian Milk Supply Management Committee, and others.

Mr. Cloutier said that the Returns Adjustment Formula referred to earlier in this Report represents the Canadian Dairy Commission's attempt to identify efficiency and to provide the opportunity to efficient producers of obtaining a fair return for their labour and investment.

Mr. Cloutier regarded the Returns Adjustment Formula that was adopted in April 1975, and which has been used since, as "a successful experiment". (He also stated that in 1980 the Canadian Dairy Commission was undertaking a complete review of the Formula in order to determine whether in the judgement of the people associated with the Canadian Dairy Commission the Formula was achieving the objectives of Section 8 so far as the Canadian Dairy Commission was able to do so. The review and assessment of the Formula was being undertaken in consultation with the industry, with the Dairy Farmers of Canada and with different Departments of Agriculture across the country.)

Prior to 1975 the target price established for dairy farmers was established on the basis of annual consultations between the Federal Government and the Dairy Farmers of Canada. Following the consultations and the exchanges of information the Minister of Agriculture would make a decision as to whether to increase, decrease or alter the target price at that time.

As outlined in Chapter III, above, the 1975 formula was arrived at on the basis of consultations between the Dairy Farmers of Canada and the Canadian Dairy Commission. The basis of the formula was data and information obtained through an analysis of 125 farm account books from Quebec and Ontario for the years 1970, 1971 and 1972. From those account books were extracted figures relating to the cost of production per hundred weight of milk, and the costs were broken down into three components. The following summarizes what Mr. Cloutier said:

- (a) Cash cost — expenses which the dairy farmer has to disburse on a daily or weekly basis to keep his operation running.
- (b) Capital costs — investment requirements for different sizes of herds and levels of production (buildings, machinery, interest on money borrowed, etc.). In 1975 the costs of the quota were taken into

account as part of the costs of investment — it was determined that it cost \$2.20 per hundredweight of milk to maintain the investment on the farm.

- (c) Labour — rather than using the average of the farms sampled, a lower average was used, derived from the account books of farmers who were milking more than 17 cows. This average was .8 hours per hundredweight of milk. "... we wanted to price the milk to enable an efficient dairy farmer to make a fair return on his labour and investment." "That labour requirement was more likely to be the labour requirements of an efficient dairy farm rather than the overall average for the industry."

After determining the three cost components that go into the Formula, a base price was needed to which the Canadian Dairy Commission could have reference. On April 1, 1975, following negotiations between the Government and the Dairy Farmers of Canada, the Minister had announced a target price for industrial milk for the dairy year commencing at that time on April 1, 1975 — of \$11.02. He also announced that the price from then on would be indexed on the basis of the cost components. In fact it is not fully indexed. The cash cost (45% of the target price) is indexed on the basis of eleven items that were determined to be relevant, and another 35% of the target price is indexed to the consumer price index. The remaining 20% is left to Ministerial discretion. The formula or the indexation is reviewed every three months.

"... the target price announced by the federal government is an approximation of what... the federal government believes dairy farms should be receiving across Canada. From that point on the way milk prices are set... is... through negotiation by, between producers and processors for each product. What they do really is they use the price announced by the federal government as a target, as an objective which they should meet. What Mr. McLaughlin has said as well is that in Quebec and Ontario the producers achieve the target price... they price their milk in a way that they can obtain that target price."

In fact, Mr. Cloutier said, there is some evidence in Ontario and Quebec that in

fact dairy farmers can achieve a better price than the target price, whereas in western and eastern Canada, because of lower milk production, processors usually need more money to process milk on a per hundredweight basis than farmers in Ontario and Quebec.

"The price support program put in place by the Canadian Dairy Commission wouldn't normally enable processors to pay whatever we call the target returns from the marketplace."

"... as soon as [the dairy farmer] receives the world price for his milk, he simply quits delivering milk at that price. So, the fair return as far as the fair price, the target price, the fair return limit is very close to the overall target price announced."

Mr. Cloutier felt that the Canadian Dairy Commission had provided some pressure for efficiency by discounting the average labour cost when it was structured into the formula. He was further of the view that the tendency during the 1970's towards larger farms, and a decline of smaller dairy farms, was evidence that this bit of pressure in the formula was having some effect. It was on this basis and in this connection that he expressed the view that "technological progress is still registered" within the formula and "market pressures have not been totally at least eliminated from the Canadian dairy industry."

Mr. Cloutier stated that "... we would like to think that we can through research, through statistics, through samples at the farm, we can identify what efficiency is all about or at least come up with some definition of it..." In Mr. Cloutier's view the opportunity for efficient producers to earn a fair return was, in effect, being achieved if farmers will produce to their quota levels on the basis of the target price as determined.

Mr. Cloutier also said that in his view the fact that 20% of the target price remains unindexed and left to Ministerial discretion, means that certain economic incentives and pressures will thereby be brought to bear on the dairy industry.

Regarding the concept of "adequate supply", Mr. Cloutier stated that in determining the national requirements for industrial milk on an annual basis the Canadian Dairy Commission examines the records of production, stocks, exports, and so on, and seeks to determine whether the target support price will throw up what has been determined to be the national requirement. The Canadian Dairy Commission assumes the target price for this purpose, although apparently economists within the Department of Agriculture utilize econometric models for

testing various price assumptions. This was not elaborated upon.

Mr. Cloutier said that the Canadian Dairy Commission seeks to ensure "adequate supply" in conjunction with the provinces through the framework of the Canadian Milk Supply Management Committee. He testified that in 1973 and 1974 prices had to be increased several times "to maintain an adequate price level to farmers so that we could obtain the milk supply which... we needed to satisfy the consumers."

(In view of the intent of Parliament when it enacted the *Canadian Dairy Commission Act*, and in the light of Dr. Skeoch's opinion evidence, a number of points should be noted: It is apparent that Dr. Barry and Mr. Cloutier in the evidence restated the problem and their evidence did not constitute an analysis of the short and long-run dimensions of Canadian Dairy Commission policies and practices in relation to Section 8. Their evidence made it clear that the valuation of quotas constituted an important cost element, that quotas controlled the amount of domestic production, that imports were strictly regulated, that the processing and distribution sectors were substantially protected — hence that prices and output were jointly controlled and the resultant finished products were disposed of on the domestic market by subsidized exports, or carried over by storage programs. Apparently also no efficiency tests in relation to comparable foreign producers were undertaken, no actual experimentation in terms of consumer prices in the market, or price discrimination programs, no market discipline through imports, and so on, were engaged in as might minimally be expected to provide some assurance that production and distribution efficiency was achieved and the consumer interest was protected.) (It should be mentioned in connection with these comments that Mr. Cloutier testified that in 1980 a general assessment of the policies was being undertaken internally to seek to measure their impact and to consider any need for modifications.)

#### **Other Evidence**

It might also be appropriate here to note one of the concluding observations of a recent study conducted by Dr. R.M.A. Loyns of the Faculty of Agriculture of the University of Manitoba ("Farm to Food Prices", Economic Council of Canada, January 1980), a copy of which was marked in evidence as Exhibit 72:

"A number of alternatives exist for dealing with longer-term food price increases. One option is subsidized producer or consumer prices: the efforts to date illustrate that the costs of these efforts for achieving even modest and temporary benefits are enormous. A second option involves more regulation of farm prices and extension of controls into other components of the food chain. It is

difficult to be optimistic about this alternative in view of the growing experience during the past few years. The other major alternative is to sharpen competitive forces, strive to improve productivity, and work to reduce structural rigidities in the entire food system. This option will not achieve price stability, but it will assure that in the long-term, food prices are as low as conditions permit and that the Canadian food industry is as productive as our resource base allows."

Dr. Loyns estimated that Federal Government support payments to producers of industrial milk during the 1977-78 dairy year approximated an average \$9,500 per farmer.

#### **Accountability**

Dr. Skeoch testified with respect to the need for some institutional mechanism whereby the Canadian Dairy Commission would be obliged to account publicly for the policies it had adopted and their long-run effects. This aspect of accountability must be distinguished from financial accountability, which is an aspect handled by the Auditor General of Canada, and from accountability for conduct in the administration of policy, which concerns such things as whether personal discrimination took place against, for example, Schafer Bros. Ltd. The subject of Dr. Skeoch's principal interest with respect to accountability was, as he put it:

"... economic accountability in the sense that it is used in industrial organization analysis. In other words, the requirement is efficient producers, fair return, adequate supply and these are the sorts of issues that I consider to be the ones that require accounting for. In other words, has the Commission assured the efficiency of the producer, has assured the fairness of the return, has assured the adequacy of the supply?"

The normal way in which economic accountability is ensured is through the operation of an open market economy. However, as stated by Dr. Skeoch, "where comprehensive government controls are imposed on the market... the longer-run requirements of accountability render the suppression of market signals related to dynamic change a very serious matter for the industry and the economy..."

An additional special concern regarding economic accountability arises with respect to government agencies such as the Canadian Dairy Commission who have extensive power and influence on both the buying and selling sides of certain markets, such as those for skim milk powder. The risk is that a person in such a position can obscure certain market signals and use its power on the selling side of the market to

validate its decisions on the buying side of the market:

"...if you are both a monopsonist and monopolist, you can settle both sides of the equation, both the supply and the demand side and you cannot say that that is a response to market pressures. That is a response to a determination made by the administrators as to how much will be allowed to be produced, how much will be allowed to be imported and so on and the net outcome of that, I don't see how anybody can say it is fair or adequate. I couldn't say. I always say there is one way to try it. Let's try to open it up to some sort of competition." (Dr. Skeoch — Transcript p. 348)

To say that there is a need for some mechanism to ensure accountability is not to say that there are obvious and widely-accepted mechanisms which can be prescribed. Indeed, as pointed out by Dr. Skeoch, there is inevitably a conflict between flexibility and accountability; very strict accountability requirements could only be imposed at the cost of reducing scope for experimentation and for trying things out. It is a matter of compromise, taking into account the long-run and experimental nature of some of the programs that should be attempted. Essentially, in addition to periodic policy assessments and review, there should be an attempt to seek to create pressures or incentives through the price structure to encourage producers to adopt economies by way of new technology, new organizational methods, and so on.

Dr. Skeoch had no objection in principle to what he called "third-degree price discrimination", which refers to the separation of submarkets for the purpose of different price structures. The evidence showed different price structures to exist as between export and domestic submarkets, and as between animal feed and human consumption applications. However, Dr. Skeoch was disturbed over the fact that there was no apparent basis provided by the Canadian Dairy Commission upon which anyone could assess its price discrimination programs in terms of achieving the public policy goals for producers or those for consumers. Certainly no evidence was given by the Canadian Dairy Commission regarding the basis upon which it undertakes its price discrimination programs. Could the price in the domestic market be lowered by selling more of the skim milk powder in the domestic market? Dr. Skeoch stated that with a properly based third-degree price discrimination program the marginal return, which should be equal to the marginal cost, should be the same in all submarkets. Although the price would differ in each of the submarkets according to the elasticity of demand in each, the marginal revenue should be the same.

As indicated above, Dr. Skeoch was emphatic in his view that a cost justification basis for prices and returns is in no sense a defensible standard of accountability, because it insulates people from market pressures and is inconsistent with dynamic change.

Dr. Barry testified that the basic mechanisms for requiring the Canadian Dairy Commission to answer as to its policies were the need to defend to the government its total estimates for expenditures, including any proposals to change the amount of the direct producer subsidy, and appearances before the Agriculture Committee of the House of Commons to answer questions regarding dairy policy. The Minister or Deputy Minister would, further, be advised regarding "any major change of policy", and apart from that there are various consultations that take place with departmental officials.

It is difficult to know just how effective the existing mechanisms are for accountability for broad policies in the terms discussed by Dr. Skeoch. *Report of the Auditor General of Canada to the House of Commons, Fiscal Year Ended March 31, 1979, Chapter 8 "Control and Accountability of Crown Corporations"* Dr. Barry stated that he could not recall ever receiving a directive as such from the Minister or the Governor in Council pursuant to the provisions of Section 11 of the Act, nor could he recall any recommendation by the Canadian Dairy Commission as to the level of the support price ever having been turned down by the Minister or the Cabinet. These facts may have little real significance in terms of effective accountability. Dr. Barry could not, however, recall any initiative having been taken by the Minister to consult with him or with members of the Canadian Dairy Commission on matters of export policy.

Dr. Barry said he found his discussions with the Consultative Committee to be very useful with respect to broad changes in the operations of the Canadian Dairy Commission, which during his tenure as Chairman were generally reviewed with the Committee.

As to another aspect of accountability mentioned above, namely, accountability for conduct in the administration of policy, Dr. Barry was asked what assurance, if any, a particular trader would have that he was being treated as favourably by the Canadian Dairy Commission as were his competitors, either with reference to the same potential business or in general terms. Dr. Barry answered that apart from an element of trust in the intelligence and integrity of the individuals in charge of the Canadian Dairy Commission, there was no assurance. There was no institutional mechanism that could give the trader the assurance that he was being treated fairly, and if he had a complaint his remedy was to complain to the Canadian Dairy Commission "or to take it a further step if they wished".



## CHAPTER V

### THE CLAIM FOR COMPENSATION

It is necessary to establish the nature of the claim of Schafer Bros. Ltd. in order to determine if it is well founded.

#### NATURE OF CLAIM

Schafer Bros. Ltd. claims compensation not only for the loss of the Mexican market, which it asserts the Canadian Dairy Commission took over in 1971, but also for damages suffered on account of irregular behaviour of the Canadian Dairy Commission, its officers and employees in 1969, 1970 and 1971.

##### 1. *Loss of Mexican Market*

Schafer Bros. Ltd. by its officer David Schafer, believes that it, alone and single-handedly, created and developed the Mexican market for Canadian skim milk powder. It believes it achieved that result by investing over a long period of time much money, time and effort to develop a unique relationship with CONASUPO officials.

David Schafer said he had been led to believe by CONASUPO officials in January 1968 that if Schafer Bros. Ltd. could offer a price in the 8¢ to 9¢ per pound range, it would get the 25,000 ton sale for which CONASUPO was inviting tenders.

Schafer Bros. Ltd. alleges that the Canadian Dairy Commission, without warning and despite the fact that it had encouraged it to develop the Mexican market, took away the market by diverting the business to itself and to others in the various ways set out in the allegations.

Schafer Bros. Ltd., by its two officers, David Schafer and George Schafer, says that its main business interest was thereby "expropriated" and that it was deprived of its main prospective source of business income without having the change to recoup its capital invested in developing this Mexican market, claimed by it to be about \$500,000.

Details of the genesis of the claims of Schafer Bros. Ltd., which commenced being made in 1969, are now set out. The purpose in doing so is to enable one to appreciate what the officers of Schafer Bros. Ltd. said at the material times, how the nature of these claims evolved and, generally, the essence of the claims of Schafer Bros. Ltd.:

- a) A claim for compensation was made by George Schafer, with reference to the

January 1968 tender, in the winter of 1969. George Schafer claimed that Schafer Bros. Ltd. lost \$40,000 when the 1968 CONASUPO contract was awarded to Commercial Credit Corporation of the United States and that Schafer Bros. Ltd. was not compensated, and suggested that "... it would only be just that only we should be the only Canadian firm to conclude the business with the Mexicans." (letter from George Schafer to the Honourable J.L. Pépin, January 17, 1969, Exhibit 12, p. 272, [in French] and to the Honourable H.A. Olson, January 29, 1969, Exhibit 12, pp. 290-292).

- b) On February 19, 1969, David Schafer wrote to the Honourable H.A. Olson, the Minister of Agriculture, (Exhibit 12, Vol. 2, p.p. 332-4) stating that "To us, the loss of the business last year has caused and is causing us severe hardships. As we were the only private firm in Canada invited to offer last year until we had been prevented by the C.D.C. from satisfying this customer, I expected that a way would be found to help us get the business we lost because of the C.D.C.: That we should be the only ones from Canada to offer to Mexico this year."
- c) On May 17, 1971, David Schafer wrote to the Honourable H.A. Olson indicating that Schafer Bros. Ltd. had been rendered "impotent" by the Canadian Dairy Commission's refusal to make an offer to it for the 1968 tender and had received no compensation for its failure to obtain the large 1969 contract for sale to CONASUPO, which was obtained by Ronald A. Chisholm Ltd. and Thomas P. Gonzalez Inc., and claiming that it had been misled by the Canadian Dairy Commission (Exhibit 12, pp. 597-598).
- d) George Schafer wrote to the Honourable H.A. Olson on June 28, 1971, stating that..."If we don't have the Mexican business, our firm has little chance for survival till the end of this year, having been weakened by the C.D.C., by inflation, tight money, high interest rates, and other hardships..." (Exhibit 12, p. 625)
- e) George Schafer wrote to the office of the Prime Minister on September 24, 1971, asking for compensation: "... we ask that we receive a reasonable normal commission of 2% after all the milk powder the C.D.C. sold direct to CONASUPO." (Exhibit 12, p. 657)

- f) David Schafer wrote to the Honourable H.A. Olson on December 16, 1971, asking for compensation for the loss of the Mexican export market (as had George Schafer when he wrote on September 24, 1971) requesting

"... a reasonable, normal commission of 2% after all the milk powder the C.D.C. sold direct to CONASUPO, Mexico." (Exhibit 12, p. 799)

- g) David Schafer also requested that: "the C.D.C. be prohibited to enter into any export sales agreement" (Exhibit 12, p. 675).
- h) In February 1973, Schafer Bros. Ltd. wrote to Dr. Barry stating that it lost more than \$500,000 as a result of the taking of its main markets and asked for his help to obtain some kind of compensation. (Exhibit 12, p. 807)
- i) On November 7, 1973, George Schafer wrote to the Honourable Eugene Whelen stating that Schafer Bros. Ltd. lost its business and all the capital it invested (\$500,000) and claiming 2% on all sales of Canadian skim milk powder to CONASUPO (Exhibit 12, p. 865)
- j) On November 23, 1973, George Schafer wrote to the Prime Minister asserting that between 1968 and 1972 Schafer Bros. Ltd. lost 95% of its sales and its capital investment of \$500,000, and stated that it had not received any compensation. (Exhibit 12, pp. 866-867)

In his letter to Gilles Choquette, then Chairman of the Canadian Dairy Commission on July 25, 1977, Michel Choquette summarized the claim of Schafer Bros. Ltd. for compensation.

In testimony at the hearing of this Inquiry George Schafer further stated that punitive damages should be assessed against the Canadian Dairy Commission (Transcript, p. 2357).

In order to understand the perception of Schafer Bros. Ltd. of its interest in the Mexican market, it is useful to keep in mind not only its philosophy regarding the creation of exclusionary rights to markets, but also its understanding of the Canadian Dairy Commission's proper role with respect to the export marketing of skim milk powder. According to Schafer Bros. Ltd., it developed the Mexican market for Canadian skim milk powder, and therefore had a monopolistic right to deal exclusively with CONASUPO that could not lawfully or fairly be taken away from it as long as CONASUPO was purchasing skim milk powder from Canada (Tran-

script pages 2350, 2354, 2358). In addition, in its view, the Canadian Dairy Commission ought not to compete with private traders, but instead had the duty to do everything possible to assist private traders in developing and maintaining any foreign markets, such as the foreign markets for Canadian skim milk powder.

This appears to be the basis for the claim by Schafer Bros. Ltd. for a commission in the order of two percent on all sales of Canadian skim milk powder made by Canadian traders or by the Canadian Dairy Commission to CONASUPO from 1968 to such time as Schafer Bros. Ltd. decided it did not want this business.

In this respect, when David Schafer first ascertained at the hearings of this Inquiry that other private Canadian traders had been selling Canadian skim milk powder to CONASUPO even earlier than 1968 and during the period 1968, 1969 and 1970, David Schafer informed this Commission of Inquiry that Schafer Bros. Ltd. in the future would be prepared to share its exclusive rights to the Mexican business and the right to commission on all sales to CONASUPO with the private traders that he had ascertained from the evidence had been selling Canadian skim milk powder to CONASUPO at least by 1968, namely Ronald A. Chisholm Ltd., Eastern Townships Produce Ltd. and Granby Co-op.

David Schafer, in his evidence, asserted that Schafer Bros. Ltd. is claiming the alleged losses and costs described in the document marked as Exhibit 6, Vol 9, Section G. Essentially, this document represents an estimate of the time spent by Schafer Bros. Ltd., to which is given a capital value, and also of its loss of profit based on the premise that Schafer Bros. Ltd. had the business during all the relevant period that was in fact carried out by the Canadian Dairy Commission and other private traders with CONASUPO. This document was prepared by Michel Choquette with the help of accountants and bookkeepers (Transcript, p. 987). An estimate is made of the Schafers' salaries and office expenses claimed to be attributable to the effort expended to obtain the CONASUPO business. In this document, according to Schafer Bros. Ltd., a two percent commission is conservative, and its counsel, in relation to this, in his written argument submitted that the Canadian Dairy Commission pays its agents between three percent and five percent.

## **2. Other Unlawful or Unfair Behaviour**

Schafer Bros. Ltd., by its officers, says it believes that the Canadian Dairy Commission, in the course of taking away the CONASUPO market, engaged in other unlawful or unfair behaviour that caused damage to Schafer Bros. Ltd. Particularly, it alleges that:

- a) In January 1968 the Canadian Dairy Commission misused information given to it by Schafer Bros. Ltd. in order to compete with Schafer Bros. Ltd., unexpectedly withdrew its support, and was responsible for the loss of the sale to CONASUPO obtained by Commercial Credit Corporation of the United States.
- b) Between January and March 1969, the Canadian Dairy Commission provided Schafer Bros. Ltd. with false information regarding supplies, caused it to be late in its deliveries to CONASUPO, and seriously compromised its efforts to demonstrate its capabilities to carry out any contract to CONASUPO, something that was important in view of the large 25,000 ton invitation to tender to supply that CONASUPO was going to issue in the then near future.
- c) In March 1969, Dr. S.C. Barry misled David Schafer regarding the circumstances under which a trader would be entitled to the payment of the subsidy and was thereby responsible for the loss of the sale to CONASUPO subsequently made by Ronald A. Chisholm Ltd. and Thomas P. Gonzalez Inc.
- d) The Canadian Dairy Commission gave favoured treatment to competitors of Schafer Bros. Ltd. viz. the August 1968 so-called Consortium sale prevented Schafer Bros. Ltd. from making sales, the Canadian Dairy Commission recommended competitors of Schafer Bros. Ltd. when inquiries

were made by foreign traders in respect to possible business; and some inside information was given to Ronald A. Chisholm Ltd. and Thomas P. Gonzalez Inc. which enabled them to outbid Schafer Bros. Ltd. and obtain the 1969 and 1970 sales to CONASUPO.

- e) The problems that the Canadian Dairy Commission created for Schafer Bros. Ltd. by its irregular behaviour resulted in a significant loss of reputation which, together with its loss of "capital", prevented it from obtaining financial backing from loan institutions.
- f) In order to demonstrate the nature of the irregular behaviour and the negative attitude of the Canadian Dairy Commission regarding Schafer Bros. Ltd., the Schafers also allege various instances of lack of cooperation from the Canadian Dairy Commission.

Michel Choquette, for Schafer Bros. Ltd., stated that it does not make "either a moral or legal claim" for compensation regarding sales or potential sales to Cuba or to the Philippines.

As to the CONASUPO market, Michel Choquette asserted that Schafer Bros. Ltd. had a good legal claim based on "criminal, civil and administrative law"; he stated, however, that Schafer Bros. Ltd. felt that "the whole matter should be approached on a moral basis rather than a legal one" and that Schafer Bros. Ltd. requested an *ex gratia* payment of compensation.

## CHAPTER VI

### THE ALLEGATIONS: FACTUAL DETERMINATIONS

The Statement of Allegations as distilled from the pre-Inquiry writings of Mr. Michel Choquette and as amended at the outset of the public hearings at the request of counsel for Schafer Bros. Ltd. and Michel Choquette, was marked as Exhibit 20 and is reproduced in full as Appendix 5 to this Report.

The Statement of Allegations is divided into Parts I and II.

Part I of the Statement of Allegations consists of a number of separate allegations which, it is alleged by Schafer Bros. Ltd. and Michel Choquette, form a factual basis for the fundamental allegation that "the Canadian Dairy Commission, its officers and employees acted unlawfully or unfairly during the years 1966 to 1977 in their dealings with Schafer Bros. Ltd. relating to the export from Canada of skim milk powder". Part I is segmented into Section "A", which contains the allegations referring to specific events, and Section "B", which contains the allegations amounting to more general complaints about Canadian Dairy Commission policies or the lack thereof.

In this Chapter of the Report there will be determinations made of the factual questions raised in Sections "A" and "B" of Part I of the Statement of Allegations. In Chapter VII will be considered the basic question as to whether, on the facts as found, the Canadian Dairy Commission, its officers or employees acted unlawfully or unfairly during the years 1966 to 1977 in their dealings with Schafer Bros. Ltd. relating to the export from Canada of skim milk powder.

Part II of the Statement of Allegations consists simply of the allegation that as a result of the conduct referred to in Part I, Schafer Bros. Ltd. suffered losses and is entitled to be compensated for those losses. This is considered and determined in Chapters VI and VII.

#### 1. *Allegation A.1(a)*

Allegation A.1(a) consists of a general allegation and two subsidiary allegations of fact. The general part of the allegation is as follows:

"The C.D.C. excluded Schafer Bros. Ltd. from the business of supplying Canadian skim milk powder to CONASUPO (a Mexican agency), and diverted business oppor-

tunities with CONASUPO to itself and to others..."

The key words in this Allegation are "excluded" and "diverted".

The means by which the Canadian Dairy Commission is alleged to have "excluded" Schafer Bros. Ltd. are, with one exception, the subject of other more specific allegations and are dealt with below, namely,

- (a) That in January 1968 the Canadian Dairy Commission refused to supply skim milk powder to Schafer Bros. Ltd. in connection with a tender call by CONASUPO, while at the same time bidding itself (see for this Allegation A.2, below) and subsequently in 1968 supplying a large volume of skim milk powder at very low prices to a consortium for the purpose of export sales (see for this Allegation A.3, below);
- (b) That in early 1969 the Canadian Dairy Commission acted and failed to act in such manner as to make it unnecessarily difficult for Schafer Bros. Ltd. to fill its first (and only) contract for the sale of skim milk powder to CONASUPO (see for this Allegation A.4, below);
- (c) That subsequently in the spring of 1969 the Canadian Dairy Commission acted and failed to act in such manner as to prevent Schafer Bros. Ltd. from winning a contract to supply 25,000 tons of skim milk powder to CONASUPO (see for this Allegation A.5, below);
- (d) That "irregular behaviour" on the part of senior officials of the Canadian Dairy Commission caused Schafer Bros. Ltd. to lose out to a competitor on prospective sales to CONASUPO in 1969, 1970 and 1971 (see for this Allegation A.6, below);
- (e) That in 1971 the Canadian Dairy Commission frustrated a maturing business opportunity for Schafer Bros. Ltd. to structure a combination wheat/powder deal with Mexico by selling a large quantity of skim milk powder to CONASUPO (see for this Allegation A.7, below);
- (f) That in 1971 the Canadian Dairy Commission discontinued the subsidy on the export sales of skim powder to CONASUPO (see for this Allegation A.1(b)(vi), below); and
- (g) That in 1977 the Canadian Dairy Commission appointed Ault Foods (1975) Ltd. as its marketing agent to sell skim milk powder to CONASUPO (see for this Allegations B.5 and part of B.8, below).

It should be noted that (a) to (e) above apply to Schafer Bros. Ltd. alone, whereas items (f) and (g) apply equally to all private exporters of skim milk powder.

One other allegation of exclusion, the one exception referred to above, is dealt with in the argument of counsel for Schafer Bros. Ltd. submitted after the conclusion of the evidence. Counsel's argument refers to rumours that were allegedly circulated about Schafer Bros. Ltd. by the Canadian Dairy Commission, the truth of which is denied by Schafer Bros. Ltd. Counsel's submission was that the rumours were that Schafer Bros. Ltd. had not contributed to the development of the CONASUPO market, that Schafer Bros. Ltd. had no experience in exporting skim milk powder, and that Schafer Bros. Ltd. was linked to skim milk powder smuggling operations in Northern Mexico.

As to these rumours, the sole evidence before the Commission is a November 1974 internal memorandum by a Department of Agriculture legal advisor repeating some comments apparently made to him, privately, by Mr. Sherk, a marketing official of the Canadian Dairy Commission. There is no evidence that the internal memorandum or the comments had any general circulation, nor that the rumours referred to in the memorandum in any event were conveyed or known to any person in authority to make decisions in the Canadian Dairy Commission. There is no evidence of any decisions having been influenced in the slightest way by the rumours. As a result, the fact that this internal memorandum records some rumours proves nothing.

The means by which the Canadian Dairy Commission is alleged to have "diverted" business opportunities are, likewise, the subject of other more specific allegations, and are dealt with below, namely,

- (a) That the Canadian Dairy Commission used information supplied to it from time to time by Schafer Bros. Ltd., which information had been obtained by Schafer Bros. Ltd. in the course of making its promotional efforts and investment in Mexico (see for this Allegation A.1(b)(i), below);
- (b) That the Canadian Dairy Commission bid directly to supply skim milk powder to CONASUPO in January 1968, thereby attempting to divert to itself this business opportunity, and that at the same time the Canadian Dairy Commission prevented Schafer Bros. Ltd. from taking advantage of the first opportunity to make a major sale of Canadian skim milk powder to CONASUPO by refusing to supply Schafer Bros. Ltd. with skim milk powder (see for this Allegation A.2(a) and (d), below);
- (c) That in May 1969 the Canadian Dairy Commission attempted to enter a contract with CONASUPO to sell it 25,000 tons of skim milk powder (see for this Allegation A.5(c), below), and that the sale was actually diverted to

Ronald A. Chisholm Ltd. and Thomas P. Gonzalez (see for this Allegation A.5(a), below);

- (d) That a business opportunity to sell 7,000 tons of skim milk powder to CONASUPO in 1970 was diverted to Ronald A. Chisholm Ltd. (see for this Allegation A.6, below);
- (e) That a full-scale diversion to the Canadian Dairy Commission of business opportunities for the sale of Canadian skim milk powder to CONASUPO occurred in and after 1971 by virtue of the Canadian Dairy Commission's discontinuance of the payment of subsidy on the export sale of skim milk powder to CONASUPO (see for this Allegation A.1(b) (vi), below);
- (f) That the exclusion of Schafer Bros. Ltd. and all other private exporters, except Ault Foods (1975) Ltd., from the opportunity to deal with CONASUPO in the sale of Canadian skim milk powder resulted from the appointment by Canadian Dairy Commission in 1977 of Ault Foods (1975) Ltd. as the Canadian Dairy Commission's marketing agent for the sale of skim milk powder to CONASUPO (see for this Allegation B.5 and part of Allegation B.8, below).

As noted, most of the above referred to categories of alleged exclusion by the Canadian Dairy Commission of Schafer Bros. Ltd. from the business of supplying Canadian skim milk powder to CONASUPO, and of diverting business opportunities with CONASUPO to itself and others, are the subject of specific allegations in respect to which determinations will be made later in this Report. As a consequence it is not necessary to do so under this general Allegation. It is sufficient here to make only certain general observations. Schafer Bros. Ltd. and its officers were in error, as was their counsel, in their allegation and submissions that it was necessary for a private exporter of Canadian skim milk powder, for a sale to CONASUPO or any other foreign buyer, to obtain the product for such sales from the inventory of the Canadian Dairy Commission, failing which such private exporter would not obtain the payment of the export subsidy on such sales.

The only thing that is true is that the Canadian Dairy Commission usually had, for the most part, a substantial inventory of skim milk powder because it bought it from the private sector under its standing offer to purchase, or price support program. But it is not true to say that a private exporter could not obtain skim milk powder for sale in the export market from Canadian sources in the private sector. The evidence discloses that certain private exporters who did sell to CONASUPO and other foreign purchasers, during the relevant years, obtained the inventory for such sales from sources other than Canadian Dairy Commission inventory, often were in the busi-

ness of manufacturing skim milk powder themselves and were also on familiar business terms with others in the trade who manufactured skim milk powder. Schafer Bros. Ltd. was not engaged in the manufacture of skim milk powder.

In this connection it should be noted that in order to complete its shipments of skim milk powder to CONASUPO under its contract with CONASUPO entered into in January, 1969, for 770 tons, Schafer Bros. Ltd. sourced some of the skim milk powder from sources other than the inventory of the Canadian Dairy Commission and was paid on the total of the skim milk powder shipped a subsidy by the Canadian Dairy Commission pursuant to its normal subsidy program in place in 1969.

Speaking generally in this connection, from the whole of the evidence it is apparent that no trader was under any misapprehension during any of the relevant years that a trader had to obtain the skim milk powder for any export sale from the Canadian Dairy Commission, failing which it would not receive a subsidy. A possible exception is the request for tenders to purchase the skim milk powder inventory then on hand at the Canadian Dairy Commission which was the subject of the Canadian Dairy Commission circular dated January 29, 1968 (see Document 185, Exhibit 12). This circular appears to have resulted in the so-called "consortium sale" of 35,000 tons of skim milk powder at 4¢ by the Canadian Dairy Commission in August, 1968. This sale will be referred to later in this Report. Briefly, it was a sale of old stock of skim milk powder to Eastern Townships Produce Ltd., who in turn resold it to a Consortium in Europe for further resale outside the western hemisphere.

## 2. Allegation A.1(a)(i)

Allegation A.1(a)(i), one of the subsidiary allegations of fact to the general allegation just dealt with, is as follows:

"The interest of CONASUPO in Canadian skim milk powder resulted substantially from promotional efforts made and expense incurred by Schafer Bros. Ltd."

The word "substantially" was added at the request of counsel for Schafer Bros. Ltd. to this allegation as originally drafted by Commission counsel. In Michel Choquette's pre-Inquiry writings it was expressly asserted that Schafer Bros. Ltd. created "single-handedly" Canada's two largest export markets for surplus skim milk powder — Cuba and Mexico. I granted the request to add the word "substantially".

This allegation turns on the source or sources of CONASUPO's knowledge of and interest in Canadian skim milk powder.

The evidence disclosed:

- (a) David Schafer did not know of other Canadian traders in Mexico. Messrs. Rodriguez Ayala and Rodriguez Licea advised David Schafer, and said in evidence statements, that Schafer Bros. Ltd. was the only serious Canadian trader in Mexico with respect to skim milk powder until about 1969. Mr. Rodriguez Licea, the Purchasing Manager of CONASUPO from 1962 to 1970, said in his evidence statement that: "To the best of my knowledge, Mr. Schafer was the first Canadian trader in milk powder who took the time and trouble to visit us at CONASUPO, and throughout the years I was at CONASUPO, he was the only Canadian trader actively promoting Canadian milk powder here." Mr. Rodriguez Ayala, Assistant to the Sales Manager of CONASUPO from 1963 to 1970, in his written evidence statement said: "The company Schafer Bros. Ltd. was the first Canadian firm to make direct sales of skim milk powder to CONASUPO... this came about as a result of several visits made by Mr. David Schafer in the beginning of 1961 (first to the predecessor of CONASUPO, i.e. CEIMSA, and then to CONASUPO when it came into existence)... during this period and by means of these visits and correspondence, Schafer Bros. Ltd. became familiar with Mexican specifications and quality requirements for milk, and kept up to date regarding these... [I]n my personal opinion... it was the effort and work of Mr. David Schafer alone which brought Canadian powdered milk to the attention of CONASUPO and made it known in Mexico."
- (b) David Schafer said that he made several trips to Mexico for the purpose of selling skim milk powder, for other business reasons and for personal reasons. David Schafer said he first met officials of CONASUPO in January 1965.
- (c) Official Government statistics of both Canada and Mexico record that Canadian skim milk powder was sold to Mexico in the late 50's and in the 60's prior to 1968. The evidence of Messrs. Rocchi and Rodriguez Licea supports this. It was in January, 1968 that the Canadian Dairy Commission first made an offer to CONASUPO. David Schafer said that in January, 1968, for the first time he felt Schafer Bros. Ltd. had an extremely good chance of concluding a sale of skim milk powder to CONASUPO.
- (d) Other Canadian private traders, as for example Eastern Townships Produce Ltd. and Coopérative Agricole de Granby were attempting to sell Canadian skim milk powder to CONASUPO directly or through agents prior to 1968. Mr. P.

Pariseault of Granby Co-op stated that "from 1950 to 1953, we [Granby Co-op] sold regularly skim milk powder to Mexico; in fact, we were controlling, at the time, 70 percent of the private Mexican market. From 1953 to 1971, we [Granby Co-op] sold skim milk powder to the Mexican market, and more particularly, we sold 3 million pounds of skim milk powder in 1965 to CONASUPO."

Messrs. D. Curtis Bishop and Ronald D. Bishop, officers, directors and shareholders of Eastern Townships Produce Ltd., stated:

"ETP has made sales of Canadian manufactured products to: Argentina, Aruba, Bahamas, Belgium, Bermuda, Brazil, British Honduras, Canal Zone, Chile, Columbia, Cuba, Curacao, Denmark, Dominican Republic, Greece, Grenada, Guatemala, British Guiana, Holland, Honduras, Hong Kong, India, Iran, Iraq, Israel, Italy, Jamaica, Japan, Korea, Lebanon, Madagascar, Malaysia, Mexico, Nicaragua, Nigeria, Pakistan, Panama, Peru, Philippines, Rhodesia, St. Lucia, St. Vincent, El Salvador, Singapore, Spain, Sweden, Taiwan, Thailand, Trinidad, Union of South Africa, U.S.A., Venezuela.

In several of the above countries, ETP was (and is) represented by an appointed agent.

In Mexico, from 1961 to the present, ETP's agent has been Walter E. McAllister, Rio Lerma 339-2, Mexico 5, D.F. As ETP agent, Mr. McAllister maintained regular contact with private businesses, CEIMSA, and subsequently CONASUPO. Between 1961 and 1966, Dean R. Bishop personally visited CONASUPO in Mexico and met with Hector Rodriguez Licea, the purchasing manager of CONASUPO. Mr. McAllister and his wife were also present at this meeting. Dean R. Bishop has also met personally with Hank Gonzalez, former General Manager of CONASUPO."

Messrs. Brunet and Pariseault of Granby Co-op, and Messrs. Bishop of Eastern Townships Produce Ltd. were personally in Mexico dealing with Mexican government officials, and latterly CONASUPO, exploring the prospects of selling Canadian skim milk powder and other products.

From the interviews in Mexico City, particularly with Messrs Rodriguez Ayala, Rocchi and Arguelles, the above evidence was corroborated:

Several Canadian traders were in fact active in promoting the sale of Canadian skim milk powder to CONASUPO during the 1960's and in the course of

this promotion met with Messrs. Rodriguez Ayala and Rodriguez Licea in the Purchasing Department of CONASUPO. Mr. Benolol, a Mexican agent, was Granby's agent, and Mr. Walter E. McAllister was agent for Eastern Townships Produce Ltd. Some other Mexican agent represented Dominion Dry Milk Ltd., another Canadian company doing business with CONASUPO. Eastern Townships Produce Ltd. and Granby Co-op appear to have been more active than Schafer Bros. Ltd., and, in fact, the first sales of Canadian skim milk powder to CONASUPO were made by these companies. Mr. Rocchi stated that he introduced David Schafer of Schafer Bros. Ltd. to CONASUPO officials in 1965. Schafer Bros. Ltd. made their first and only sale to CONASUPO in 1969, 770 tons.

In addition, information was given that in the late 1960's, at approximately the time that CONASUPO's demand for foreign skim milk powder began to escalate, U.S. supply diminished substantially and the availability of skim milk powder from the U.S. to CONASUPO virtually ended, for a number of years, because of an incident or incidents involving the unauthorized re-sale of powder that was apparently supplied under an aid program.

- (e) In 1965 the Agricultural Stabilization Board began paying a small export subsidy on export sales of Canadian skim milk powder. This subsidy was increased by the Canadian Dairy Commission after it was established in 1966.

Until 1968 the major source of skim milk powder for the Mexican market was the United States. One of the principal reasons for this was no doubt the proximity of the two countries, resulting in low shipping costs.

A further factor that appears to have improved the prospects for the sale of Canadian skim milk powder to Mexico by 1969 was an alleviation of the concerns of CONASUPO officials regarding the bacteria count of skim milk powder in Canadian Dairy Commission stocks. Mexican officials were initially concerned about the high DMC count permitted by the Canadian Dairy Commission purchasing specifications, viz. 200 million, whereas CONASUPO limits were 75 million. In October 1967 Canadian Dairy Commission officials addressed themselves to this problem and advised the CONASUPO officials that there was no brucellosis or TB in Canadian cattle and that therefore a 200 million DMC count in Canadian powder was a tolerable limit for skim milk powder destined for human consumption.

In this latter connection, notwithstanding the efforts of Canadian Dairy Commission officials beginning in late 1967, CONASUPO insisted in January 1969 that for its purchase of 770 tons of

skim milk powder, the powder have only a 75 million DMC count.

It should be emphasized, as noted above, that this allegation relates to "the interest of CONASUPO in Canadian skim milk powder." The evidence clearly establishes that CONASUPO and its predecessor government agency CEIMSA were quite familiar with the fact that Canadian skim milk powder was being sold in the export market.

The only apparent equivocation in respect to this allegation is found in the witness statements of Mr. Rodriguez Ayala and Mr. Rodriguez Licea, but a careful reading of their statements and what they said indicates that their evidence does not relate to the point that is the subject of this allegation, viz. whether or not the interest of CONASUPO in Canadian skim milk powder resulted substantially from the promotional efforts made and expense incurred by Schafer Bros. Ltd. Instead, their evidence is directed to the more limited assertion that David Schafer was the only private Canadian trader who was personally active in trying to promote the sale of Canadian skim milk powder to CONASUPO. In so stating, Messrs. Rodriguez Ayala and Rodriguez Licea are not saying that other Canadian traders, such as Granby Co-op and Eastern Townships Produce Ltd., were not actively promoting the sale of Canadian skim milk powder to CONASUPO through their respective agents. What they are saying is that the other private Canadian traders, such as those mentioned and others, are not doing it directly, themselves, with CONASUPO.

From the above evidence and from all the other evidence, both oral and documentary, especially the evidence of David Schafer, Dr. Barry, Mr. T.A. Chisholm of Ronald A. Chisholm Ltd., Mr. Pariseault of Granby Co-op and Messrs. Bishop of Eastern Townships Produce Ltd., and the Mexican witnesses, this allegation is not supported by the evidence.

### 3. *Allegation A.1(a)(ii)*

Allegation A.1(a)(ii), the other subsidiary allegation to the general allegation of "exclusion" and "diversion", is as follows:

"The promotional efforts were made and the expense was incurred by Schafer Bros. Ltd. in reliance upon assurances by the C.D.C. to Schafer Bros. Ltd. that the C.D.C. would cooperate fully with Schafer Bros. Ltd. in the event that possibilities of sales to CONASUPO materialized."

The evidence in respect of this allegation, in the main, was as follows:

- (a) David Schafer said that he gave to Mr. D.B. Goodwillie, Director of Marketing of the Canadian Dairy Commission, and before that to officials of its predecessor, the Agricultural Stabilization Board, commencing October 1959, certain information, and that in return Mr. Goodwillie assured him that the Canadian Government would do anything it could to help David Schafer. David Schafer in his evidence statement put this matter as follows:

- "30. From this time [1959] onwards I communicated regularly with Mr. Goodwillie and other officials of the Agricultural Stabilization Board and subsequently the Canadian Dairy Commission, giving them all the information that I had obtained concerning the requirements of the various markets which I had been attempting to solicit, especially those of Mexico and Cuba. These officials, especially Mr. Goodwillie, always encouraged me to pursue my efforts in Latin America.
34. Throughout 1960, I kept in touch with Mr. Goodwillie of the Agricultural Stabilization Board and he indicated to me that he was keeping Mr. S. Clifford Barry, the Director General of Production and Marketing Branch informed of Schafer Bros. Ltd.'s activities. Mr. Goodwillie assured me that the Canadian Government would do everything to help me.
68. Throughout 1961, I kept Mr. Goodwillie informed of my activities in both Cuba and Mexico and he told me that he was keeping Mr. S. Clifford Barry and Mr. S.B. Williams, the Director General of the Production and Marketing Branch up to date. Before and after each trip to Cuba and Mexico, I met with or telephoned Mr. Goodwillie. I continued to do this until 1971....
84. Throughout 1962, I kept Mr. Goodwillie and other Canadian Government officials informed of my activities with respect to developing markets for Canadian milk powder in Cuba and in Mexico. Mr. Goodwillie continued to assure me that the Canadian Government would cooperate with me if a serious sale possibility ever presented itself.
91. Throughout 1963, I kept Mr. Goodwillie of the Agricultural Stabilization Board informed of my promotional efforts in Mexico, and he told me that Mr. Barry and Mr. S.B. Williams were being kept



advised. Mr. Goodwillie told me that I could count on his full cooperation concerning milk powder sales to Mexico.

97. Throughout 1964 I kept in close touch, as always, with Mr. Goodwillie at the Canadian Dairy Commission, and kept him informed of my attempts to break into the Mexican market in spite of stiff competition from the United States and other countries.
104. Throughout 1965, I gave Mr. Goodwillie full reports of my progress in Mexico and provided him with the list of names of the new officials at CONASUPO. He told me that he was passing on this information to both Mr. Barry and Mr. Williams, and he continued to assure me that the ASB would do everything to support my efforts to sell Canadian milk powder to Mexico.
113. During 1966, I kept Mr. Goodwillie, now Director of Marketing at the Canadian Dairy Commission, thoroughly informed, and Mr. Goodwillie assured me, as usual, that the Government would assist me in any way it could to sell milk powder in Mexico.
151. Throughout 1967, I kept Mr. Goodwillie informed of the sort of prices which CONASUPO was currently paying or willing to pay for milk powder, as well as the quantities it was likely to need in the near future and the quality requirements upon which it was now insisting. And Mr. Goodwillie told me to keep him informed of my progress."

Michel Choquette in his letter to Gilles Choquette dated July 25, 1977 put the matter this way:

"Although I am certain that it must be obvious by now that Mr. Whelan's conclusion is totally incorrect, I would like to stress once again the fact that throughout the 10 years which David Schafer devoted to developing his business relationship with CEIMSA and CONASUPO he was in constant touch with Mr. Goodwillie — first at the Agricultural Stabilization Board and later at the Dairy Commission. Before and after each trip to Mexico (and regularly between these trips) he wrote or otherwise communicated with Mr. Goodwillie to inform him of Schafer Bros.' intentions, to give him full and detailed progress reports, to provide him with the names of CONASUPO officials and advise him of any new appointments there, and to give him complete and up-to-date informa-

tion about the Mexican market situation. He discussed openly with Mr. Goodwillie the sort of prices which CONASUPO was willing to pay for milk powder, the quantities it was likely to need in the near future and the quality requirements upon which it was insisting."

Other than these statements by David Schafer and Michel Choquette there is no other oral or documentary support for the proposition. And Michel Choquette had no sources of information on the point other than David Schafer.

- (b) There was no evidence that Schafer Bros. Ltd. would not have discussed whatever it did discuss with Mr. Goodwillie at the Canadian Dairy Commission "but for" the assurances allegedly given by Mr. Goodwillie to David Schafer. In this connection, Schafer Bros. Ltd. was at all material times more inclined than other private exporters to depend upon government support in terms of information and sourcing. It was more central to its modus operandi to be speaking with Canadian Dairy Commission officials.
- (c) As to whether or not there was full cooperation by the Canadian Dairy Commission with Schafer Bros. Ltd. with respect to possibilities of sales to CONASUPO, there is at least no evidence of greater cooperation by Canadian Dairy Commission officials with any of Schafer Bros. Ltd.'s competitors. In this connection, it was suggested that Schafer Bros. Ltd. in fact received special cooperation not given to others in the financing of its January 1969 contract with CONASUPO, in that the Canadian Dairy Commission varied its announced policy and practice of requiring 2¢ per pound deposit against the promised subsidy before releasing its stocks. This was a minor matter, however. Other instances of a similar special cooperation by the Canadian Dairy Commission are its cooperation with Granby Co-op in its October 1967 pricing arrangement, its 1¢ per pound export guarantee in connection with its large 1968 sale to Eastern Townships Produce Ltd. for resale to the European Consortium, and in connection with a transaction with Dominion Dry Milk in November 1969. There was also insufficient evidence that the transfer of the Chilean Letter of Credit, to assist Schafer Bros. Ltd., was an unusual favour as argued in the so-called Joint Submission of the other parties recognized at this Commission.

From a consideration of all the evidence in respect to this Allegation, the finding is that this Allegation is not supported by the evidence. Any information given by Schafer Bros. Ltd. to Canadian Dairy Commission officials was given on a voluntary basis and any

assurances given by the Canadian Dairy Commission were of a general nature given to all traders. It may again be relevant here to note that it was important to Mr. David Schafer's philosophy of how to deal in this export market, to associate with and rely on government officials to a greater extent than other private traders in the market.

The co-operation that Canadian Dairy Commission officials gave to Schafer Bros. Ltd. cannot be categorized otherwise than as full cooperation, no different in any material way from that afforded to all other private traders.

In making this finding I do not suggest that the Canadian Dairy Commission should not have been more flexible in some of its policies vis-à-vis all private traders, as for example in the matter of its financial arrangements generally.

#### 4. *Allegation A.1(b)(i)*

Allegation A.1 (b) (i) is as follows:

"The C.D.C. used information supplied to it by Schafer Bros. Ltd. at the request of the C.D.C., which information had been obtained by Schafer Bros. Ltd. in the course of making its promotional efforts and investment."

As noted above, David Schafer stated that he supplied information to Mr. Goodwillie regularly, commencing in 1959, and that he received assurances from Mr. Goodwillie that the Canadian Dairy Commission would assist Schafer Bros. Ltd. as much as possible in making sales of skim milk powder to CONSAUPO. David Schafer said that he gave the information willingly and voluntarily.

As to specifics regarding the "information" given by David Schafer to Mr. Goodwillie, David Schafer said that it was not necessarily information that could not have been obtained elsewhere or later. He said that he gave specific tender information, and specific and general market intelligence to Mr. Goodwillie from time to time. Specifically, for example, he said that he was the first to learn that the United States would not be tendering on the large 1969 contract.

There is no evidence of any specific reliance by Canadian Dairy Commission officials on any information given them by the Schafers. Dr. Barry, Chairman of the Canadian Dairy Commission from 1966 to 1973, specifically rejected the assertion contained in Allegation A.1(b)(i).

The evidence is that all Canadian private traders exchanged information with Canadian Dairy Commission officials about all world markets in which they were interested, including the Mexican market.

There is, further, no evidence that any information supplied by Schafer Bros. Ltd. to Canadian Dairy Commission officials was used in any way against Schafer Bros. Ltd. There is only the statement of George Schafer that he suspected such was the case.

Dr. Barry testified that in his view the Canadian Dairy Commission ought not to use information of a trade secret nature, received in confidence from a trader, in a manner contrary to the interest of that trader, as for example to exclude the trader from a deal. Nowhere in the evidence of David Schafer does he say that he or Schafer Bros. Ltd. gave Canadian Dairy Commission officials any information of that type.

The finding in respect of this allegation is that whatever information Schafer Bros. Ltd. supplied to Canadian Dairy Commission officials was not information that was not otherwise available to it. It was information of a type that other private traders also from time to time communicated to Canadian Dairy Commission officials, and that Canadian Dairy Commission officials in turn exchanged with such private traders. It might colloquially be referred to as general street knowledge in the market. As a consequence, there is also no evidence that Canadian Dairy Commission officials used this information in any particular way, let alone to the detriment of Schafer Bros. Ltd.

#### 5. *Allegation A.1(b)(ii)*

Allegation A.1(b)(ii) is as follows:

"The C.D.C. took unfair advantage of its control over large stocks of Canadian skim milk powder and of its power to determine and grant export subsidies, and not so as to limit the generality of the foregoing, more specifically in that:

- (a) on April 26, 1968, the C.D.C. refused to provide 400 metric tons of high heat powder with a production date of 90 days or less, thereby causing Schafer Bros. Ltd. to be unable to be awarded a contract, and
- (b) on June 26, 1968, the C.D.C. refused to provide 330 metric tons of low heat powder, thereby causing Schafer Bros. Ltd. to be unable to be awarded a contract."

The only evidence touching on the general words of this allegation was that given by George Schafer (transcript pp. 2569-74) to the effect that Schafer Bros. Ltd. had no evidence that did not also relate to other, more specific, allegations, viz. Allegations A.2, A.3 and A.5.

The underlined portion of this allegation was added to the Statement at the specific request of counsel for Schafer Bros. Ltd. and Michel Choquette on January 14, 1980. Said counsel subsequently, however, in written form (see Exhibit 54) informed as follows:

"My clients have informed me that they have no evidence to support the following amended allegations, I.A.1(b)(ii)(a) and I.A.1-(b)(ii)(b)."

As a consequence there is no evidence to support this allegation.

#### 6. Allegation A.1(b)(iii)

Allegation A.1(b)(iii) is as follows:

"The C.D.C. falsely represented that CONASUPO insisted upon dealing directly with the C.D.C.; and in fact in 1967, the C.D.C. proposed a direct agency to agency agreement with CONASUPO and Mr. S.C. Barry, then Chairman of the C.D.C flew to Mexico in Oct. 1967 in order to negotiate such a direct agreement."

The main documents regarding the origin and rationale of the direct dealing between the Canadian Dairy Commission and CONASUPO appear in Exhibits 12 and 12A at pages 94-97, 103-104, 126-134, 138-139, 149, 464, 1739, 606-609 and 1740.

The main oral testimony was given by David Schafer and Dr. Barry, and also in the course of the interviews held in Mexico City. David Schafer had no personal knowledge; his evidence consisted of inferences or suspicions he had drawn from certain documents and conclusions he drew from conversations with certain Mexican persons.

The evidence in essence is as follows:

- (a) Commencing apparently with the election of the new government in Mexico in the mid-1960's, Mexico became increasingly interested in making its government purchases on a direct government-to-government basis. This general policy affected a wide range of agencies and products including CONASUPO and its purchases of skim milk powder, and extended to all supplying countries including Canada. It appears to have arisen from an interest in ensuring a reliable supplier and obtaining the best possible price. (It further appears that although until 1971 Mexico had no wish to exclude the private sector in Canada from attempting to sell to it, the policy of direct government-to-government dealing became so important to Mexico with its new government in 1971 that, as was stated by one of the persons interviewed in Mexico City, if the Canadian Dairy Commission had insisted on selling skim milk powder only to private exporters for resale, and had not been willing to sell direct to CONASUPO, CONASUPO would have declined to buy Canadian skim milk powder).
- (b) By 1967, the first full year of operation of the Canadian Dairy Commission, Canadian skim milk powder surpluses had risen to uncomfortable levels. The Canadian Dairy Commission was concerned about the effectiveness of the private sector, acting alone, in selling those surpluses abroad. The potential significance to Canada of the escalating Mexican demand for skim milk powder was also becoming known.
- (c) In August, 1967, the Haitian Ambassador to Canada advised Mr. S.B. Williams, then Deputy Minister of the Department of Agriculture, that a Mr. Peniche, who was a CONASUPO official responsible for quality standards, wished to contact Canadian authorities regarding skim milk powder.
- (d) On September 22, 1967, Mr. Rodriguez Licea of CONASUPO advised Canadian government officials that he would like to visit Canada to explore the possibility of purchasing Canadian skim milk powder, specifically in respect to an imminent order of 20,000 tons. In this connection, Canadian Dairy Commission officials indicated by internal government memorandum that they did not wish the CONASUPO representatives to visit private sector representatives in Canada. They wished to have the visits paid for out of the Canadian Dairy Commission's budget and not out of the budget of the Department of Industry, Trade and Commerce because if it were paid out the latter, private sector representatives would have to be invited to visit with the CONASUPO officials.
- (e) In October, 1967, Dr. Barry and Mr. Goodwillie of the Canadian Dairy Commission visited CONASUPO in Mexico. Dr. Barry testified that "... we told CONASUPO that if they wished to deal directly we would be prepared to do so."
- (f) In January, 1968, the Canadian Dairy Commission bid directly to CONASUPO on its large call for tenders, having been invited by CONASUPO to make such a bid. The bid was not successful, nor was another bid made by the Canadian Dairy Commission to CONASUPO in 1969. The Canadian Dairy Commission did not in fact make a sale of skim milk powder to CONASUPO until 1971, when CONASUPO insisted on dealing exclusively with the Canadian Dairy Commission for its supplies of skim milk powder from Canada.

It is fruitless in the circumstances to seek to identify the source of the first initiatives in establishing direct contact between CONASUPO and the Canadian Dairy Commission. CONASUPO's growing interest in direct government-to-government dealing coincided with a growing concern by the Canadian Dairy Commission over how to ensure maximum export sales of the surplus skim milk powder and thereby to reduce the cost of the price support program.

It is true that Canadian Dairy Commission officials took some pains to convince other, sometimes sceptical, Canadian Government officials that the initiative for direct dealing had come from CONASUPO and that CONASUPO insisted on such. It also appears that the Canadian Dairy Commission hoped at the time that it would become the sole Canadian vendor of Canadian skim milk powder to CONASUPO. These communications and hopes can be questioned, but they were without material consequence so far as Schafer Bros. Ltd. and other private Canadian traders were concerned. It is clear that the Canadian Dairy Commission was motivated solely by a concern to sell its surpluses and thereby to minimize the costs to the Canadian public of the price support program.

#### 7. *Allegation A.1(b)(iv)*

Allegation A.1(b)(iv) reads as follows:

"The C.D.C. did not reveal to Schafer Bros. Ltd. its intentions to take over the market for the sale of Canadian skim milk powder to CONASUPO until this taking over took place in 1971-1972."

This allegation was added to the draft statement of allegations at the request of counsel for Schafer Bros. Ltd. in the early stages of the hearings, although it was not made in the pre-Inquiry writings of Michel Choquette. Nor does it appear to add anything to the Inquiry. Counsel for Schafer Bros. Ltd. made no submissions directed particularly to this allegation.

The allegation appears to have been inspired by the disclosure, in the documents filed by Commission counsel at the commencement of the hearings, that Dr. Barry and Mr. Goodwillie had held meetings with CONASUPO in October 1967. This fact had not previously been known to the Schafers or to Michel Choquette, although the fact that the Canadian Dairy Commission submitted a bid to CONASUPO in January, 1968 was made known to David Schafer by the Canadian Dairy Commission at the time.

The other apparent reason for making this allegation was that it was believed by Schafer Bros. Ltd. that a deliberate and voluntary act by the Canadian Dairy Commission caused the exclusion of the Canadian private sector from the CONASUPO busi-

ness as of 1971. This was simply not the case, as has been referred to above and as is also dealt with below in connection with Allegation A.1(b)(vi).

#### 8. *Allegation A.1(b)(v)*

Allegation A.1(b)(v) reads as follows:

"The C.D.C. on several occasions was deliberately vague in its representations to Schafer Bros. Ltd. concerning availability of supplies and the amount of subsidy to be given."

This allegation was also added at the request of counsel for Schafer Bros. Ltd., but again, after all the evidence was adduced and written submissions were requested of all counsel, counsel for Schafer Bros. Ltd. made no submissions directed particularly to this allegation.

The evidence disclosed that the Canadian Dairy Commission issued circulars on a regular basis and distributed them to private traders spelling out its policy regarding payment of subsidies.

The evidence also established that there is a small time lapse between the receipt of skim milk powder by the Canadian Dairy Commission from the manufacturers and the recording of such skim milk powder in the inventory records of the Canadian Dairy Commission.

Use of the word "deliberately" in this allegation was presumably intended to connote malice or irresponsibility of some sort on the part of the Canadian Dairy Commission, rather than referring to vagueness in circumstances where the Canadian Dairy Commission was simply unable to be specific or to give a definite future commitment.

There is no evidence at all to substantiate an allegation of any such deliberateness. Nothing can be inferred from the documents, and both David Schafer and George Schafer testified that they had no evidence or information in this respect other than what might appear from the documents.

Accordingly, there is no evidentiary basis for this allegation.

#### 9. *Allegation A.1(b)(vi)*

Allegation A.1(b)(vi) reads as follows:

"In 1971, the C.D.C. officially took over the market for the sale of Canadian skim milk powder to CONASUPO, thereby making it impossible for Schafer Bros. Ltd. to benefit from the 13 years of investment and promotional efforts which it had spent in the development of this market."

This is a further allegation that was added early in the course of the inquiry at the request of counsel for Schafer Bros. Ltd., but again, in their submissions at the conclusion of evidence such counsel did not make any submission directed in particular to this allegation.

The last half of this allegation as framed, following the comma, consists merely of argumentative words.

It is clear that in early 1971, probably as a result of the policy of the new administration in Mexico, CONASUPO insisted upon dealing exclusively on a government-to-government basis for its growing requirements for skim milk powder imports. An internal memorandum in the Department of Industry, Trade and Commerce dated May 5, 1971 records that CONASUPO had "formally advised the Canadian Dairy Commission that it is now their policy to negotiate directly with foreign governments for all their requirements." (see Document 583, Exhibit 12). The existence of this new policy in the spring of 1971 was confirmed in the course of the interviews held by the Commission of Inquiry in Mexico City, where it was also indicated that had the Canadian Dairy Commission not agreed to sell directly to CONASUPO, CONASUPO would in all likelihood have purchased its skim milk powder from one of Canada's competitors.

(The documentary evidence indicated that in April, 1972, CONASUPO may have invited price quotations from one or two private Canadian traders (not including Schafer Bros. Ltd.) for a possible sale of skim milk powder, but the evidence was not clear nor was it explained by anyone. It may have been a small or specialized order, or may even have resulted from some confusion at CONASUPO.)

In view of CONASUPO's position in the spring of 1971, the Canadian Dairy Commission discontinued the practice it had followed for the prior two years, of issuing a special trade circular announcing the export subsidy level for Canadian sales of skim milk powder to CONASUPO and also the terms and conditions upon which the Canadian Dairy Commission itself would supply skim milk powder for such sales. Dr. Barry's evidence was that by not issuing such a circular in 1971 or subsequently, the Canadian Dairy Commission thereby discontinued making any export subsidy or stocks available for such sales. He said that although no special announcement was made to this effect, the private trade understood the significance of discontinuing the circulars.

The first sale of skim milk powder by the Canadian Dairy Commission to CONASUPO was evidenced by the contract dated May 14, 1971 to sell 10,000 metric tons (Exhibit 12, pages 589-596).

David Schafer in his evidence said that his reason for making this allegation was his belief that it was

the Canadian Dairy Commission, and not CONASUPO, that was responsible for excluding the private sector altogether in the spring of 1971 from the sale of Canadian skim milk powder to CONASUPO. Mr. Schafer's belief that this was so resulted, he said, from his having been told by the Director General of CONASUPO that the Canadian Dairy Commission had initiated the talks in respect to arrangements between the two government agencies. Dr. Barry's evidence is to the contrary, and in view of his evidence, the internal Department of Industry, Trade and Commerce memorandum dated May 5, 1971 and the interviews held in Mexico City, it appears that Mr. Schafer's belief is not well founded.

The taking over of the CONASUPO business by the Canadian Dairy Commission clearly was not an exclusionary act of the Canadian Dairy Commission. It resulted from Mexican government policy, a fact corroborated unequivocally by the interviews with the witnesses in Mexico. Judging from complaints made by Ronald A. Chisholm Ltd. and others in 1971 and 1972 about the trading activities of the Canadian Dairy Commission with CONASUPO, however, it is evident that Schafer Bros. Ltd. was not alone in either feeling hurt or in not understanding the reasons for the new trading relationship that was established in 1971 between the Canadian Dairy Commission and CONASUPO.

I do not deal here with the argumentative words "thereby making it impossible for Schafer Bros. Ltd. to benefit from the 13 years of investment and promotional efforts which is had spent in the development of this market", because the facts assumed by that statement are dealt with elsewhere in this Report.

## 10. Allegation A.2

Allegation A.2 reads as follows:

"In January 1968 the C.D.C. prevented Schafer Bros. Ltd. from taking advantage of the first opportunity to make a major sale of Canadian skim milk powder to CONASUPO by:

- (a) refusing to make its stocks available to Schafer Bros. Ltd.,
- (b) refusing to cooperate with respect to subsidies and financial arrangements,
- (c) not indicating its intention of competing directly with Schafer Bros. Ltd. for a CONASUPO tender until January 24, 1968, and
- (d) making a direct offer itself to CONASUPO involving C.D.C. stocks and benefiting from subsidies and financial

arrangements which the C.D.C. had accorded to itself."

It should be noted that subparagraphs (c) and (d) were added at the request of counsel for Schafer Bros. Ltd. during the Inquiry.

The evidence showed that until evidence was adduced at this Inquiry David Schafer believed that Schafer Bros. Ltd. was the only private firm in Canada to be invited by CONASUPO to bid on this contract. This belief appears to have originated in Mr. Schafer's lack of awareness of the presence of other private Canadian exporters doing business in Mexico at the time, in his belief that among Canadian exporters he was uniquely known and trusted by certain CONASUPO officials, and in the Canadian Dairy Commission's failure to show him copies of requests or offers by other private Canadian traders to buy supplies from the Canadian Dairy Commission in connection with this tender.

The evidence established that other private Canadian traders received invitations from CONASUPO to bid for the sale to it of skim milk powder under the January 1968 tender. As to this, Dr. S.C. Barry and Mr. Goodwillie said at the time that at least three or four private Canadian traders had received invitations from CONASUPO, one of whom was Granby Co-op. There is in evidence a written invitation to Granby Co-op care of Benelol (its Mexican agent) which, at the Inquiry, caused David Schafer to doubt what he had been told by certain persons who were CONASUPO officials at the time. The evidence also established that Mr. Rodriguez Licea advised the Canadian Dairy Commission, shortly before Schafer Bros. Ltd. received its invitation from CONASUPO to tender, that all registered producers and suppliers were being contacted regarding this January 1968 tender. The evidence also established that Canadian skim milk powder had been exported to Mexico by others since at least the early 1960's, according to official government statistics of both Mexico and Canada. These statistics did not identify any particular traders in such purchase and sale of Canadian skim milk powder but such statistics did establish that Mexicans were familiar with the characteristics and availability of Canadian skim milk powder since the early 1960's.

The witnesses interviewed in Mexico, and Messrs. Bishop and Pariseault, confirm that sales of Canadian skim milk powder were made by other Canadian private traders to CONASUPO in the 1960's.

The evidence established that the Canadian Dairy Commission informed Schafer Bros. Ltd. that it was making a direct offer to CONASUPO in response to the January 1968 invitation to tender from CONASUPO and that it would not make its stocks available to Schafer Bros. Ltd. for such tender

because, as stated, if CONASUPO accepted both the Canadian Dairy Commission's tender and the tender of Schafer Bros. Ltd., the Canadian Dairy Commission would not have had sufficient skim milk powder to fulfil the requirements of both contracts.

The evidence in respect to the discussions between Schafer Bros. Ltd. and the Canadian Dairy Commission with respect to this do not support the allegation. In fact, the evidence seems to establish that the only offer that Schafer Bros. Ltd. made to the Canadian Dairy Commission to buy inventory to fulfil the requirements of this tender to CONASUPO was conditional upon CONASUPO accepting the Schafer Bros. Ltd. tender.

There is no evidence that the Canadian Dairy Commission discriminated against Schafer Bros. Ltd. or any other private trader with respect to subsidies and financial arrangements. The Canadian Dairy Commission treated all private traders alike.

The evidence establishes that the Canadian Dairy Commission did not indicate to Schafer Bros. Ltd. its intention to make a direct bid or to make a direct tender for this January 1968 sale to CONASUPO until sometime in January. It was not, however, required to do so. While there was no statutory or other duty on the Canadian Dairy Commission to disclose its intention to make a direct bid itself to CONASUPO, at the same time there is no evidence to suggest that the Canadian Dairy Commission deliberately kept such intention a secret.

Subparagraph (d) of the allegation, namely, that by making a direct bid to CONASUPO the Canadian Dairy Commission benefitted from subsidy and financial arrangements which it accorded to itself, is in substance correct but irrelevant.

It should be noted that the bid price made by the Canadian Dairy Commission to CONASUPO with respect to this 1968 contract was at 10.24¢, whereas the Canadian Dairy Commission was only offering a subsidy such as would give private exporters a subsidized price of 13.5¢ per pound. The Canadian Dairy Commission could have increased its subsidy payable to private traders by 3.26¢ per pound and still not have cost the fund or the taxpayers any more net dollars than would have been the case had the Canadian Dairy Commission's bid been accepted.

Counsel for Schafer Bros. Ltd. in his submissions in respect to this allegation, describes Dr. Barry's conduct in connection with the January, 1968 tender as "deceitful" and "dishonest", specifically with reference to the advice that Dr. Barry gave to Ministers that CONASUPO wished to deal directly with the Canadian Dairy Commission. The employment of these words is entirely unwarranted and improper.

### 11. Allegation A.3

Allegation A.3 reads as follows:

In August 1968 the C.D.C. sold a large quantity of skim milk powder to competitors of Schafer Bros. Ltd. at a price considerably lower than had been offered unsuccessfully by Schafer Bros. Ltd. to the C.D.C. for skim milk powder in January 1968, and considerably lower than was subsequently offered to Schafer Bros. Ltd. in October, 1968. In fact some of the powder which was actually delivered by the C.D.C. constituted fresh 1969-produced powder. The C.D.C. thereby prevented Schafer Bros. Ltd. for almost two years from competing effectively in the sale of skim milk powder to certain foreign countries."

The background of this so-called consortium transaction was described by Timothy Chisholm of Ronald A. Chisholm Ltd. as follows:

"In 1968, the world market in skim milk powder was in a depressed state, and the world price declined steadily from January 1968 into the summer of that year.

"By the summer of 1968, the Canadian surplus, which was known to be substantial, was one of the major factors in contributing to the then depressed state of the market.

"At that time, Ronald A. Chisholm Limited was dealing in Europe primarily with Van den Bergh, a major European trader in milk powder and other commodities. At the same time Eastern Townships Produce Ltd. of Sherbrooke, Quebec (a competitor of Ronald A. Chisholm Limited), was dealing in Europe primarily with Ecoval, another major European milk trader based in Brussels.

"By the summer of 1968, both Van den Bergh and Ecoval felt that the market would not recover until the Canadian surplus was dealt with, and accordingly each approached Ronald A. Chisholm Limited and Eastern Townships Produce Ltd. with a view to our participating in a consortium which would purchase the entire Canadian surplus.

"On or about July 30, 1968, Dean Bishop of Eastern Townships Produce Ltd., Peter Van Wauyenberge of Ecoval and Mr. Van Ballegooijen of E.A. Ballegooijen & Zn. N.V. (who were to finance the consortium operation), and I met with Dr. Clifford Barry and D.B. Goodwillie of the Canadian Dairy Commission in Ottawa. At this meeting, we offered on behalf of the consortium to pur-

chase the entire Canadian surplus of skim milk powder, without regard to the age of the powder.

"During the same meeting, negotiations took place with regard to the purchase price, the commitment by the consortium to take certain amounts of powder within certain limited times, and related matters. Eventually, an agreement was reached, and this agreement was between the Canadian Dairy Commission and Eastern Townships Produce Ltd. (on behalf of the consortium)...

"The contract called for the purchase by the consortium of 35,000 metric tons of skim milk powder, which I do not believe was the entire surplus which the Canadian Dairy Commission had in store at that time, but which was the maximum amount which the Commission was prepared to sell to the consortium at that time. The price agreed upon was 4¢ per pound, which was the approximate world price at that time.

"The purchase of this large portion of the Canadian surplus had the expected effect on the world market price of skim milk powder, in that the world price gradually started to increase when it became known in the trade that the major proportion of the Canadian surplus had been taken off the market."

The evidence confirmed that the skim milk powder that was sold by the Canadian Dairy Commission to Eastern Townships Produce Ltd. on August 12, 1968 for re-sale to the consortium in export markets was not the same powder to which either the January, 1968 or October, 1968 proposals pertained. The powder that was sold in the August, 1968 consortium sale was 1967 powder with perhaps a *de minimis* quantity of fresh powder that might have been required to complete particular shipments.

A restriction was attached to this sale; the Canadian Dairy Commission agreed not to sell skim milk powder below 5¢ a lb. for the next eight months for export outside North and South American without giving Eastern Townships Produce Ltd. the right of first refusal.

In the result, there is therefore no basis for this allegation insofar as it alleges that the Canadian Dairy Commission offered Schafer Bros. Ltd. in October, 1968 skim milk powder at a price higher than was offered to Eastern Townships Produce Ltd. because, as stated, the two proposals related to skim milk powder of different age and quality. Apparently Schafer Bros. Ltd. did experience some difficulties selling fresh skim milk powder for the following two years in the European market, but that is no criticism

of the Canadian Dairy Commission in making this sale to Eastern Townships Produce Ltd. for re-sale to the consortium.

The pre-Inquiry writings of Michel Choquette treated this so-called consortium sale transaction as a substantial issue insofar as Schafer Bros. Ltd. and David Schafer were concerned. As a result of the evidence produced and given at the Inquiry, however, this allegation ceased to have real importance or significance to David Schafer or Schafer Bros. Ltd. In fact, David Schafer testified (Transcript p. 2776) that it was not his intention to make this allegation.

This whole matter seems strange and unsupportable in that once again, shortly after commencement of the public hearings, counsel for Schafer Bros. Ltd. requested that the allegation as framed by Commission counsel on the basis of Michel Choquette's writings be amended by adding the words underlined above in the allegation. His request was granted.

This is especially unsupportable in view of the fact that David Schafer in evidence stated that he made the amended allegation, as to the inclusion of fresh 1969 powder, because a trucker, a Mr. Rouleau in Montreal, had told him that fresh 1969-produced powder had been delivered as part of this so-called consortium purchase. That is the sole basis David Schafer had for amending this allegation to include those words. As to any fresh powder being included in such sale, Dr. Barry stated that a bit of fresh powder may possibly have been included to complete shipments under the August 12, 1968 contract, but that obviously only an insignificant amount of fresh powder, at most, was included.

Not relevant to the allegation, but as a matter of some other interest, the amount of public funds expended or lost in connection with the powder sold to Eastern Townships Produce Ltd. was approximately \$12,000,000, not including storage, finance or other costs.

## 12. Allegation A.4

Allegation A.4 reads as follows:

"In the spring of 1969, the C.D.C. made it unnecessarily difficult for Schafer Bros. Ltd. to fill its first order from CONASUPO by:

- (a) repeatedly giving false and misleading information to Schafer Bros. Ltd. as to the availability, location and the heat treatment and bacteria characteristics of the skim milk powder available from the C.D.C. for the transaction,
- (b) refusing to cooperate concerning financial arrangements, and

- (c) causing Schafer Bros. Ltd. to incur additional laboratory, manufacturing, and transportation costs in order for them to be able to fulfil CONASUPO's contractual requirements."

On February 3, 1969 Schafer Bros. Ltd. entered its first (and only) contract with CONASUPO for the supply of skim milk powder. It was a contract for 450 tons of high-heat powder and 320 tons of low-heat powder, all to have a DMC count below 75 million.

The essence of this allegation seems to be a belief on the part of David Schafer that the Canadian Dairy Commission deliberately sought to frustrate the efforts of Schafer Bros. Ltd. to complete the shipments according to this contract.

Michel Choquette's writings set out the factual basis of this allegation in this way:

- (a) "...David Schafer would not have made a commitment to CONASUPO if Mr. Goodwillie had not said that the Commission could supply Schafer Bros. — i.e. if he had not said that supplying high heat powder would present no problem and that Schafer Bros. could test as many lots as necessary". (Exhibit 6, Vol. VI, p. 120)
- (b) Schafer Bros. Ltd. "... was intentionally misled by the Dairy Commission as to the location and availability of certain lots of skim milk powder" (Exhibit 6, Vol. IX(G), pp. 3-4; [at p.16 it is alleged that it may have been "gross negligence"]; Exhibit 6, vol. IX(C), pp. 6-7)
- (c) "... thus obliging them to spend an unnecessary amount of time looking elsewhere for supplies, (and causing) them to be late with their deliveries on what was their first sale to CONASUPO, thus seriously jeopardizing their relationship with a customer they had worked 8 years to secure..." (Exhibit 6, Vol. IX(G), p. 16)
- (d) The Canadian Dairy Commission caused them to pay more than they had been led to rely on for both the high heat and low heat portions of the order. (Exhibit 6, Vol. IX(G), pp. 18-19; Exhibit 6, Vol. VII, pp. 32-33, 47)
- (e) Although the Canadian Dairy Commission's records of its own inventory seemed to be disorganized, and deficient regarding heat treatment specifications, thereby causing loss to Schafer Bros. Ltd., the Canadian Dairy Commission repeatedly gave information regarding the DMC (bacteria) counts that was false according to records it did have. (Exhibit 6, Vol. IX(C), pp. 6-7; Exhibit 6, Vol. IX(G), pp. 19-20 And see: Exhibit 6, Vol. VII, pp. 31-57; Exhibit 6, Vol. VI, p. 122 ["it is... a question of whether



the misrepresentation. . . was innocent, negligent or fraudulent”)]

- (f) Generally, through matters of financing, supplying information, and granting access to inventory lots for sampling, “. . . the Dairy Commission made it unnecessarily difficult for the Schafers to obtain supplies from government stocks for Schafer Bros.’ sale to CONASUPO”. (Exhibit 6, Vol. IX(G), p. 16; Exhibit 6, Vol. VI, pp. 6, 106-124; Exhibit 6, Vol. VII, pp. 47-49, 53-56)
- (g) In dealing with Schafer Bros. Ltd. in connection with its attempts to fill the small 770 ton order in 1969, was the Canadian Dairy Commission seeking to prejudice the competitive position of Schafer Bros. Ltd. with respect to the large annual tender calls from CONASUPO, including the very large tender call from CONASUPO that was expected imminently? (Exhibit 6, Vol. 7, p. 51; Exhibit 6, Vol. 6, pp. 123-124)

The factual basis of David Schafer’s complaint in this respect is contained in his evidence as follows:

“On January the 8th, I went to Ottawa to meet with Mr. Goodwillie and inquired about the availability of such supplies as well as the subsidy. I informed Mr. Goodwillie that once again CONASUPO required powder no more than 90 days old and with a D.M.C. Count not exceeding 75,000,000.

“Mr. Goodwillie asked me if I was certain that CONASUPO would not accept a D.M.C. Count of 200,000,000 and whether it was absolutely essential that the 320 tons be low heat as opposed to high heat or medium heat.

“I answered that I believed it was important to offer the Mexicans exactly what they specified.

“Mr. Goodwillie informed me that since the Commission kept a record of the D.M.C. Count of the lots it purchased from producers, and that several producers regularly delivered powder with a D.M.C. Count lower than 75,000,000 to the C.D.C., Schafer Bros. would be able to fulfil Mexico’s requirements in this respect.

“As far as low and high heat were concerned, however, Mr. Goodwillie informed me that the Commission was not obliged to test for heat treatment, since its purchasing regulations did not include a whey protein nitrogen analysis.

“Mr. Goodwillie, however, stated that the Commission would be prepared if and when

Schafer Bros. actually made the sale, to indicate which lots of powder were most likely to be high heat and which were most likely to be low heat.

“Mr. Goodwillie stated that Schafer Bros. would have no trouble finding sufficient high heat powder in the Commission’s stocks, though finding enough low heat powder could present a problem.

“He stated that Schafer Bros. would have to employ at its own expense, a sampling agency and a private laboratory to double-check the lots for heat treatment and that Schafer Bros. would probably be obliged to commission a private manufacturer to produce most of the low heat powder custom-made, which would cost us a little more.

“Mr. Goodwillie informed me that the C.D.C. would supply such powder at 6¢ per pound (subsidized price) ex-warehouse Montreal or Toronto, and that this price would apply to all powder exported for this order, whether it were purchased from C.D.C.’s stocks or from private manufacturers.

“On January the 9th, 1969, Schafer Bros. Ltd. contacted J.G. Morazain Co. Ltd., a private manufacturer’s agent, and asked Mr. Morazain to make preliminary inquiries concerning the availability of custom-made production of low heat powder.”

The evidence established that, at the time, the Canadian Dairy Commission did not have an adequate record system, so as to enable it to provide accurate information regarding the D.M.C. Count of its inventory of skim milk powder.

Nor did the Canadian Dairy Commission have any inventory records showing which lots of its powder were high heat or low heat, because the Canadian Dairy Commission purchasing regulations did not require a whey-protein-nitrogen test which would have identified the heat treatment characteristics of the powder.

The Canadian Dairy Commission officials, as for example Mr. Goodwillie, did, however, know in a general way which of the manufacturers produced high heat and low heat skim milk powder and, in that general way, indicated to Schafer Bros. Ltd. who those manufacturers were and where the supplies might be found.

The evidence established that there is no basis for David Schafer’s contention that the Canadian Dairy Commission guaranteed him a supply of high-heat powder. The documents in evidence, in fact, include a telex dated January 23, 1969, from Mr. Marcellus of

the Canadian Dairy Commission to Schafer Bros. Ltd. (see Document 277, Exhibit 12, Vol. 1) wherein Mr. Marcellus states that the Canadian Dairy Commission does not give any guarantee of the availability of high-heat skim milk powder from Canadian Dairy Commission stocks.

Therefore, there is no basis for allegation A.4(a).

As to subparagraph (b) of the allegation, the complaint of Schafer Bros. Ltd. relates to the 2¢ deposit against proof of export of skim milk powder from Canada and the question as to whether the Canadian Dairy Commission should have accepted an assignment of CONASUPO's Letter of Credit.

The evidence establishes that in respect of the 2¢ deposit, the Canadian Dairy Commission waived this requirement at the request of CONASUPO. In respect of the Letter of Credit, David Schafer admitted on cross-examination that the Canadian Dairy Commission was justified in refusing to accept the assignment, because if the Canadian Dairy Commission had done so the effect would have been for the Canadian Dairy Commission to give a guarantee as to the availability of supplies that it had already expressly refused to give.

There is likewise no basis for subparagraph (c) of the allegation. As stated above, the Canadian Dairy Commission did not keep records respecting the heat treatment characteristics of its inventory. Insofar as Schafer Bros. Ltd. was required to go to sources other than the Canadian Dairy Commission for supplies to fulfill this CONASUPO contract, it, like any other private trader, was required to pay the laboratory costs, transportation costs and any other cost associated with such purchases.

It is worth noting that Rodriguez Ayala, in the interview with the Commissioner at Mexico City in the presence of certain counsel, all having been invited, and Michel Choquette, said that he and Rodriguez Licea had discretionary authority to accept small tenders. He said that this 770 ton tender acceptance (a small tender) was, so to speak, for them a test case in respect to Schafer Bros. Ltd. to see if Schafer Bros. Ltd. could perform a contract entered into, and if so, Schafer Bros. Ltd. would be put on the list of persons to be invited to submit offers on large tender calls.

### 13. Allegation A.5

Allegation A.5 reads as follows:

"In the spring of 1969, the C.D.C. prevented Schafer Bros. Ltd. from winning a contract with CONASUPO for the supply of 25000 tons of skim milk powder by:

- (a) giving false and misleading information to Schafer Bros. Ltd. regarding the pay-

ment of export subsidies to Canadian firms dealing through foreign agents,

- (b) refusing to make its stocks available to Schafer Bros. Ltd. and then agreeing to make its stocks available to other Canadian exporters, and
- (c) discouraging Schafer Bros. Ltd. by announcing its intention of making a direct offer by itself to CONASUPO, involving C.D.C. stocks and benefitting from subsidies and financial arrangements which the C.D.C. would accord to itself."

The essence of this allegation is contained in subparagraph (a). Subparagraphs (b) and (c) of the allegation, underlined, were added to the Statement of Allegations at the commencement of the public hearings at the request of counsel for Schafer Bros. Ltd.

Mr. David Schafer, Dr. Barry and Mr. Timothy Chisholm gave oral evidence in respect to this matter and there was substantial documentary evidence, all of which are referred to in Appendix 11 to this Report.

The evidence established that it was known early in 1969 to all Canadian private traders and to the Canadian Dairy Commission that CONASUPO was about to invite offers for the supply of 25,000 tons of skim milk powder.

Thomas P. Gonzalez, an agent with offices in both Los Angeles and Mexico City, was a long-established agent and was known to be successful in respect to contracts generally with CONASUPO.

Thomas P. Gonzalez and David Schafer had certain conversations in early 1969. David Schafer stated that Mr. Gonzalez offered to act for him on two occasions in connection with the forthcoming CONASUPO invitation for tenders but that he, David Schafer, declined to join with him in any business relationship.

David Schafer then contacted Dr. Barry, the Chairman of the Canadian Dairy Commission, and stated in his evidence that the following took place:

"On March the 31st, 1969, I telephoned Mr. Barry, who was staying at the Hotel Ritz in Mexico City.

"I made this call from the office of Mr. T.F. Harris, Commercial Counselor at the Canadian Embassy in Mexico, in the presence of Mr. Harris, and a local Commercial Officer, Mr. Fidencio Arguelles.

"I told Mr. Barry of the offer which I had received from Mr. Thomas P. Gonzalez.

"Mr. Barry told me that the Canadian Dairy Commission would pay an export subsidy only to a Canadian exporter dealing directly with Mexico.

"Subsequently, Mr. Thomas P. Gonzalez contacted me once again and, believing that I had Mr. Barry's support in this matter, I told Mr. Gonzalez that Schafer Bros. Ltd. refused to become a purchasing agent in Canada for an American firm selling directly to CONASUPO."

In further elaboration of his evidence David Schafer stated: "I asked Mr. Barry not to give a subsidy when it is not a Canadian seller. That was what I asked and Mr. Barry accepted..." (Transcript p. 552)

The fact of the matter is that what subsequently transpired was that Ronald A. Chisholm Ltd., a Canadian trader, supplied the Canadian skim milk powder to CONASUPO under the contract as eventually awarded.

Timothy A. Chisholm, President of Ronald A. Chisholm Limited, in evidence stated as follows:

"In 1969, we received an inquiry from Thomas P. Gonzalez Corporation for 25,000 metric tons of skim milk powder (subject to a 10% tolerance either way), once again for shipment to CONASUPO in Mexico. Although the Canadian Dairy Commission would not guarantee any supplies for this contract, it was our opinion that the contract could be filled by purchasing from the private Canadian processors of skim milk powder, and accordingly we offered to sell the full 25,000 metric tons, subject to the 10% tolerance, and our offer was accepted. Eventually, approximately 27,000 metric tons were shipped on this contract, and I believe that all but the last 1,000 tons were purchased from private processors..."

"With respect to all of the contracts... in 1968, 1969 and 1970, Ronald A. Chisholm Limited acted as a principal in all respects, including that:

- (a) it sourced the powder from private Canadian producers or from the Canadian Dairy Commission;
- (b) it negotiated the purchase price from the suppliers;
- (c) it financed the purchase of the powder from its own resources;
- (d) it arranged for and paid for the shipment of the powder to Mexico;

- (c) where necessary, it arranged for and paid for any testing of powder which was required in order to meet CONASUPO's specifications."

As to this, David Schafer in evidence stated:

"On May the 9th, 1969, I learned from CONASUPO officials that the American trader Thomas P. Gonzalez of Los Angeles had submitted an offer for the large CONASUPO tender, of Canadian powder which he had apparently made arrangements to obtain through a Canadian purchasing agent.

"I immediately telephoned my son George in Montreal to tell him that this was contrary to Mr. Barry's oral promise, and to ask him to remind Mr. Barry that milk powder is subsidized at the expense of Canadian taxpayers, and that it was unjust to Canadians for an American company to receive the benefit of Canadian export subsidies.

"On May the 12th, 1969, Mr. Barry wrote to Schafer Bros. Ltd., that although the C.D.C. dealt only with the Canadian firms concerning milk powder exports, he could not take a position which would require Canadian firms to conduct their negotiations with foreign buyers directly rather than through agents." (Exhibit 12, Vol. 2, p. 396)

That is the evidence so far as the situation obtained in 1969.

Subsequently, as noted, in the spring of 1971 the Canadian Dairy Commission made its first direct sale of skim milk powder to CONASUPO and ceased to pay any subsidy to any private traders who attempted to deal with CONASUPO, and thereby effectively excluded all private traders from the CONASUPO market for skim milk powder.

As to this latter, Ronald A. Chisholm Ltd. complained by telex on the 2nd of April, 1971 to the Honourable H.A. Olson, Minister of Agriculture, regarding the actions of the Canadian Dairy Commission with respect to the CONASUPO market for Canadian skim milk powder. Ronald A. Chisholm Ltd. proposed that a delegation of three private sector traders meet with the Minister to discuss the matter. (Exhibit 12A, Vol. 8, p. 1482)

Ronald A. Chisholm Ltd. apparently also made complaints to other Ministers including the Minister of Industry, Trade and Commerce.

As a result of this latter complaint, Mr. A.G. Kniewasser, Senior Assistant Deputy Minister, Industry and Trade Development of the Department of Industry, Trade and Commerce wrote to Dr.

Barry, Chairman of the Canadian Dairy Commission on the 20th of May, 1971. On the 26th of May, 1971 Dr. Barry replied to Mr. Kniewasser, in part as follows:

"In the last two years at least, that is in 1969 and 1970, we established a rate of subsidy which we would pay to anyone who got the Conasupo business, but insisted that it had to be a direct contract between a Canadian firm and Conasupo.

"Now, I think I know the Canadian firm [Ronald A. Chisholm Ltd.] which is complaining the most about the recent arrangement with Conasupo. If I am correct, it is the one which claims to have done most of the recent business from Canada to Conasupo. That firm has also complained because some sales of Canadian powder have been made by foreign firms.

As matters turned out, and in spite of our insistence that to qualify for subsidy a Canadian firm should contract directly with Conasupo, that did not happen in the case of this firm. The contract was taken by an American firm and the Canadian merely acted as the agent of the American firm to secure the powder in Canada." (Exhibit 12, Vol. 3, p. 608)

Dr. Barry in oral evidence at the Inquiry said that he was in error to have included the reference to "1969" in the portion of the letter as quoted above.

From this and all the evidence, the conclusions are:

First, it was known in the trade that there would be practically no skim milk powder from the United States available to supply this 1969 CONASUPO request for 25,000 tons of skim milk powder.

Second, it was known in the trade, including David Schafer of Schafer Bros. Ltd., that Thos. P. Gonzalez Corporation of Los Angeles and Mexico City had been very successful in joining with various private traders to conclude contracts with CONASUPO for the sale of skim milk powder and other products.

Third, David Schafer probably thought that if Thos P. Gonzalez Corporation could be taken out of the picture, so to speak, the prospects of Schafer Bros. Ltd. concluding the contract with CONASUPO would be enhanced.

Fourth, as a consequence, he had the above-mentioned conversation with Dr. Barry. David Schafer understood as a result of that conversation that no subsidy would be paid on the export of Canadian skim milk powder if the powder was not sold directly by a Canadian private trader to CONASUPO without the use of any intermediary, such as Thomas P. Gonzalez.

Fifth, Dr. Barry's understanding of his conversation with David Schafer is not the same as David Schafer's.

Sixth, Ronald A. Chisholm Ltd. exported from Canada 27,000 tons of Canadian skim milk powder to fulfil this contract with CONASUPO in 1969. Although the company says it acted as principal in all respects, the form such contract took was that Ronald A. Chisholm Ltd. sold the powder to Thos. P. Gonzalez Corporation who in turn resold to CONASUPO.

In this latter connection, the evidence disclosed that because of complaints made in respect to this 1969 transaction with CONASUPO, the form of the contract was changed for the 1970 sale so that in form Ronald A. Chisholm Ltd. contracted directly with CONASUPO. But the important and significant matter is that Thos P. Gonzalez Corporation acted for Ronald A. Chisholm Ltd. in connection with the 1970 contract substantially as it did in connection with the 1969 contract. The only difference in respect to the 1970 contract was that a company called CEPASA, who frequently acted as the agent of Thomas P. Gonzalez in Mexico, was formally appointed the agent of Ronald A. Chisholm Ltd. in Mexico for the purposes of this particular contract.

The conclusions, therefore, are that it was within the authorized power of the Canadian Dairy Commission to pay the subsidy it did to Ronald A. Chisholm Ltd. in respect to the export sale of the 27,000 tons of Canadian skim milk powder in 1969 and that the Canadian Dairy Commission was under no obligation to David Schafer or Schafer Bros. Ltd. to limit the circumstances under which it would pay such a subsidy. In any event, that is not the real underlying basis for the complaint here.

The real basis of the complaint is that David Schafer did not succeed in excluding Thos P. Gonzalez Corporation from participating in the negotiation for the 1969 contract to sell skim milk powder to CONASUPO. But even if this complaint had any merit, it is irrelevant because, in fact, Schafer Bros. Ltd. would not have received the contract. The Schafer Bros. Ltd. bid was 61¢ above the bid made by what may be termed the successful Ronald A. Chisholm Ltd.-Thos P. Gonzalez Corporation bid. As to this, counsel for Ronald A. Chisholm Ltd. computed the differential between the two bids and put the computation to David Schafer in evidence, to which he had to agree: the Schafer Bros. Ltd. bid for 25,000 tons of skim milk powder was \$336,000 higher than the successful Ronald A. Chisholm Ltd. — Thos P. Gonzalez Corporation bid.

Subparagraph (b) of the allegation, namely that the Canadian Dairy Commission refused to make its stocks available to Schafer Bros. Ltd. and then agreed to make its stocks available to other Canadian exporters, is also without merit. The evidence is that

the Canadian Dairy Commission telexed to all private traders on February 11, 1969 that the Canadian Dairy Commission would not supply powder for this 1969 proposed contract with CONASUPO except for small amounts for emergencies. (It also advised that the amount of the subsidy would be 13.8¢.) David Schafer believed prior to the evidence at this Inquiry that Ronald A. Chisholm Ltd. had sourced all the powder for this contract from the Canadian Dairy Commission inventory. In this he was shown to be wrong. The Canadian Dairy Commission only supplied 1,000 tons on an emergency basis to Ronald A. Chisholm Ltd. so that it could deliver the 27,000 tons actually called for under the contract. In supplying the 1,000 tons the Canadian Dairy Commission exacted a 1¢ per pound premium, amounting to \$22,000, from Ronald A. Chisholm Ltd.

Nor is there any merit in subparagraph (c) of this allegation. The evidence of David Schafer as to this is:

"On April the 28th, 1969, I phoned Mr. Barry in Ottawa, from Mexico. He informed me that the Dairy Commission intended to make a direct offer to CONASUPO and that although he might be prepared later, if the CDC got the contract, to discuss possible involvement on Schafer Bros.' part, he wished to do the actual negotiating with CONASUPO himself."

"On May the 1st, 1969, I went to Ottawa to meet with Mr. Barry.

"He told me that the Canadian Dairy Commission had full intentions of continuing its negotiations with CONASUPO and that he was not prepared to work out any sort of arrangements with Schafer Bros. Ltd. before the tender."

The Canadian Dairy Commission's action in making a tender did not discourage either Ronald A. Chisholm Ltd. or four other firms from making tenders.

Counsel for Schafer Bros. Ltd., at the conclusion of all evidence, agreed that Schafer Bros. Ltd. had no evidence to support this allegation.

(The incidents relating to this allegation do, however, illustrate the ad hoc nature of much of the Canadian Dairy Commission's conduct, a matter that will be returned to in this Report.)

#### 14. Allegation A.6

Allegation A.6 reads as follows:

"In 1969, 1970 and 1971, Schafer Bros. Ltd. lost out to a competitor on sales to CONASUPO as a direct result of irregular behaviour on the part of the senior officials of the C.D.C."

The year 1971 was added to this allegation at the request of counsel for Schafer Bros. Ltd., but no evidence was adduced in respect of 1971 so only the years 1969 and 1970 need be considered.

The source of this allegation is the letter of Michel Choquette to Gilles Choquette, then Executive Assistant to the Minister of Agriculture (Exhibit 6, Vol. VI, p. 161 and 162), where he writes: "... having, both in 1969 and 1970, lost out to Gonzalez/Chisholm on the large sales to CONASUPO as a direct result of what they felt was most irregular behaviour on the part of the senior officials of the Commission..." In elaboration of this, Michel Choquette alludes to the following suspicions:

1. The giving, or facilitating the giving, of inside information regarding bids to Ronald A. Chisholm Ltd. and/or Thomas P. Gonzalez in 1969 and 1970. (Exhibit 6, Vol. VI, pp.7, 139-140; Exhibit 6, Vol. VII, p.78; Transcript pp. 2468, 1841, 2783-86, 733-39, and Exhibit 12, Vol. 3, p. 505)
2. The matter of deliberately and repeatedly giving false information to Schafer Bros. Ltd. (Exhibit 6, Vol. VI, p.174), specifically in respect to:
  - (a) the 770 ton sale in early 1969 (see Allegation A.4), and
  - (b) the March 31, 1969 telephone conversation between David Schafer and Dr. Barry (see Allegation A.5(a)) (Exhibit 6, Vol. VI, p. 157);
3. The alleged receipt of kickbacks from Ronald A. Chisholm Ltd. or Thomas P. Gonzalez in return for preferential treatment (Exhibit 6, Vol. VI, p.175 above quoted);
4. The use of the word "fraud" (Exhibit 6, Vol. VI, p. 175, above quoted).

In this connection, it is convenient to quote from the said letter of Michel Choquette to Gilles Choquette, particularly pages 174 and 175, namely:

"Criminal liability: To consider, first of all, the criminal implications, may I draw your attention to what I have described earlier concerning the misleading actions of the senior officials of the Canadian Dairy Commission who, at the time of Schafer Bros.' loss leader sale to CONASUPO in 1969, threw obstacles in the Schafers' path by repeatedly giving them totally false information about the quality specifications and the whereabouts of registered powder in government stocks — not only with respect to heat treatment, of which for reasons best known to itself the Commission preferred not to keep records, but also with respect to DMC

count, of which the Commission most certainly did keep records.

"May I also remind you of the most irregular manner in which the Commission acted in providing information about supplies and subsidies at the time of the large 1969 and 1970 CONASUPO tenders, thereby allowing two of Schafer Bros.' competitors — Ronald A. Chisholm of Toronto and Thomas P. Gonzalez of Los Angeles — to join forces and make the sales.

"In addition, if it were to be proven that certain officials of the Canadian Dairy Commission received illegal "kickbacks" for their preferential treatment of Messrs. Gonzalez and Chisholm, or even extended favoured treatment to these traders without receiving supplementary remuneration, then this secretive transfer of the Mexican market for Canadian skim milk powder to these favoured individuals would surely constitute legal grounds for prosecution.

"Furthermore, if, in spite of the Canadian Dairy Commission's 'official' statements that by 1971 it had monopolized the Mexican market for skim milk powder and that consequently it was no longer giving export subsidies to private traders for sales of this commodity to Mexico, it could be shown that the same favoured Canadian exporters or any other traders received subsidies for sales to CONASUPO which the Dairy Commission refused to extend to Schafer Bros., it is probable that a court of law would find the past senior officials of the Commission guilty of fraud."

At the Inquiry, David Schafer, George Schafer and Michel Choquette were invited to give any evidence they had supporting this allegation. David Schafer said he had no evidence of any impropriety by Ronald A. Chisholm Ltd. (Transcript, pp.2254). George Schafer said he had no knowledge of anything to justify the allegation of kickbacks (Transcript, pp. 2374-75). Michel Choquette said he had nothing to support the "hypothesis" regarding Ronald A. Chisholm Ltd. He said they were merely questions he felt should be raised. (Transcript, pp. 2358-59).

David Schafer said that he felt that for Ronald A. Chisholm Ltd. and Thos P. Gonzalez Corporation to have outbid him by what to him were small margins, they must have had inside information. He said he "thinks" Messrs. Rodriguez Ayala and Rodriguez Licea told him that Thomas P. Gonzalez had inside information but that he did not know what it was.

(As to this latter there is no evidence, but it may very well be that Thomas P. Gonzalez had some kind

of inside information from CONASUPO. Apparently that was possible because David Schafer himself said that he had on occasion obtained inside information from CONASUPO and that that was how he outbid Gonzalez in January 1969.)

In respect to the 1970 contract with CONASUPO for 7,000 tons, Ronald A. Chisholm Ltd.-Thomas P. Gonzalez outbid Schafer Bros. Ltd. by a tenth of a cent per pound as stated. David Schafer said this was a very small margin and was the reason he suspected that Ronald A. Chisholm Ltd.-Thos P. Gonzalez Corporation had inside information. (See Exhibit 6, Vol. VII, p.78). However, this .1¢ a lb. translated into a difference of \$15,400 on the contract. The fact is, also, that Ronald A. Chisholm Ltd.-Thos P. Gonzalez Corporation bid lower than other rivals on that tender by an even narrower margin than .1¢ per lb.

There is unequivocally no evidentiary basis for this allegation.

As discussed elsewhere in this report, it is highly improper, inexcusable and shocking for allegations to have been made in the form in which they were made in the July 25, 1977 letter of Michel Choquette to Gilles Choquette without any evidentiary basis.

#### 15. *Allegation A.7*

Allegation A.7 reads as follows:

"In 1971, the C.D.C. frustrated a maturing business opportunity for Schafer Bros. Ltd. to structure a combination wheat/powder deal with Mexico by selling a large quantity of skim milk powder to CONASUPO."

Mr. David Schafer in his evidence put the actual basis for the allegation in this way:

"In the presence of Mr. Rocchi, Mr. de la Vega told me that the Canadian Dairy Commission had expressed interest in dealing directly with Mexico and had informed CONASUPO officials that since the C.D.C. controlled the export subsidies for Canadian Dairy products, it was in a better position to offer the most competitive prices from Canada.

"While at CONASUPO headquarters, I also met the new Purchasing Manager, Mr. Manuel Bravo Senties.

"Mr. Bravo Senties told me that CONASUPO might be looking for as much as 40,000 tons of skim milk powder for the current 1971 year and that Mexico was also interested in purchasing a large quantity of wheat.

"I suggested to him that it might be possible for Canada and Mexico to arrive at an

arrangement where Canada would deliver skim milk powder as well as wheat to Mexico on a combination sale on a long term credit basis.

"Mr. Bravo Senties expressed interest in this possibility, asked me to present a formal, written proposal, and told me that he would be most appreciative if I could speak to the Canadian Government about it upon my return to Canada.

"On February the 19th, 1971, Mr. Goodwillie wrote to us, stating that the C.D.C. would not commit itself to supplying more than 1,500 tons of powder for the Chilean tender, and that this quantity would not be available until May. Mr. Goodwillie added that the subsidy would be 10¢ per lb...

"On February the 24th, 1971, in Mexico, I personally delivered a letter to Mr. Bravo Senties at CONASUPO, outlining the basic elements of a combination skim milk powder and wheat sale...

"On March the 2nd, 1971, I returned to Montreal, and called Mr. Goodwillie at the C.D.C., advising him that there was a possibility of making a large combination milk powder and wheat sale to CONASUPO.

"On April the 6th, 1971, I went to Ottawa in order to meet with Mr. Goodwillie and during that interview I described to him the details of the proposed combination milk powder and wheat sale.

"Mr. Goodwillie told me that the C.D.C. could make absolutely no decision about grain sales and he refused to commit himself as to whether the C.D.C. would be interested in such a combination deal.

"Mr. Goodwillie told me at that time that CONASUPO had recently purchased a large quantity of high heat powder from Thomas P. Gonzalez at \$575.00 US per ton (about 26.2¢ Canadian per pound).

"On April the 6th, 1971, I met with Mr. N.A. O'Connell, of Market Operations at the Grains Program Office, in order to discuss the potential combination deal.

"Both Mr. O'Connell and Senator McNamara, former Chief Commissioner of the Canadian Wheat Board suggested that I contact XCAN Grain Limited in Winnipeg, which handles exports for the prairie province wheat pools.

"On that same day, I met the Honourable Otto Lang, Minister responsible for the

Canadian Wheat Board, and outlined the details of the combination milk and wheat sale in which Mr. Bravo Senties of CONASUPO has stated he was interested.

"Mr. Lang said that he would speak with officials at the Canadian Wheat Board as well as at the Canadian Dairy Commission.

"On April the 15th, 1971, I wrote to Mr. E.W. Pierce, General Manager at XCAN, explaining the details of the proposed combination sale...

"On April 20 I flew to Winnipeg to spend two or three days, looking into wheat sale possibilities. At XCAN I met with Mr. Pierce, and also Mr. George Turner. These two gentlemen expressed interest in working on the combination milk and wheat sale to Mexico.

"While I was still in Winnipeg carrying on these discussions, I learned that the Canadian Dairy Commission had just sold approximately 10,000 tons of skim milk powder to CONASUPO, thereby making the combination sale which I had been working on impossible."

From this evidence, Dr. Barry's evidence, and the documentary evidence, it is clear that although Schafer Bros. Ltd. were attempting to formulate a proposal, it could not be described as a "maturing business opportunity".

The Canadian Dairy Commission was entitled to and did make a direct sale of skim milk powder to CONASUPO in 1971. As already discussed, the Canadian Dairy Commission had to do so, or otherwise CONASUPO would not have purchased Canadian skim milk powder.

In sum, there is no evidence:

- (a) that the Canadian Dairy Commission made the sale to CONASUPO in order to prejudice the attempt by Schafer Bros. Ltd. to structure a skim milk powder/wheat deal to CONASUPO;
- (b) that the Canadian Dairy Commission's sale had the effect of prejudicing any Schafer Bros. Ltd. efforts, or
- (c) that the skim milk powder/wheat deal could have been put together in any event. (There were considerable difficulties setting up the wheat part of the proposed deal. (See Exhibit 12, Vol. 3, p. 627).

In the result, there is no evidentiary basis for this allegation.

## 16. Allegation A.8

Allegation A.8 reads as follows:

"In the winter of 1975-1976, when the Philippines invited tenders for a large three year contract the C.D.C. made it unnecessarily difficult for Schafer Bros. Ltd., which was the only Canadian trader contending, to compete with foreign competitors by

- (a) its lack of cooperation in providing timely assurances of prices and supplies, and also regarding preparation and support for important meetings, and
- (b) falsely denying that a request had come from Manila for the Commission to attend an important meeting."

The evidence before the Inquiry regarding this allegation consisted almost exclusively of the evidence of George Schafer, that of Richard Tudor Price (Director, Marketing Intelligence for the Canadian Dairy Commission) and certain documentary evidence.

Before going into details of this matter, it should first be noted that George Schafer said orally in evidence at the Inquiry that he had received cooperation from the Canadian Dairy Commission and that it was not the fault of the Canadian Dairy Commission or its officials that this sale was lost. He stated that it was lost because of some internal matter in the Philippines. George Schafer seems to blame, in part, his agent in the Philippines.

Speaking generally, the essence of what might be termed the so-called Philippines complaint is not one of discrimination by the Canadian Dairy Commission and its officials against Schafer Bros. Ltd., but rather a lack of aggressiveness by and depth of assistance rendered to Canadian exporters by the Canadian Dairy Commission.

In this connection it may be noted that the Canadian Dairy Commission and, in particular, Richard Tudor Price, did not have a large technical staff. Notwithstanding that, however, with the assistance of Mr. Tudor Price and other Canadian Dairy Commission officials all the technical problems of this proposed transaction in the Philippines were overcome. (See Michel Choquette memo to Gilles Choquette Exhibit 6, Vol. V, September 30, 1976.)

Exhibit 6, Vol. V consists of a series of memoranda made by Michel Choquette at the material time as to this matter, and after, all of which were sent to Gilles Choquette who was then Executive Assistant to the Minister of Agriculture. Together they set out what Michel Choquette conceives to be the position of Schafer Bros. Ltd. re the Philippines.

The facts are that the Canadian Dairy Commission had a very large surplus of skim milk powder in 1975,

and it was a priority to get rid of it as soon as possible and before it aged unduly. The Department of Industry, Trade and Commerce was itself involved in the search for markets. The origin of the Schafer Bros. Ltd. interest in this particular Philippines contract was as follows: Mr. Maravillas, from the Canadian Embassy in the Philippines told George Schafer that the Philippines purchase program was being reorganized and probably all purchases in future would be made through a new organization known as Food Terminal Inc. As a result of this information, on the 25th November, 1975, Schafer Bros. Ltd. offered to Food Terminal Inc. 50,000 tons of skim milk powder a year for three years with prices subject to verification. This offer was not, ultimately, accepted.

The reasons the Schafer Bros. Ltd. offer was not accepted (the offer of the New Zealand Dairy Board was accepted) appear to be:

- (a) Food Terminal Inc. did not, in fact, end up being the purchasing agent for the Philippines government and so did not have the power to complete the deal with Schafer Bros. Ltd.;
- (b) New Zealand and Australia maintained substantial representation in the Philippines for the sale of their skim milk powder and had many established contacts with local manufacturers and government officials there;
- (c) The agent of Schafer Bros. in the Philippines, one Isip, was not effective in any event in getting the specifications as to the heat treatment requirements from the local Philippines manufacturers. These specifications did not come until well after the January 8, 1976 meeting with the Philippines authorities in the Philippines, which meeting was the opportunity for Canadian exporters and officials to satisfy local authorities that Canadian skim milk powder could meet the requirements for the applications envisaged in the Philippines.

It should be noted that as a result of an international arrangement among Australia, New Zealand, the Canadian Dairy Commission and the E.E.C., none of the bidders on this contract could initially obtain supplies of skim milk powder for sale to the Philippines under a floor purchase price of \$520/ton. As to this, Exhibit 165, prepared by Mr. Tudor Price, reads in part as follows:

"In October 1975 Canadian Dairy Commission entered an informal understanding with other exporters intended to stabilize the human food skimmed milk powder price at U.S. \$520 per metric ton f.o.b. country of origin. This understanding operated until 1 April 1976 when the price fell to the GATT minimum. By early 1977 the human food price had risen above the minimum and has



continued to increase until the present time when it is U.S. \$950 — U.S. \$1000 per metric ton f.o.b. as balance has been restored to the market.”

The price quoted by the Canadian Dairy Commission to Schafer Bros. Ltd. did not, however, have anything to do with the failure to make this sale. In fact, although Schafer Bros. Ltd. did not request a better price in December, 1975 or January, 1976, on the 5th April, 1976, when price cutting was taking place among this group, the Canadian Dairy Commission dropped its price to Schafer Bros. Ltd. to \$350/ton from \$526/ton.

There was a certain amount of confusion in the correspondence between David Schafer and George Schafer with the Canadian Dairy Commission as to quantities, the fault which did not lie with the Canadian Dairy Commission.

The great difficulty in getting the specifications from the manufacturers in the Philippines is not satisfactorily explained. Apparently there was some dispute in the Philippines between the processors and the Philippines government as to whether more skim milk powder was needed and for what. In any event, Schafer Bros. Ltd. did not supply the specifications to the Canadian Dairy Commission in time for the Canadian Dairy Commission to do anything more than it did.

In respect to the allegation that Schafer Bros. Ltd. was the only Canadian exporter who may have been involved in attempting to obtain a contract in the Philippines in this matter, Canada Packers Ltd. may have also been negotiating for the sale, but there is insufficient evidence to substantiate this. Canada Packers Ltd. informed the Inquiry that its relevant records had been destroyed.

As to the interest and participation of other Canadian traders in this business prospect, on December 9, 1975 Schafer Bros. Ltd. asked Richard Tudor Price for some exclusivity but was “firmly refused”. Michel Choquette also suggested exclusivity for Schafer Bros. Ltd. in one of his memoranda to Gilles Choquette.

In respect to subparagraph (b) of the allegation, there may have been some misunderstanding between George Schafer and Richard Tudor Price at some point, but the facts are that Richard Tudor Price did go to Manila, attend the meeting and render every assistance to George Schafer. George Schafer confirmed in evidence that he did so.

In sum, there is no evidentiary basis for this allegation.

#### 17. *Allegation A.9(a)*

Allegation A.9(a) reads as follows:

“In 1977, the C.D.C. made it virtually impossible for Schafer Bros. Ltd. to take advantage of the following business opportunities by failing to answer its inquiries or by unduly delaying information regarding the availability of supplies, subsidies or potential sale opportunities:

- (a) a Peruvian inquiry in March concerning a certain type of high stabilized heat powder;”

Whether or not there is any merit in this allegation depends on whether or not six questions put on different occasions between March and May, 1977 by Schafer Bros. Ltd. to the Canadian Dairy Commission were answered by the latter. The questions concerned availability, quantity, specifications, packing, credit terms and performance bond.

On May 12, 1977, Richard Tudor Price of the Canadian Dairy Commission telexed George Schafer (Doc. 1128, Exhibit 12) with answers to the six questions:

- (a) Availability - “C.D.C. hereby extends you options for Canada first grade SMP. . . as per EPCHAP tender.”
- (b) Quantity - “High heat up to 60 metric tons medium heat up to 660 metric tons low heat up to 552 metric tons.”
- (c) Specifications - “Canada first grade. . . as per EPCHAP tender. C.D.C. not offering AMF heat stabilized powder or whey milk powder.”
- (d) Packing - SMP packed to C.D.C. general requirements of purchase for shipment.”
- (e) Credit Terms - “C.D.C. will not offer Canadian traders credit.”
- (f) Performance - “C.D.C. will not offer Canadian traders. . . performance bond.”

On May 13, 1977, George Schafer telexed Richard Tudor Price in acknowledgement of the above May 12, 1977 telex; and commented that it was “impossible for us to offer what buyer needs with terms you offered us.”

In respect to the credit matter, George Schafer commented that Schafer Bros. Ltd. may be able to get credit from the private sector; and in respect to

the performance bond he asked for the Canadian Dairy Commission's "kind cooperation". In addition, George Schafer requested extension of the validity of the offer to May 31, 1977. (See Document 1130, Exhibit 12).

On cross-examination David Schafer agreed that Richard Tudor Price did in fact answer every question contained in George Schafer's telex to Richard Tudor Price of May 9, 1977. (Transcript p. 1160). David Schafer also agreed in evidence that the April 25, 1977 telex was also answered by the May 12, 1977 telex. (Transcript p. 1172).

David Schafer also said in evidence that three days is sufficient time to prepare an offer; that the questions were asked on May 9, 1977, the reply was received on May 12, 1977, and the tender was to close on May 16, 1977. (See Transcript p. 1161)

In addition, George Schafer on cross-examination said that Schafer Bros. Ltd. received answers from the Canadian Dairy Commission to all the questions Schafer Bros. Ltd. had put to the Canadian Dairy Commission. (Transcript p. 1870).

Accordingly, it is difficult to understand why this allegation was made when Schafer Bros. Ltd. had in their possession at all material times the answers to every question that they had put to the Canadian Dairy Commission. Perhaps an explanation is that this transaction was of little or no importance to them in any event. Counsel for Schafer Bros. Ltd. submitted no argument directed to this allegation.

There is therefore no evidentiary basis to support this allegation.

#### 18. *Allegation A.9(b)*

Allegation A.9(b) reads as follows:

"In 1977, the C.D.C. made it virtually impossible for Schafer Bros. Ltd. to take advantage of the following business opportunities by failing to answer its inquiries or by unduly delaying information regarding the availability of supplies, subsidies or potential sale opportunities:

- (b) a Mexican inquiry in August for a potential sale of 30000 tons of skim milk powder;"

By formal agreement dated 17th August, 1977, but effective from May 20, 1977, the Canadian Dairy Commission entered into a contract with Ault Foods (1975) Ltd., appointing it the Canadian Dairy Commission's agent for sales to CONASUPO of Canadian skim milk powder.

Notwithstanding the existence of this contract between the Canadian Dairy Commission and Ault Foods (1975) Ltd., the following transpired.

On August 19, 1977 George Schafer telexed L.J. Marcellus, Director of Marketing Operations of the Canadian Dairy Commission, indicating that Schafer Bros. Ltd. had received an inquiry from Mexico for Canada first grade skim milk powder for human consumption. (See Document 1640, Exhibit 12A).

On August 30, 1977, Schafer Bros. Ltd. telexed Gilles Choquette, saying it had received an inquiry from an "official source in Mexico" for 30,000 metric tons of Canada first grade skim milk powder. (See Document 1643, Exhibit 12A). David Schafer testified at the Inquiry that the "official source in Mexico" was in fact the Commercial Secretary in Ottawa, Mr. Olivares, and that he, David Schafer, had spoken to him at a reception for Mayor Drapeau in Montreal (Transcript pp. 1043-46).

David Schafer testified that subsequently Gilles Choquette told him that the Canadian Dairy Commission would be offering to sell 45,000 metric tons of skim milk powder to CONASUPO and that Schafer Bros. Ltd. would be able to handle part of this quantity if a contract were entered into. David Schafer said further that when Mr. Choquette returned from Mexico in November 1977, Mr. Choquette phoned him to say that the Mexican transaction was smaller than had been expected and that the transaction would be handled completely by Ault Foods. (Transcript pp. 1048-49).

At this Inquiry Gilles Choquette stated that the Canadian Dairy Commission had received several inquiries about a 30,000 ton sale and that in response to each, presumably including that of Schafer Bros. Ltd., the Canadian Dairy Commission had said that the exporter would have to be able to assure the Canadian Dairy Commission that CONASUPO wished to deal directly with that exporter before a sale could be discussed further. If there was no such assurance the Canadian Dairy Commission would deal directly with CONASUPO. This view is consistent with the information received in the interviews in Mexico.

Gilles Choquette also stated in connection with the proposed 30,000 metric ton tender for skim milk powder for CONASUPO that in November 1977 David Schafer had come to his office to say that Schafer Bros. Ltd. wanted to be the Canadian Dairy Commission's agent for sales of skim milk powder in Mexico but that Gilles Choquette informed him that the Canadian Dairy Commission had already appointed an agent for it, namely Ault Foods (1975) Ltd., who were already, pursuant to that arrangement, making deliveries of skim milk powder to CONASUPO in Mexico.

Accordingly, there was no evidence to suggest that the Canadian Dairy Commission failed to answer the inquiries of Schafer Bros. Ltd. in respect to this matter or that it unduly delayed information regard-

ing the availability of supplies, subsidies, or potential sales opportunities as alleged.

In this connection also, counsel for Schafer Bros. Ltd. made no submission in respect to this allegation except in reply to the joint submission of counsel for the Canadian Dairy Commission and the other parties. The reply was irrelevant in respect to the allegation.

#### 19. *Allegation A.9(c)*

Allegation A.9(c) reads as follows:

"In 1977, the C.D.C. made it virtually impossible for Schafer Bros. Ltd. to take advantage of the following business opportunities by failing to answer its inquiries or by unduly delaying information regarding the availability of supplies, subsidies or potential sale opportunities:

- (c) an Algerian call for tenders in November for 10,000 tons of skim milk powder and 6,000 tons of anhydrous milk."

On October 13, 1977 Schafer Bros. Ltd. telexed Gilles Choquette that an inquiry had been received from Algeria for the possibility of supplying it with 6,000 metric tons of anhydrous milk fat and 10,000 metric tons of skim milk powder.

On October 26, 1977 David Schafer visited Richard Tudor Price at Ottawa and discussed with him this Algerian inquiry. David Schafer at that time said he had not seen any tender documents.

On November 8, 1977, Richard Tudor Price telexed David Schafer and asked him for the closing dates of the tender.

On November 8, 1977, George Schafer communicated to Richard Tudor Price that he would provide the closing date of this Algerian tender later.

On November 16, 1977, George Schafer, instead of replying to Mr. Tudor Price, wrote to Gilles Choquette asking the Canadian Dairy Commission whether it could furnish the supplies and if so at what price, and to provide him with the tender conditions. On November 23 and 24, 1977, David Schafer telexed Gilles Choquette saying no reply had been received to the telex to him of October 13, 1977, and also the letter of November 16, 1977, and stated that he must respond to the tender at the latest on November 25, 1977.

Richard Tudor Price said in evidence that after the November 8 reply of George Schafer stating that he would telex him the tender closing dates later, he had heard nothing more about this matter from Schafer Bros. Ltd. until November 25, 1977, when he noticed the telex of November 25, 1977, of Schafer Bros.

Ltd. to Gilles Choquette in the latter's office while Mr. Choquette was absent from Ottawa.

Richard Tudor Price said that he telephoned George Schafer who told him the tender was due the next day, and then advised George Schafer that the Canadian Dairy Commission could not offer anhydrous milk fat, but gave him a price indication for the skim milk powder. Mr. Tudor Price said that George Schafer was supposed to contact the Canadian Dairy Commission to provide the Algerian specifications, and to get their reaction to the indicated price, but he failed to do so. The details of that telephone conversation, according to Mr. Tudor Price, were confirmed in a telex sent on Monday, November 28, 1977.

David Schafer said in evidence that he approached Gilles Choquette directly in this matter because he had lost faith in Richard Tudor Price. He agreed that some time was lost by seeking to contact Gilles Choquette directly. He also agreed that Richard Tudor Price had phoned George Schafer on November 25, 1977 and, further, he agreed with Mr. Tudor Price's account of the conversation given in Mr. Tudor Price's evidence above referred to.

Finally, David Schafer said in evidence that he did not remember whether or not Schafer Bros. Ltd. made a tender offer in response to this request for tender to Algeria.

On this evidence there is no basis for any complaint by Schafer Bros. Ltd.

It should be also noted in this respect that counsel for Schafer Bros. Ltd. made no submissions in respect to this allegation.

#### 20. *Allegation A.10*

"In 1977, the C.D.C. unnecessarily required an attestation certificate for Schafer Bros. Ltd. to export 1,000 tons of skim milk powder to be used as animal feed in Chile.

As of at least May 10, 1976, pursuant to the General Agreement on Tariffs and Trade, an attestation certificate has been required from the country of import in the case of skim milk powder intended for animal feed, to the effect that the imported product would be used only for animal feed purposes in that country and not for human consumption. Such certificate was to be issued within 30 days of sale, and made available to the exporting country.

On May 13, 1976, there was a meeting of private traders held by the Canadian Dairy Commission and attended by David Schafer where the Canadian Dairy Commission explained the GATT requirements.

The evidence therefore establishes that David Schafer and George Schafer knew of this require-

ment. Further, David Schafer admitted in testimony that the Canadian Dairy Commission was obliged to request the certificate and that he was wrong in making this allegation.

Again, counsel for Schafer Bros. Ltd. made no submissions directed to this allegation, even though the allegation was added at the commencement of public hearings at the request of said counsel.

There is therefore no basis for this allegation.

## 21. *Allegation B.1*

Allegation B.1 reads as follows:

"The C.D.C. competed unnecessarily with private Canadian exporters."

On cross-examination by counsel for Schafer Bros. Ltd., Dr. Lawrence Skeoch said there were no necessarily adverse implications for efficiency if a marketing board competes with private exporters. In Dr. Skeoch's words, "the more people you have trying to explore market opportunities and so on, the better". In his view there was no reason why competition from the marketing board should discourage the efforts of people in the private sector — "soft competition is not really what we are trying to get in this world . . . ." Dr. Skeoch said that marketing boards should work energetically on all fronts, and should not have to rely totally on individuals. He referred specifically to the Canadian Wheat Board as one board that does a very good job in foreign marketing.

Dr. Skeoch said there was nothing unfair about a government moving in even where an individual has expended time and money in developing a market.

He further stated, in answer to a question from counsel for Schafer Bros. Ltd., that the well-being of private traders should not be the overriding concern in a government decision to give away food surpluses in an international aid program. The following exchange occurred in the cross-examination of Dr. Skeoch by counsel for Schafer Bros. Ltd. (Transcript pp. 376-78, 384-85):

"Q. If we could take a specific example, for instance the sale of skim milk powder over the years such as 1967 through 1976, a trader had to pay a two cent cash deposit on anything he wanted to export. That two cent cash deposit required certain financing if the amount of the powder he wanted to export was large. In addition, the trader had to pay for either five per cent or even less for a performance bond in order to guarantee the full amount would be exported and of course the trader would have to pay for his voyages back and forth to any given country as well as the various financing or personnel prob-

lems, if you will, figuring out what rates. If you take that on the one hand, and on the other hand a government marketing agency who has at their disposition, people who calculate freight rates and are paid by the government who don't have to undergo any financing problems in order to borrow money to pay either the full amount necessitated by the purchases or even a small amount such as the two cent per pound cash deposit necessitated by the government, all those problems are not faced by a big government but they are, are they not, by a private trader. How is it fair — this is the question I am putting to you based on your answer to my previous question — for a private trader to go into the market and be at the same level as the government especially if I may just complete it, since a private trader has to calculate a profit margin into his own scheme of figures, whereas the government doesn't necessarily have to calculate a profit margin to exist?

"A. The government as a representative of producers has no particular obligation to see anyone else is permitted or is subsidized in one way or another, listing certain costs and so on. The government has no obligation. The government is performing on behalf of the producers. It is not interested presumably in doing anything else. So if it feels it can perform more effectively, then I think it should be given the chance. If the individual is willing to — he must of course get his financing. That is obvious in any case, but there is no particular reason why the government should accept responsibility of providing him with financing. Suppose he doesn't do a good job? I can see no — I think you obviously are trying to establish the notion that there are certain preserved areas into which the government shall not enter even on behalf of the producers of the country if a private seller wants to go into those areas. I am not satisfied that one could make that condition.

"Q. But the government also represents exporters and taxpayers as well as producers?

"A. Yes, to some extent, but it doesn't have any obligation to subsidize them.

"Q. No. Dr. Skeoch, would you therefore consider it efficient on the part of the government to intervene and take over markets that have been developed by private traders? Do you think that is efficient economically, or does that discourage traders to develop other markets?

"A. The fact that somebody develops a market domestically doesn't mean that that market is guaranteed to him indefinitely. Other people can invade it very quickly and as a matter of fact this is done all the time. This is what is meant by competition. The fact that you are established in a market, that you spent some money developing a market doesn't mean that you would thereby acquire a right to continue to hold that market over any indefinite period of time. Now, if you were doing something in a superior fashion you should be allowed to do it, and should not be allowed arbitrary discrimination, but the essence of a competitive society, it's not that you have secure positions which are defended from other people, from other competitors, be they government or other agencies . . . ."

"Q. If we could just hypothesize that those things were true, that there was a taking over of the two largest markets for Canada for the sale of skim milk powder by the Canadian Dairy Commission and that these two markets are by far the largest, then would you not say that that type of intervention discourages private traders from developing other markets?"

"A. Well, I don't think you should worry too much as a matter of public policy. I don't think you should worry too much about whether it will put them out of the market so much as did they succeed by their marketing methods to improve the returns that the producers were getting. That is what they are supposed to do. You know they are not supposed to worry too much about other traders. They have a responsibility, as I recall their objectives here, they don't say anything much about protecting the interests of exporters. If they did not do a better job, if they did not do a better job in exploiting, developing the export market, then I would think they should give some explanation as to why they did what you said they did. I am not saying that they did this but from what you — the facts you give to me I would say that you want to ask them "Well, have you done a better job of promoting the interests of the groups, particularly the producers that you are responsible for, whose interest you are responsible for promoting?" and if they did I think they would have a logical basis for defending what they did. If not — but this is something, I think, Mr. Commissioner, that you will know more about after you have finished your proceedings than I can possibly say anything about. I do not want to get into that area."

Dr. Barry set out his view of the Canadian Dairy Commission's position in respect to this matter in general in a letter to Mr. A.G. Kniewasser, Senior Assistant Deputy Minister (Industry and Trade Development), Department of Industry, Trade and Commerce, dated May 26, 1971, in response to a letter from Mr. Kniewasser to him, dated May 20, 1971. Mr. Kniewasser replied to Dr. Barry by letter dated June 7, 1971. It will be helpful to reproduce this correspondence in full.

May 20, 1971.

Mr. S.C. Barry,  
Chairman,  
Canadian Dairy Commission,  
2197 Riverside Drive,  
OTTAWA, Ontario. K1A 0Z2.

Dear Mr. Barry:

Export Sale of Dry Skimmed Milk  
by the Canadian Dairy Commission.

I wish to refer to the recent sale of dry skimmed milk by the Canadian Dairy Commission to the Mexican Government purchasing agency, CONASUPO.

I appreciate the circumstances under which this sale was made but, as was to be expected, we have received complaints from exporters who are apprehensive about the Commission selling directly in export markets to the possible detriment of their own export sales.

I share their concern and felt that I should bring this matter to your attention.

Yours sincerely,

A.G. Kniewasser,  
Senior Assistant Deputy Minister  
Industry and Trade Development.

May 26, 1971

Mr. A.G. Kniewasser,  
Senior Assistant Deputy Minister,  
Industry and Trade Development,  
Department of Industry, Trade &  
Commerce,  
Place de Ville,  
112 Kent Street,  
Ottawa 4, Ontario.  
K1A 0H5

Dear Mr. Kniewasser:

Export Sale of Dry Skimmed Milk  
by the Canadian Dairy Commission

I have your letter of May 20 with reference to complaints which you have received from exporters on the above subject. There have been similar representations to us.

To put the matter in focus I should point out first, that we became involved in exports in any way only where export subsidies, or the sale below cost of product which we own, are concerned. We take no part in export business at commercial prices.

The costs of any such subsidies, or of losses on the sale of product which we have purchased under support, are not a charge against the government. The bulk of the funds required come from a levy against the price paid to the farmers for their milk. The rates of the levy are set by us. They are collected by, or under the authority of, provincial marketing agencies and are remitted to us.

We are, therefore, using producer money to cover these subsidies or losses. In the final analysis we are accountable to them for the proper management of the operation.

Export sales of skim milk powder on which we provide subsidy or supply product from our stocks fall into two broad categories.

One is purely commercial, from commercial firms in Canada to commercial firms abroad. On this type of business, where subsidy may be required, we merely establish a rate of subsidy and the commercial firms do the business.

The other category involves buying by, or under the authority of, government or semi-government organizations of the buying country. Mostly, this is by tender. Centralized Mexican buying, under Conasupo, has fallen in this category.

In this, also, our general operating procedure has been to fix a rate of subsidy, or a selling price on our product, on which exporters can base their quotations.

Up to the time of the present issue with Conasupo we have deviated from this principle in only two markets.

One is Cuba. In this case we negotiate a basic price with the Cuban authorities. They then designate a Canadian agent to handle the forwarding for them. The agent pays us, at the agreed price, for powder before we release it to him from storage and he in turn collects from the Cubans. We pay him his commission, again at an agreed rate which we negotiate.

The other case, which has so far been on only one occasion, was with India. CIDA had made a donation of skim milk powder to India on the condition that they purchase an equivalent quantity of Canadian powder. The Indian authorities insisted on dealing directly with us. We could, of course, have refused, but did not. They bought F.A.S. We merely engaged a forwarder to arrange the movement to one dock and assemble the documents, and the Indians paid us directly.

This brings me to Mexico, and Conasupo.

Up until recently, and apart from their purchases from the CCC in the United States, which they have negotiated directly, Conasupo's procedure has been to invite quotations from exporters in various countries. It has not been a tender procedure in the true sense.

In the last two years at least, that is in 1969 and 1970, we established a rate of subsidy which we would pay to anyone who got the Conasupo business, but insisted that it had to be a direct contract between a Canadian firm and Conasupo.

Now, I think I know the Canadian firm which is complaining the most about the recent arrangements with Conasupo. If I am correct, it is the one which claims to have done most of the recent business from Canada to Conasupo. That firm has also complained because some sales of Canadian powder have been made by foreign firms.

As matters turned out, and in spite of our insistence that to qualify for subsidy a Canadian firm should contract directly with Conasupo, that did not happen in the case of this firm. The contract was taken by an American firm and the Canadian merely acted as the agent of the American firm to secure the powder in Canada.

We had been particularly insistent on direct contracting by a Canadian firm in 1970 and had an indication that this had not been done only when the Canadian firm gave us details of the volume, shipping arrangements, etc. These involved some arrangements which we had not anticipated and which would have been more expensive to us.

We checked these out with Mexico and found that the information which had been given to us was not correct. When we confronted the Canadian firm with this, they confirmed that they had not made the contract with Conasupo, but had taken the word of the American contractor. They offered to get us a copy of the contract, but never did so.

There have been almost interminable problems in doing business with Conasupo through commercial channels. Every time they have called for bids all of the numerous agents in Mexico have tried to get numerous Canadian firms, whether or not they know much about the business, to submit bids.

There was a case where another Canadian firm, which also complains at any hint that we may negotiate directly, took a small contract with Conasupo for a special type of powder. We gave him a price at which we thought would sell our powder but warned him that we did not know which of our powder, or how much, would meet the specifications to which he had committed himself. We gave him lot numbers which we thought would come closest and arranged to let him draw samples for analysis. He had trouble filling his contract, was late in his deliveries to the embarrassment of Conasupo and tried to put the blame on us.

Whether or not because of experiences of this nature a Conasupo representative came to Ottawa recently and asked if they could negotiate a purchase directly with us. We told them we would. We gave them a price on both an f.a.s. and c&f basis and left it with them to decide which of the two to take.

If they had bought c&f, with all the involvement of shipping, we probably would have had a Canadian agent to handle it. However, they bought f.a.s., so we merely engaged a forwarder to get the powder to the dock, accumulate the documents, etc. We could hardly justify paying an agent up to five dollars a ton of farmers' money.

I apologize for the length of this letter. We are not interested in becoming the exclusive exporter of Canadian dairy products nor to take away the not only legitimate, but valuable, function of commercial interests. But I thought that in view of the complaints which you have been getting I should put down the full background.

Yours truly,  
S.C. Barry,  
Chairman.

June 7, 1971.

Mr. S.C. Barry,  
Chairman,  
Canadian Dairy Commission,  
2197 Riverside Drive,  
Ottawa, Ontario. K1A 0Z2.

Dear Mr. Barry:

Export Sales of Dry Skimmed Milk  
by the Canadian Dairy Commission

Thank you for your comprehensive letter of May 26 on the above-mentioned subject.

I have noted the circumstances under which you have made direct sales to Cuba, India and Mexico, and I appreciate your position in this regard.

I am pleased to have your assurance that you are not interested in becoming the exclusive exporter of Canadian dairy products nor in taking away the legitimate function of commercial interests.

Yours sincerely,

A.G. Kniewasser,  
Senior Assistant Deputy Minister,  
Industry and Trade Development.

Ronald A. Chisholm Ltd. on April 2, 1971 telexed the Honourable H.A. Olson, then Minister of Agriculture protesting the exclusion of the private sector from selling Canadian skim milk powder to Mexico and proposing to him that a delegation of three from the private sector meet with him.

Mr. Timothy Chisholm of Ronald A. Chisholm Ltd. said in respect to this subject:

"In 1971, the Canadian Dairy Commission made it virtually impossible for any private Canadian trader to export skim milk powder to CONASUPO, by itself selling powder directly to CONASUPO at a price below the then prevailing world price, notwithstanding that Ronald A. Chisholm had gone on record with representatives of the Canadian Dairy Commission to the effect that no export subsidy was required, that the private trade was well able to serve the needs of CONASUPO, and indeed that we had done so in the preceding 3 years. The Canadian Dairy Commission's decision to sell directly to CONASUPO had the direct effect of severing the mature sales arrangements which Ronald A. Chisholm Limited had had with CONASUPO during 1968, 1969 and 1970, and deprived Ronald A. Chisholm Limited of a considerable opportunity to do further large volume export business of skim milk powder to CONASUPO. This decision resulted in the loss of substantial business opportunities by Ronald A. Chisholm Limited in 1971 and the ensuing years. It was my opinion at that time, and has remained my opinion to the present, that a Crown agency such as the Canadian Dairy Commission shall assist and compliment the private sector in the effort to attract and retain export sales rather than competing directly with the private sector, since the private traders can maintain a competitive edge through their marketing knowledge and experience, and the profit incentive which is inherent in the private sector.

"I believe that this opinion is supported by the fact that in 1977 the Canadian Dairy Commission decided to return to the private

sector by appointing a Canadian agent to deal with the export of skim milk powder to CONASUPO.

"Notwithstanding my support of the Canadian Dairy Commission decision to return to the private sector, I nonetheless must express my disagreement with the decision to do so by appointing an exclusive agent. It is my belief, based upon my experience and that of my Company, that the Canadian milk producer, processor and trader are all best served by permitting the Canadian traders who are skilled and knowledgeable in international marketing to compete with each other in attempting to obtain the best price for the product which is available for export."

The Canadian Milk Powder Manufacturers Association on February 1, 1972 passed a resolution protesting direct sales of Canadian skim milk powder to CONASUPO by the Canadian Dairy Commission.

There is a substantial difference between the Canadian Dairy Commission competing with private traders, and in it using its substantial powers to exclude competition. As of 1967-1968 it began to compete. The exclusion that occurred in 1971 was not, as stated above, the result of an act by the Canadian Dairy Commission but was instead the result of a policy of the Mexican government.

As a consequence there is no basis for this allegation.

## 22. *Allegation B.2*

Allegation B.2 reads as follows:

"The C.D.C. did not favour Canadian exporters, who dealt directly with foreign purchasers, over exporters who dealt through foreign agents."

This allegation is very similar to allegation A.5(a), and in discussing this particular allegation no repetition will be made of what was said there.

Before discussing this allegation it should be noted that the Canadian Dairy Commission Act does not require the Commission to act (at public expense) in the interests of exporters, Canadian or otherwise. In any event, as to this allegation all that is being referred to here is the March 1969 telephone call made to Dr. Barry by David Schafer in Mexico, as a result of which David Schafer believed that Schafer Bros. Ltd. should have been favoured over Ronald A. Chisholm Ltd. and Thomas P. Gonzalez Ltd. in obtaining the 25,000 ton contract for the sale of skim milk powder.

The conclusion is that there is no statutory basis for the complaint. Further, it is impossible to accept David Schafer's concept of what was correct policy for the Canadian Dairy Commission in this respect.

## 23. *Allegation B.3*

Allegation B.3 reads as follows:

The C.D.C. did not offer reasonable assistance to private Canadian exporters in that:

- (a) it did not cooperate fully in making supplies of skim milk powder readily available from its stocks, and
- (b) it was inflexible with regard to the terms and conditions of financing transactions and in adjusting export subsidies."

The only evidence in respect to this allegation is evidence that has already been referred to elsewhere under other allegations.

The conclusion is that there is no basis for these allegations.

## 24. *Allegation B.4*

Allegation B.4 reads as follows:

"The C.D.C. was not sufficiently aggressive and efficient in assisting Canadian exporters, who were faced with stiff competition, to develop and maintain markets for surpluses of skim milk powder."

The only evidence in respect to this was the evidence given in connection with Allegation A.8 concerning the Philippines.

The conclusion is that there is no basis for this allegation.

## 25. *Allegation B.5 and part of Allegation B.8*

Allegation B.5 and part of Allegation B.8 are conveniently dealt with together because the evidence relating to them concerned the same incident. They read as follows:

B.5 "The criteria and process by which the C.D.C. selected exclusive agents for its foreign sales were not subjected to adequate public scrutiny";

B.8 (part)

"The C.D.C. showed preference to certain Canadian exporters of skim milk powder other than Schafer Bros. Ltd. . . by appointing them marketing agents of the C.D.C. for certain international markets..."



The subject matter of these allegations is the circumstances surrounding the appointment of Ault Foods (1975) Ltd. as agent for the Canadian Dairy Commission to sell skim milk powder to CONASUPO, which appointment was made in 1977.

The principal oral testimony relevant to these allegations was given by Messrs. Tudor Price, Gilles Choquette and Samuel Ault. In addition, three officials of the Privy Council Office testified on an aspect of the matter as referred to below.

The documents of principal relevance originated with the Canadian Dairy Commission and related to the reasons for seeking an agent, the process of selection, and the contract with the agent.

It will be convenient to summarize the evidence in point form, without at this point making any findings as to its accuracy:

1. The relationship between the Canadian Dairy Commission and CONASUPO deteriorated late in 1976 as a result of the new government being elected in Mexico. There were extensive changes in the personnel at CONASUPO with whom the Canadian Dairy Commission dealt, which not only disrupted established contacts, but which also introduced less experienced people at the CONASUPO end. One particular immediate cause for concern was that the new administration at CONASUPO regretted the purchase by CONASUPO from the Canadian Dairy Commission, in December 1976, of 14,000 metric tons of 1976 skim milk powder. (See Evidence Statement of Gilles Choquette, paragraphs 17 to 24; Canadian Dairy Commission Minute, drafted May 18 as of May 10, 1977 — Exhibit 12b, pp. 1797-99)

2. In January 1977, the Canadian Dairy Commission made an offer to CONASUPO to sell an additional 25,000 metric tons of skim milk powder to CONASUPO. Mr. Tudor Price went to Mexico in March in connection with this potential sale, and when he returned he sent a memorandum dated March 17, 1977, to G. Choquette. In that memorandum he advised that CONASUPO had just purchased 25,000 metric tons of skim milk powder (not the same order for which the Canadian Dairy Commission had submitted an offer) from the Dairy Board of the Irish Republic, and stated further as follows:

"It appears that the Irish were able to make this sale because they and, more particularly, their Mexican agent, were able to keep in far closer contact and place more pressure on the new and relatively inexperienced team at CONASUPO than C.D.C. is able to do with such a limited marketing staff and no agent in Mexico.

"Since CONASUPO is such an enormously important market for us (about 35,000 metric tons per annum) the risks of continuing to operate as we do now appear very great and the Commission may wish to consider a reinforcement of its marketing effort in Mexico through the use of agents.

"It would be contrary to the present C.D.C. policy of maintaining a viable private sector in dairy product exports for C.D.C. to hire a Mexican agent direct. The hiring of a Canadian agent on the understanding that he will concentrate his efforts in Mexico either through direct efforts or through the hiring of a Mexican sub-agent would be consistent with present policy...

"Perhaps you would be kind enough to give this matter your consideration."

(See Evidence Statement of Gilles Choquette, paragraphs 25 to 27, Memorandum, R. Tudor Price to G. Choquette, March 17, 1977 — Exhibit 103).

3. Mr. Gilles Choquette in his evidence describes the next sequence of events as follows:

"In April 1977, I went to Mexico;

"A meeting was organized with the senior Directors of CONASUPO before finalizing the sale of 25,000 metric tons of skim milk powder;

"Following my refusal to meet at the suggestion of the Mexicans with a Mr. Nordermann, who was supposed to serve as an agent for the Canadian Dairy Commission, the meeting and the sale of skim milk powder were cancelled.

"Nevertheless, I was able to meet for a few minutes with the Director General of CONASUPO who received me coldly."

4. On April 22, 1977, following his return from Mexico, Mr. G. Choquette went to see Mr. James R. Midwinter, then a senior official in the Privy Council Office. He had requested the meeting by telephone. Mr. Midwinter recorded the matters discussed at the meeting in a memorandum prepared immediately after the meeting. The salient points in this memorandum are as follows:

(a) Mr. Choquette sought the meeting "to report, in more detail, a potential impropriety in the Canadian Dairy Commission's sales arrangements in Mexico"

(b) The business between the Canadian Dairy Commission and CONASUPO in the past had been "clean", but "Now, however, individuals in, or associated

with, CONASUPO have told C.D.C. that sales should be processed through a Mexican agent to be named by them. C.D.C. is currently quoting milk powder at 16.5¢/lb. The arrangement is that they would bill at a higher price with the difference, representing about 3.5%, going to the agent for appropriate distribution. There would be a similar margin on sales of butter oil. On 25,000 tons of skim milk powder and 2,000 tons of butter oil which is currently at issue, the pay-off would be in excess of \$400,000." "(Possibly one quarter of the commission could be justified in terms of a legitimate percentage on sales, handling of documents, inspection of shipments and so forth, the rest being clearly an unearned bonus for someone.)"

- (c) Mr. Choquette reported that he had been informed in Mexico that if the Canadian Dairy Commission did not conform it would be phased out as a preferred supplier of skim milk powder.
- (d) Mr. Choquette advised Mr. Midwinter that he did not wish to have the Canadian Dairy Commission enter such an agency arrangement, but wondered about the possibility of selling to a Canadian exporter at 16.5 cents per pound "leaving it to the exporter to make his own arrangements, whatever these might be, with the Mexicans". "The firm he has in mind is Ault Foods Limited. . . Ault apparently have been selling milk products in Mexico for the last few years and a possibly plausible argument could be made that they were a more effective sales vehicle for the C.D.C. than its own employees". "Choquette would like to do business with Ault. . . If the C.D.C. did sell to or through Ault, it presumably would state in response to any inquiry that it was prepared to sell at that price to any Canadian exporter." (See: Memorandum of James R. Midwinter, April 22, 1977 — Exhibit 174A)

5. Mr. Midwinter advised Mr. Choquette, on the basis of the strictures contained in the Government Guidelines for Crown Corporations, that the Canadian Dairy Commission should not knowingly have any part of any arrangement that would result in improper payments being made in Mexico. He also recommended, by letter dated May 9, 1977 to Mr. Choquette, that if the Canadian Dairy Commission decided to use an agent in connection with its sales to CONASUPO it "should ensure that all reputable

Canadian exporters had an equal opportunity themselves to participate according to ordinary commercial practices". Mr. Midwinter concluded his letter of May 9 as follows:

"If I understood you correctly, the Commission would continue to sell directly to CONASUPO at its going export price but would engage a Canadian agency to service the business in return for a commission of the order of three per cent. Unfortunately, such an arrangement would still not place the Commission at arms-length and would not be within the guidelines unless the agency selected as the Commission's representative could account, in a proper way, for the expenses incurred in the earning of its commission. Needless to say, the Commission would have difficulty in explaining why it now needed to have an agent to conduct business which it had itself been carrying out successfully without a middleman." (See: Letter from Mr. Midwinter to Mr. Choquette, May 9, 1977 — Exhibit 176)

6. A Canadian Dairy Commission Minute dated May 10, 1977, which was actually prepared by Mr. Tudor Price on May 18, 1977, records that the Commission's major competitors in the Mexican skim milk powder import market, namely, New Zealand, Australia and Ireland, all used agents in making sales to CONASUPO and that the Canadian Dairy Commission had decided to do likewise "at least for one year". It concluded as follows:

"The Commission resolved to select the agent(s) used according to the following criteria:

- (a) The agent(s) selected shall be Canadian, or if a company or cooperative, Canadian-owned as defined in the Foreign Investment Review Act.
- (b) The agent(s) shall be experienced in the export marketing of dairy products from Canada.
- (c) The agent(s) shall have shown competence in dealing with CONASUPO, Mexico or with a similar organization in an overseas country buying dairy products from Canada.
- (d) The agent(s) shall be willing to provide the services which C.D.C. requires in its efforts to sustain and improve C.D.C.'s market share in the Mexican dairy products market.
- (e) Canadian traders shall be asked to submit in writing applications to partici-

pate and only those that do so on the time-scale requested shall be considered.

- (f) C.D.C. shall select the agent(s) on merit on the basis of the written submissions and such other interviews and discussions as the Commission may judge necessary.
- (g) The agent(s) selected shall be required to enter into a contract with C.D.C., prepared in conformity with Treasury Board guidelines for use of agents by Crown Corporations."

7. On May 11, 1977, the Canadian Dairy Commission sent identical telexes to fifteen Canadian traders, including Schafer Bros. Ltd., Ault Foods (1975) Ltd., Ronald A. Chisholm Ltd., Eastern Townships Produce Ltd., and the Granby Co-op, inviting applications for the opportunity to assist the Commission in its marketing of Canadian dairy products in Mexico. With respect to the criteria for selection, the telexes stated as follows:

"The Commission expects to select trade assistance on merit, taking into account:

A. What assistance you indicate in your written submission you can provide and

B. Experience and competence in providing such services in Mexico or similar situations involving dairy products." (See Exhibit 12, pp. 1113, 1115)

Fourteen applications were received, including applications from each of the above-named traders.

8. A Canadian Dairy Commission staff memorandum prepared on or about May 19, 1977, states that of the applicants, four met all the criteria set by the Canadian Dairy Commission: Ronald A. Chisholm, Ltd., Eastern Townships Produce Ltd., Granby Co-op and Ault Foods. Ault was stated to be recommended by the Commission staff because of its recent and close relationships with CONASUPO. (See: Exhibit 40)

9. A Canadian Dairy Commission Minute dated May 20, 1977, records that Ault Foods was selected as the Commission's agent and the other thirteen applications were refused. (See: Exhibit 12, Volume 6, p. 1155)

10. By a reporting memorandum to the Minister of Agriculture dated May 31, 1977, Gilles Choquette stated that an agent was required to meet the competition in the important Mexican market. Pertinent excerpts from that memorandum are as follows:

"New Zealand, Australia and Ireland are maintaining resident representatives who are in contact with CONASUPO. The resident agent is available at all times to recognize

opportunities and advise on the availability of product from Canada, discuss specifications and quality and other related matters, thereby facilitating maximum access for Canadian product to the Mexican market.

"The recent change in the Mexican Government has brought with it a different approach to the situation which prevailed before in which the state trading agency CONASUPO dealt directly with the Canadian Dairy Commission. The new staff in CONASUPO are not yet fully familiar with the business and depend more on agents for information....

"It is also a fact that the previous direct trading was initiated at a time when competition was less severe and there was a shortage of product on the world market.

"CONASUPO, in its letter of April 14, 1971, addressed to the Chairman of the Canadian Dairy Commission, stated its interest in direct trading with C.D.C. as follows:

'In view of the short supply of dehydrated milk existing around the globe, we are very interested in reaching Government to Government import agreements with Canada through your Commission whose legal aims coincide with Mexican law applicable to CONASUPO'

"The Commission requires assistance from an agent to give the best quality of service to its customer in respect of rapid service in dealing with quality complaints, delivery schedule, presentation of documents, rapid receiving of moneys due, and other services which are necessary to present a good image for Canadian products sold to Mexico. The Commission also needs information on pricing and activity of competitors to maximize its effectiveness. The Commission has recently experienced quality complaints from CONASUPO in respect of burnt particles in skim milk powder and excessive peroxide values in butter oil which require ongoing and daily attention to sales and service which the Commission is not equipped to supply without the services of an agent.

#### ECONOMIES ACHIEVED THROUGH THE USE OF AN AGENT

One economy is achieved through dovetailing C.D.C. purchases with shipments to Mexico. This streamlining of operations will permit shipments to be loaded directly from the first warehouse which will result in a saving of

56¢ per hundred pounds of skim milk powder or \$12.35 per M.T. On a total expected business of 30,000 M.T., this economy amounts to \$370,500. "Prompt receipt of payment due to C.D.C. which would be arranged by an agent will reduce interest costs. Based on the customary \$2,000,000 cheque, this saving is approximately \$500 per day.

"The major economy achieved through the use of an agent could be the retention of the Mexican business at current price for human use of 16.8¢ per pound rather than a price of 10¢ for feed use. On the basis of an expected volume of 30,000 M.T. (66 million pounds) this economy will amount to \$4.5 million.

"In addition, if the Mexican market should not materialize, the chances are that additional typical storage and interest charges will be incurred by the Commission. At a rate of \$3.52 per M.T. per month for storage, and \$2.86 per M.T. per month for interest (on 16.8¢ powder) a total of \$6.38 per M.T. per month will be incurred. On a volume of 30,000 M.T., this would be \$191,400 per month, and for a 6 month period the cost would amount to \$1.1 million."

11. Although negotiation of the details of the contract between the Canadian Dairy Commission and Ault Foods (1975) Ltd. took some time, and the contract was not executed until August 17, 1977, Ault Foods began serving as the Commission's agent immediately after May 20, 1977. It also began utilizing Mr. Nordermann's company, Intercontinental de Mexico, S.A., as its local Mexican agent immediately, so the agency commissions were paid on a basis which included a commission on a large sale made shortly after May 20, 1977.

12. The contract between the Canadian Dairy Commission and Ault Foods (1975) Ltd. described Ault as a "non-exclusive commercial representative". It also expressly stated that Ault was not a "legal agent" of the Canadian Dairy Commission. Ault was to provide its services only with respect to "Specified Sale Transactions", defined as being such "specific sale transactions between the C.D.C. and CONASU-PO as the C.D.C. in its discretion may expressly specify in writing". Ault was to be paid for its services at the rate of 3.326% of the value of the products delivered pursuant to Specified Sale Transactions. It was not to hire any sub-representative to carry out any of its responsibilities without the prior written authorization and consent of the Canadian Dairy Commission.

Paragraphs 7 and 8 of the contract read as follows:

"7. Ault warrants that while providing services to CDC pursuant to this Contract it:

- (a) shall not directly or indirectly take any action in connection with transactions under this Contract which violates the laws of Canada or the laws of the country in which those transactions take place;
- (b) render or accept any bribe or other improper benefit;
- (c) apply improper influence to any person or authority;

8. Ault undertakes to comply with the Policy and Guidelines concerning the commercial practices of Crown Corporations of the Government of Canada, a copy of which is attached to the present Contract as Annex 'A' and fully accepts that CDC will comply with these Policy and Guidelines as well."

The Guidelines referred to, as attached to the contract, read in part as follows:

#### "THE COMMERCIAL PRACTICES OF CROWN CORPORATIONS"

1. In the process of doing business, officials of Federal Crown corporations shall not, directly or indirectly:

(1) take any action in Canada that is not in accordance with the laws of Canada, or take any action outside Canada that violates the laws of the place where the transaction occurs, or that if taken in Canada would be in violation of the Criminal Code of Canada;

(2) render or accept any bribe or other improper benefit;

(3) apply improper influence.

2. In retaining sales and procurement agents, Crown corporations shall adhere to the following:

##### (1) Selection

Crown corporations must adopt an established selection process to ensure that the agents' qualifications for the work are clearly established and evaluated.

##### (2) Contracting

a. Agency agreements shall be formally written and shall include specific undertakings by the agents to act in accordance with the laws of the place where the transaction occurs.

- b. Remuneration under the Agreements shall be based on justifiable and sound business practice.
- c. Payments shall be strictly in accordance with the formal written agreement."

(See: Exhibit 12B, pp. 1824-32)

13. By letter dated August 22, 1977, the Canadian Dairy Commission formally approved the appointment of Intercontinental de Mexico, S.A. (Mr. Nordermann's company) by Ault Foods (1975) Ltd. as its "sub-agents" in Mexico for the purposes of the contract. (See: Exhibit 12A, p. 1641)

14. Of a total commission of \$15.20 per metric ton paid by the Canadian Dairy Commission to Ault Foods, \$13.00 was paid by Ault Foods to Intercontinental. (See: Testimony of Mr. S. Ault, Transcript p. 4197)

15. Ault Foods (1975) Ltd. served as the Canadian Dairy Commission's agent on all its sales of skim milk powder to CONASUPO until 1979, since which time the Commission has dealt directly with Intercontinental de Mexico, S.A. as its agent in Mexico. Even while Ault was serving as the Commission's agent, many of the Commission's contacts were direct with Intercontinental.

16. Messrs. Gilles Choquette, Richard Tudor Price and Samuel Ault all testified that they had no reason to believe that any improper payments were ever made in Mexico in connection with sales or potential sales by the Canadian Dairy Commission of skim milk powder to CONASUPO.

So much for the summary of the evidence without making any findings as to its accuracy.

Interviews with the Mexican witnesses, held in October 1980, provided additional information relating to the events in 1977:

- (a) The evidence given by Dr. Barry was confirmed to the effect that the Canadian Dairy Commission did not use an agent in connection with its sales to CONASUPO during the years 1971 to 1976 and that it was able to function perfectly well without an agent during this period.
- (b) Many of the new senior personnel at CONASUPO who took office in late 1976, including the Director and other officials, continued in office for about one year and a half. Apparently while they were in office, the administration of CONASUPO fell into some disarray. Great difficulties were experienced by all persons attempting to do business with

CONASUPO. Without discussing some of the reasons for this, it is sufficient to state that the Government of Mexico at that time felt compelled to, and did, replace the Director General and certain other senior officials at CONASUPO by restoring to office the previous Director General and certain other officials who had held office with CONASUPO prior to 1976. Since the restoration of these persons to office, the administration of CONASUPO vis-à-vis exporters and otherwise apparently has been satisfactory. Since 1978, certain of the more minor officials who had been in office during that one and a half year period ('76-'78) have been charged in the criminal courts in Mexico for certain acts done during their terms of office with CONASUPO.

- (c) Mr. F. Arguelles, commercial officer with the Canadian Embassy in Mexico City said that the role of agents in the sale of skim milk powder to CONASUPO had changed from the mid-1960's when the private sector competed for sales to CONASUPO. He said agents used to be more active in seeking sales and negotiating contracts than they now are. Now, the work of an agent in connection with import sales into Mexico by CONASUPO of skim milk powder is mostly in the processing of the bills of lading and other documents, and in the delivery of the product pursuant to contracts that are negotiated directly between CONASUPO and foreign government agency suppliers.

My conclusions as to the two allegations made by Schafer Bros. Ltd. regarding this matter, based on the documentary and oral evidence are as follows:

- (a) The Canadian Dairy Commission was entitled to establish the process recorded in the documents for choosing an agent, and it was not incumbent on it to inform the public of the criteria and process of selection.
- (b) Regardless of why Ault Foods (1975) Ltd. was selected, there is no evidence of improper discrimination against Schafer Bros. Ltd. on the part of the Canadian Dairy Commission in appointing Ault Foods (1975) Ltd., or of any improper preference being given Ault Foods (1975) Ltd. There is no ground for believing that Ault Foods (1975) Ltd. was an unreasonable choice from among all the applicants for the work of assist-

ing the Canadian Dairy Commission in marketing its products in Mexico. By stating the above conclusions as being the only conclusions permitted by the evidence, I do not suggest that everything about the events in 1977 was completely explained by the evidence. As to this, for example, Mr. Timothy Chisholm, the President of Ronald A. Chisholm Ltd., stated in evidence:

"... with respect to the particular selection of its exclusive agent in 1977, (Ault Foods (1975) Ltd.), I acknowledge that this company had experience in exporting ingredients for infant formula to CONASUPO, but would question the selection of this particular company to export skim milk powder to CONASUPO, since it had never had dealings with CONASUPO in this commodity in the past, and indeed had no experience in bulk exports of skim milk powder to any country. We therefore found their appointment by the Canadian Dairy Commission to be, at least, surprising, the use by Ault of a Mexican agent mystifying, and the financial arrangements between Ault and its Mexican agent even more mystifying."

As an example, the reason why the contract with Ault Foods (1975) Ltd. was structured as it was, was not fully explained, envisaging as it did the use by Ault of a Mexican agent, which Mexican agent would have no duty to account to the Canadian Dairy Commission for his costs and activities. As to this, in view of publicity in 1976 regarding certain other Crown Corporations which gave rise to the establishment of the Guidelines and to an amendment to the Criminal Code, in view of Mr. Choquette's meeting with Mr. Midwinter, and in view of the time it took to negotiate and draft the Canadian Dairy Commission's contract with Ault, one would have thought that more care would have been taken to provide for adequate controls in this contract.

Notwithstanding the above conclusions as to Allegations B.5 and B.8, it is necessary before leaving them to make these further comments:

The nature of Allegations B.5 and B.8 required that the "criteria and process" used in the selection of Ault Foods as agent be identified, and that the basis for the preference of Ault Foods be explored. The content of Mr. Midwinter's discussions with Mr. Gilles Choquette were obviously relevant for this purpose although, equally obviously, not conclusive inasmuch as they occurred prior to the dates of the Canadian Dairy Commis-

sion's documentation regarding selection of an agent.

Because Mr. Gilles Choquette denied in evidence that he had said to Mr. Midwinter the sorts of things that Mr. Midwinter recorded in his memorandum of April 22, 1977, as set out above, regarding what Mr. Choquette had been told in Mexico and regarding a preference at that time for Ault Foods, and because Mr. Choquette was quite definite in his denials on each of two separate occasions when he testified, it was necessary to hear further testimony. The purpose of such further testimony was to establish whether or not Mr. Choquette had said to Mr. Midwinter what Mr. Midwinter had recorded in his memorandum as having been said, and not to determine whether or not what was recorded was true.

As to whether or not Mr. Choquette said what Mr. Midwinter's memorandum recorded that he said, and at the request of counsel for the Canadian Dairy Commission, Mr. Midwinter was called to testify. Mr. John Tait and Mr. Steven Rosell, two other officers of the Privy Council Office who were present during different portions of the meeting between Mr. Midwinter and Mr. Choquette, were also called to testify. Mr. Midwinter reaffirmed the accuracy of his memorandum in every respect. Mr. Tait, who had been present during the first portion of the meeting had made his own notes of the portion attended by him. His notes were filed in evidence and confirmed the accuracy of the record made by Mr. Midwinter. Mr. Rosell did not make any notes of the portion of the meeting attended by him when he replaced Mr. Tait at the meeting, but he did review Mr. Midwinter's memorandum after the meeting, on the same day as the meeting, and testified that he recalled being of the view at the time that Mr. Midwinter's memorandum was accurate insofar as he could judge from the portion of the meeting attended by him.

My conclusion in respect to this further matter is that the evidence given by Mr. Midwinter, Mr. Tait and Mr. Rosell, including the notes of Mr. Tait, and also the information received from the interviews with the witnesses in Mexico City, support unequivocally the accuracy of Mr. Midwinter's memorandum and the evidence given by each of Messrs. Midwinter, Tait and Rosell. Mr. Choquette's evidence in this regard, insofar as it conflicts in any material way with the evidence given by Messrs. Midwinter, Tait and Rosell, or with Mr. Midwinter's memorandum dated April 22, 1977, is disbelieved.

This finding as to credibility is not, of course, to be taken as making a finding as to whether or not anything improper actually took place. No proof was adduced that there was any conspiracy involving any official of the Canadian Dairy Commission or any other person in Canada to commit in Canada a breach of foreign law. Nor was there any proof that the Guidelines were violated, although the contract between the Canadian Dairy Commission and Ault Foods was structured in such a way that improper payments could have been made in Mexico without the knowledge of the Canadian Dairy Commission, its officers or employees.

Finally, as to whether or not any person in Mexico breached any Mexican law in connection with any part of any sale of Canadian skim milk powder by the Canadian Dairy Commission to CONASUPO, it was understandably not within the mandate of this Commission of Inquiry to attempt to make such an investigation. In saying this, it is not to suggest, nor should one infer, that there was any proof before this Commission that any such offense did occur.

#### 26. *Allegation B.6*

Allegation B.6 reads as follows:

"The C.D.C. did not take specifications of importing countries adequately into account when adopting measures for the development of the domestic dairy industry."

The only evidence pertinent to this allegation is the evidence in respect to the 770 ton sale of skim milk powder to CONASUPO made by Schafer Bros. Ltd. in 1969 (see Allegation A.4).

As referred to above, the problem was that the Canadian Dairy Commission at that particular time did not have an adequate record system so as to be in a position to properly inform the private sector or others of its inventory characteristics so that they could be in a position to adequately satisfy the specifications of importing countries.

There was no evidence to suggest that the Canadian Dairy Commission does not continually revise its purchasing requirements and inventory records, as appears to it to be necessary from time to time in order to enable it to continue to best serve the requirements of Canada's export customers. This does not mean there might not be some time lag between identifying a new need and reflecting that new need in its procedures.

The conclusion therefore is that there is insufficient evidence to support this allegation.

#### 27. *Allegation B.7*

Allegation B.7 reads as follows:

"In 1969 the C.D.C. had in its stocks skim milk powder which contained bacteria characteristics substantially outside the C.D.C.'s own purchasing requirements."

This allegation was added at the request of counsel for Schafer Bros. Ltd., and appears to have been based largely on the bacterial characteristics of powder supplied by the Canadian Dairy Commission for Schafer Bros.' 770 ton sale to Mexico in 1969.

More time was taken in adducing evidence in respect of this allegation than was warranted. The allegation is a minor one.

The evidence adduced was inconclusive.

There was some conflict in the evidence as to the nature and purpose of the tests performed on samples of this powder on behalf of Schafer Bros. Ltd. by Mr. Henri Trochu, a chemist with Les Laboratoires Industriels et Commerciaux Limitée. The samples of skim milk powder were supplied from various warehouses in Ontario and Quebec. Mr. Trochu said that on ten occasions between February and May 1969, he analyzed a total of 86 samples of dried milk powder "in order to estimate and quantify the presence of bacteria and undenatured whey protein." The copies of his reports to Schafer Bros. Ltd. on the samples provided, appended to his evidence statement, indicate bacteria levels per gram ranging from 8,000,000 to 525,000,000.

On cross-examination by counsel for the Canadian Dairy Commission, Mr. Trochu said that the tests carried out were plate count tests, as opposed to tests for direct microscopic clump count (DMCC). A plate count measures levels of live bacteria while a DMCC measures combined levels of live and dead bacteria, and the two tests are different.

A manual entitled "Standard Methods for the Examination of Dairy Products", filed as an Exhibit by counsel for the Canadian Dairy Commission during his cross-examination of Mr. Trochu, states that "Standards for dry milks include Standard Plate Count, coliform and direct microscopic counts." (p.154) After describing the method of preparation, the manual gives the following instructions for "plating, incubating and counting plates" (pp. 155-56):

"D. Plating, incubating and counting plates:  
Incubate plates at 32°C for 48 ± 3 hours.  
Count colonies in accordance with 5.11.  
Since samples may contain appreciable numbers of aerobic spore formers, plates may contain spreading colonies that make it dif-

difficult to count colonies accurately. An overlay of 3-5 ml of sterile agar is reported to reduce the number and size of spreaders without significantly reducing the plate count. If undissolved particles of dry milk may be confused with colonies, verify identity of doubtful colonies under low power of the microscope.

**E. Reporting results:**

Report results as Standard Plate Count per gram of dry dairy product. Since determinations by the agar plate method do not reveal all the sanitary conditions of production, processing and storage, examination of samples using the direct microscopic method [14.4] and other microbiological analysis [10.3(G,H,I)] may be of value."

Immediately following, at paragraph F., are the instructions for performing a direct microscopic clump count.

**"F. Direct microscopic count:**

Because of the progressively lethal effect of processing and storage on microorganisms in dry milk, determination of the number of viable bacteria may not reliably indicate its previous sanitary quality or the sanitary handling of raw milk before drying. Direct microscopic examination of stained preparations of dry milks will give valuable additional information [14.4].

- 1) Preparing and staining films: with readily soluble samples, follow 10.3(G) (11 g of milk in a 99-ml water blank). Use a binocular microscope, 500,000-600,000 factor preferred [14.12], to count sufficient fields [14.14, 14.18] and insure proper illumination [14.11]. To avoid undissolved particles of casein in films prepared from less readily soluble samples, use 1.25% sodium citrate blanks for the 1:10 dilution. Apply the Levowitz-Weber single-solution stain [14.7]. Do not refrigerate stain, and discard it when precipitate or foreign matter appears. Make only direct microscopic clump counts [14.6], following the definition of 'clump' given in 14.18. Some cells stain poorly but must be counted if they are identifiable as microorganisms. It must be recognized that in single-sample comparisons, count differences between laboratories may be rather large.
- 2) Reporting results: Using an appropriate microscopic factor [14.12], multiply the count by 10 (to compensate for the 1:10 dilution), correct if necessary for the film

area used, and observe precautions [14.16]. Report results as Direct Microscopic Count per gram of dry milk."

Mr. Trochu said that all the results he reported to the Schafers measured live bacteria. He said that some of the higher results, such as 375,000,000 and 525,000,000 bacteria per gram were "quite high".

On cross-examination by counsel for Ronald A. Chisholm Ltd., Mr. Trochu said that a DMCC could be higher or lower than a plate count, and that, given the same sample of milk powder, the DMCC should be higher. He was not sure if the two tests could be performed on the same sample of milk, or if the sample might be destroyed in the performance of either test.

Dr. J.A. Elliott, a consultant in food microbiology, who prior to his retirement had been senior scientist with the Food Research Institute, in his evidence called into question the accuracy of Mr. Trochu's assertion that the tests he performed measured plate counts. Dr. Elliott stated that "unless a standard plate (sic) count is done very carefully by someone skilled in microbiological methods, significant errors can occur." He said further that:

"A 525 million standard plate count is typical of such products as yogurt and some buttermilk. An ordinary milk sample would have to be literally fermenting to generate a count this high."

Dr. Elliott said that in a good laboratory with competent personnel, one would expect repeatability of perhaps 20%, plus or minus 20%; however, the errors inherent in biological testing are rather large and one might meet with errors as high as 100%. He nevertheless said that he did not consider it possible to obtain plate counts as high as those reported by Mr. Trochu, which he said were typical of fermented dairy products.

On cross-examination by counsel for Schafer Bros. Ltd., Dr. Elliott said that it would be impossible to obtain Mr. Trochu's results for a standard plate count, but that they were typical of DMC counts. He said that he could, in fact, think of no other test performed on skim milk powder that would yield such results.

In any event, Mr. Trochu's confusion over what tests he did perform in itself casts doubt on the accuracy or reliability of his results.

The allegation therefore that in 1969 the Canadian Dairy Commission had in its stocks skim milk powder with bacteria characteristics substantially outside the Canadian Dairy Commission's own purchasing requirements is not proven.



## 28. *Allegation B.8*

Allegation B.8 reads as follows:

"The C.D.C. showed preference to certain Canadian exporters of skim milk powder other than Schafer Bros. Ltd. by storing surplus milk powder in these other exporters' warehouses, by naming some of them to the Consultative Committee, by appointing them marketing agents of the C.D.C. for certain international markets, and by suggesting their names as potential beneficiaries to other Canadian Government Departments and international clients."

This allegation was one of the allegations added at the commencement of the hearings at the request of counsel for Schafer Bros. Ltd.

The evidence disclosed that the Canadian Dairy Commission did store the skim milk powder which it purchased from the manufacturers in those manufacturers' warehouses. The Canadian Dairy Commission apparently had no warehouses of its own.

Schafer Bros. Ltd. was not a manufacturer of skim milk powder. It had no warehouses for such storage.

There is no evidence that the Canadian Dairy Commission showed any preference to those manufacturers who had warehouses. Some of the manufacturers also happened to be exporters besides being manufacturers of skim milk powder.

As to the Canadian Dairy Commission showing preference by naming some Canadian exporters to the Consultative Committee, the Canadian Dairy Commission had no power to name. That is the prerogative and responsibility of the Minister under Section 5 of the *Canadian Dairy Commission Act*. In any event, there is no evidence whatsoever of any preference of this nature being given on any basis other than merit.

The part of the allegation that alleges that the Canadian Dairy Commission showed preference by appointing some marketing agents to certain international markets has been dealt with in connection with Allegation A.5 in respect to the appointment of Ault Foods (1975) Ltd.

As to the part of the allegation that the Canadian Dairy Commission showed preference by suggesting the names of certain Canadian exporters as potential beneficiaries to other Canadian Government Departments and international clients, there is some evidence by way of two or three letters that the Canadian Dairy Commission in response to some international inquiries for the names of certain exporters, did send to such inquirers a restricted list of names of private Canadian exporters. This may not be a good practice, but there is no evidence to support any suggestion that the Canadian Dairy Commission showed preference in any other way or that any harm was done on these two or three occasions. This is a *de minimis* matter.

The evidence therefore is that there is no basis for this allegation.

## 29. *Part II of the Statement of Allegations*

This Part reads as follows:

"As a result of the conduct referred to in Part I, above, Schafer Bros. Ltd. suffered losses and is entitled to be compensated for those losses."

Based on the above findings as to the allegations contained in Part I of the Statement of Allegations, and also on the analysis of the claim for compensation made in Chapter V above, it is patent that Schafer Bros. Ltd. did not suffer any losses as a result of the conduct referred to in Part I and is not entitled to any compensation.