The Policy Bulletin

SUMMARY

The proposed Policy Bulletin ("the Bulletin") would rewrite U.S. law and the international agreement, specifically the Subsidies and Countervailing Measures Agreement ("SCM") of the World Trade Organization ("WTO"), which underlies the U.S. statute. Its adoption as legal authority would ignore final decisions of two different WTO panels. It would establish legal requirements for Canadian provinces that do not exist in the law and, because of its unique application to softwood lumber from Canada, would not apply to any other products from any other countries. It thus would also create a parallel legal regime to the law as otherwise written, while creating a precedent for the Department of Commerce ("the Department") to use policy bulletins as a technique for unilaterally, and without Congress, rewriting the law and creating special bodies of law for specific products from specific countries.

The Bulletin states in its "Summary" that it is providing an "incentive for Canadian provinces to move to market-based systems of timber sales." This statement is an assumption, that Canadian provinces do not now operate market-based systems. This assumption is being contested before panels of the WTO and the North American Free Trade Agreement ("NAFTA").

Later in the Bulletin (at I.A.2), the Department states, "[D]ownstream product markets [that] drive the actual demand." The stumpage system in Ontario, for example, is tied directly to the prices in downstream markets. By contrast, there are no known stumpage systems on public land in the United States that are connected in any way whatsoever to downstream product markets. Hence, the assumption in the Bulletin

Summary, which pervades the entire Bulletin, is not only contradicted in the body of the Bulletin: it is contrary to public timber systems in the United States.

PURPOSE OF THE POLICY BULLETIN

Summary Of The Comment

The Bulletin attempts to perpetuate the myth that "adequate remuneration" means "fair market value," despite two WTO panels that already have found the Department's substitution in the softwood lumber case of "fair market value" for "adequate remuneration" to be contrary to U.S. obligations under the SCM Agreement.

Comment

The Bulletin addresses directly issues argued unsuccessfully by the United States at the WTO, and attempts to undo those results by rewriting the SCM. It begins with the key term of the SCM in Article 14(d), which is the same term in U.S. law at section 771(5)(E)(iv), "adequate remuneration." The United States argued at length before two different WTO panels that "adequate remuneration" means "fair market value," and the Bulletin begins with this proposition: "The Department interprets the term 'adequate remuneration,' as used in section 771(5)(E)(iv), to mean fair market value." "Adequate remuneration" does not mean "fair market value," and the Department is well aware that WTO panels have expressly rejected the Department's interpretation.

The WTO panel went beyond declaring definitively that "adequate remuneration" does not mean "fair market value," but the Bulletin would impose a contrary interpretation. The second sentence in "Purpose Of The Policy Bulletin" declares, "The term 'adequate remuneration' is not defined in the statute," which is the premise for offering Commerce's own interpretation as "fair market value." The WTO panel, however, concluded that the term "adequate remuneration" has a plain meaning.

"We find that the text of Article 14(d) SCM Agreement is very clear: the adequacy of remuneration is to be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase. . . . The ordinary meaning of the term 'prevailing' market conditions is the market conditions '*as they exist'* or 'which are '*predominant*.'"[1] Hence, "adequate remuneration" is not an undefined term that Commerce is free to "interpret." It does not mean "fair market value."

The entire Policy Bulletin depends on making "adequate remuneration" mean "fair market value." All of the propositions that follow thus are constructed on a premise that is contrary to the international obligations of the United States. The premise, moreover, is that Canadian softwood lumber producers should satisfy a standard that is not required by U.S. law, and not required by the WTO. Instead, the standard to be memorialized in the Bulletin is the standard Commerce has failed to advance successfully before appellate tribunals and hence would be applicable uniquely to Canadian softwood lumber.

[1] *United States-Preliminary Determinations with Respect to Certain Softwood Lumber from Canada, Report of the WTO Panel,* WT/DS236/R, paras. 7.44 and 7.50 (Sep. 27, 2002) (emphases in original). According to press reports, the WTO's panel decision on the final determination, to be published in August 2003, takes a similar view to that of the prior panel.

GENERAL STATEMENT OF POLICY

Summary Of The Comment

The Bulletin sets up a two part test in which a province fully implements reforms required by the Bulletin, but may then have to wait years for the effects of those reforms to be apparent and for the Department, at its sole discretion, to determine whether the effects are good enough for revocation of the countervailing duty order. The "no new subsidies" language in the Bulletin improperly imports into a changed circumstances review an examination that is the proper subject of an administrative review. And the Bulletin's policy provides for revocation of the countervailing duty order as to individual provinces as and when they satisfactorily complete changed circumstances reviews, yet the order applies to all of Canada (except the Atlantic Provinces), without comment as to how, in accordance with the law, revocation for individual provinces is to be accomplished.

Comment

Provincial governments may escape the countervailing duty order through changed circumstances reviews only when they can satisfy the Department that they (a) have enacted reforms that satisfy the Bulletin's standards, and (b) that their timber sales systems "charge[s] adequate remuneration." These requirements mean that provincial governments must meet a standard not to be found in the law for adequate remuneration, and they must accept that their stumpage systems are not "market-based," even when they may be. Provincial systems whose prices are driven by downstream markets are more market-based than any government timber sales

systems in the United States, yet apparently do not satisfy the requirements of the Bulletin.

The General Statement Of Policy also requires provincial governments to have fully implemented reforms, and to have installed systems that demonstrably yield "fair market value" for stumpage. Hence, the countervailing duty order will not be revoked for a province unless and until the province can demonstrate that the effects of its reforms satisfy Commerce by yielding prices that Commerce considers fair market value.

The inclusion of an effects test (Commerce will determine whether the reformed provincial system does "charge" adequate remuneration) entrusts extraordinary discretion to Commerce, which can decide without guiding definitions or terms that prices simply are not high enough because they do not represent fair market value. It also means that no province can reasonably expect to conclude a changed circumstances review satisfactorily in the near term because full implementation and testing of reforms and systemic change will be prerequisites to the legal process.

The countervailing duty order currently applies to "Canada," although it conspicuously excludes all of Canada east of Québec. The Bulletin provides for revocation of the order for each province, and makes no mention of revocation for all of Canada. The Department needs to clarify when and whether the countervailing duty order is to be revoked for all of Canada, and under what terms or conditions it may be revoked for particular provinces. The Department must further clarify how the statute and regulations will apply to provincially-based revocation.

The General Statement Of Policy concludes with a footnote: "Revocation is also contingent on the absence of any other countervailable subsidies (above *de minimis* in the aggregate), whether such subsidies are new or preexisting." This contingency is contrary to law and the Department's practice. New subsidies are not the proper subject of a changed circumstances review, which is a review of the determination, 19 U.S.C. § 1675 (b), unlike an administrative review, which is to "review and determine the amount of any net countervailable subsidy." 19 U.S.C. § 1675 (a)(1)(A). New subsidy allegations therefore are properly the subject of an administrative review, but not a changed circumstances review.

By introducing this proposal, making revocation of the countervailing duty order expressly contingent upon a finding of no new countervailable subsidies, the Bulletin expands the changed circumstances review beyond its legal limitations and adds an important element of uncertainty to the process. No matter what a provincial government may have done consistent with the requirements of the Bulletin, it may find itself subject to a new and unexpected investigation before finding a way out of the countervailing duty order.

I. Standard for a Market-Based Timber Sales System

Summary Of The Comment

The Bulletin's unqualified command for provincial governments to eliminate all practices and policies that "inhibit the ability of lumber producers to respond to changes in the market" is overbroad and makes no allowance for public purposes, such as environmental, public health and safety, or labor regulations. The Bulletin also creates standards of "independent functioning" markets and "artificial constraints" that, were they enforced literally, could never be met in the real world.

Comment

The summary statement in the first paragraph of this section of the Bulletin repeats the assumption that there are "practices and policies" in every province that "inhibit the ability of lumber producers to respond to changes in the market," and that they must be "eliminated." Even were the assumption correct, the command for elimination of all such practices and policies is without qualification. The requirement makes no allowance for public purpose. An environmental restriction inhibiting free competition to buy and cut down trees, for example, would be impermissible under these terms, as would safety and labor regulations limiting the number of hours mill workers can work in a day. The Department would be free in a changed circumstances review to find that such restrictions render a provincial stumpage system not sufficiently "market-based" to qualify for revocation of the countervailing duty order.

The second paragraph of the summary statement introduces terms that, again, Commerce would control. They are "open," "competitive," "independently functioning," and "artificial constraints."

The most troubling of these terms are "independently functioning" and "artificial constraints." There is no such thing as an "independently functioning" market when more than one market sells the identical product within geographic proximity, and there is considerable attention devoted in the Bulletin to open and competitive markets requiring transparency and "adequate public information." When information is readily available in different markets for the same product, the information in one inevitably will influence conduct in the other. The markets then cannot function "independently" of one another. By creating this requirement, the Bulletin sets an unattainable standard, and the Department retains discretion to judge when and whether a reference market is functioning independently according to unspecified criteria.

"Artificial constraints," the second especially troubling term, seems to refer to public policy. For natural resources, there likely is no example in North America where there are no "artificial constraints," no public policies limiting the flexibility of companies to respond freely to all market signals. For example, an environmental regulation that limits harvesting in ecologically sensitive areas, or during certain times of the year, could be considered an "artificial constraint" preventing a timber company from harvesting more in response to market signals.

The deployment of these terms as conditions to be satisfied by Canadian provinces has two fundamental consequences: they set standards that are facially unattainable, and they confer extraordinary discretion on the Department. The Bulletin thus does not create a road map with clearly-defined exits.

The remainder of Section I, which will be examined in each of its subheadings, hypothesizes a perfect and fictitious market where buyers and sellers all

operate with complete information, sellers lack market power to set prices and buyers lack market power to control or drive prices down. There are always numerous buyers and sellers. Such a market does not exist in the United States, nor anywhere else, but it is the market that the Department would require of Canadian provinces in order to satisfy legal requirements and prove that transactions are otherwise not subsidized or "constrained".

I.A. Policies and Practices That Inhibit Market Response

Summary Of The Comment

The Bulletin requires provinces to remove all regulations that might interfere with a lumber producer's ability to respond to changes in the market. Such a requirement converts a public resource to be managed for the benefit of all the people, including the environment, into a private preserve to be exploited by single interests. The United States is asking of Canada what it has never asked or required of itself.

Comment

The Bulletin would create in Canada what does not exist in the United States. Public forests in the United States, which the Bulletin later suggests can be the source of reference prices for Canadian public stumpage because they supposedly satisfy the criteria for "market-based timber systems," are always subject to regulations ("government practices") "that limit the operation of market forces and interfere with an industry participant's ability to respond freely to changes in the marketplace." Were there no such restraints, there would likely be no forests. Whether it was the Clinton Administration restricting road construction (an unfettered industry participant would pave when and where needed to access trees of preferred species and size according to market demand), or the Bush Administration licensing extra cutting to reduce forest fires (an unfettered industry participant might forego cutting were the demand not sufficient, but may well cut extra in response to an expansion of inexpensive supply), public policy is as prominent in the United States as in Canada in impacting private sector decisions in the marketplace.

This section of the Bulletin requires reform to "remove[s] the current constraints on a lumber producer's ability to respond to changes in the market." The Bulletin thus requires Canadian governments to abandon regulation of the natural resource of trees in favor of a single interest, the lumber industry. This requirement cannot be met fully anywhere in Canada, and has never been approximated in the United States.

I.A.2. Minimum Cut Requirements

Summary Of The Comment

No provincial government imposes or enforces minimum cut requirements. The current Ontario system reflects demand for downstream products, unlike auctions on U.S. public lands.

Comment

The Bulletin presumes that tenure holders in Canada are either forced to act in response to minimum cut requirements, or perceive that they are so obliged. Yet, as Canada explained to a WTO Panel, none of the provincial governments imposes or enforces minimum cut requirements. [1]

More important in this paragraph is the concession that downstream product markets drive actual demand for timber on the stump. The record of the investigation shows that auctions on U.S. public lands take no account at all of downstream products in setting "reservation" prices.[2] By contrast, Ontario's stumpage system is based expressly on the market prices and demand for downstream products. Yet, the Bulletin calls upon Ontario to abandon this system of pricing, and to replace it

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[1] Paragraph 7.15 of the WTO Panel report states:

> Canada further acknowledges that the tenure agreements contain various processing requirements as well as certain minimum and maximum cut requirements. For example, tenure agreements in Alberta, Ontario and Québec contain maximum cut limits. According to Canada, Ontario and Québec have no minimum cut requirements. Canada further asserts that some of Alberta's tenures also contain minimum cut requirements, but that they are not enforced. In British Columbia, licensees under certain designated types of tenures are subject to minimum cut requirements, which require the harvester to harvest plus or minus 50 per cent of the annual allowable cut for that licensee in any given year, and plus or minus 10 per cent over a five year period.

United States—Preliminary Determinations with Respect to Certain Softwood Lumber from Canada, Report of the WTO Panel, WT/DS236/R, para. 7.15 (Sep. 27, 2002).

[2] *See* Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 28, 2001) at attachments 3 and 4, P.R. Doc. 629.

with a system that references U.S. prices, the very prices that are unrelated to downstream product markets.

I.A.4. Minimum Processing Requirements

Summary Of The Comment

The obligation on tenure holders to process, or to have processed, what they cut protects markets from oversupply. Elimination of such requirements could have exactly the opposite effect of that intended by the Bulletin.

Comment

Provincial governments may impose minimum processing requirements for conservation, to assure that a tenure holder does not cut timber without commitments to use it. The alternative "free market" solution could encourage serious overcutting and oversupply of cut timber by encouraging companies to cut more than they need because of convenience by season, or availability of equipment, or a depressed timber market. The obligation to process, or to have processed, what they cut, places a control on the potential incentive to flood the market with cut timber.

The Department's description of minimum processing requirements, and the inherent assumption about constraining market forces, misreads history and public policy imperatives. The Department is demanding the elimination of a regulation that, at least in some instances, may be protecting markets from oversupply. Consequently, elimination of such requirements could have exactly the opposite effect intended and declared by the Bulletin, because these requirements may "reinforce the normal operation of supply and demand."

I.A.5. Long-term, Non-Transferable Tenure

Summary of The Comment

Long-term tenures enable governments to impose upon private industry obligations to maintain and preserve the forest for public use. On U.S. public lands, government pays these costs. Any adjustment for security of supply must also take into account the costs of fulfilling public obligations that long-term tenures allow provincial governments to impose on tenure holders.

Comment

Long-term non-transferable tenures guarantee government control, consistent with government ownership, of public forests. They enable governments to impose upon private industry obligations to maintain and preserve the forests for public use, at private expense. Without such arrangements, the cost of preserving public forests would fall entirely upon the taxpayer, as in the United States. In the United States, the costs of fire and disease protection, planning, reforestation and silviculture more generally all fall upon the United States Forest Service or the forest services in the several states and many counties and municipalities. In Canada, private enterprise bears these costs.

Most of the forests in the United States are in private hands. There is no more secure supply than direct ownership. The largest private owners, moreover, lease lands on long-term arrangements. That these leases are private means only that they may not be subject to strict regulation and provide no assurance that the forests are being preserved for the public good. They still provide security of supply.

The Bulletin treats Canada's public ownership of forests, and the consequent long-term tenures that enable the public to impose the costs of the forests on the private sector, as a serious market impediment. It pays no attention to public policy, regulation, and typical government practices in the United States (to subsidize the U.S. forest products industries by having the public pay directly for roads, fire and disease protection, planning and silviculture). And the Bulletin presumes that the Canadian practice of shifting the costs of the forests onto the private sector in exchange for some security of supply "undermine[s] the overall operation of market forces," while the public provision of services – replacing the market outright – is benign.

The conclusion drawn in this section of the Bulletin betrays an intent incompatible with a mission of a long-term durable solution to conflict over softwood lumber between Canada and the United States. The Bulletin concludes that, "Adjustments to the observed prices may be required to take into account the differences in the attributes of sales in the independently functioning market and long-term, non-transferable arrangements on provincial lands, including the security of supply associated with a (sic) long-term, non-transferable tenures on the administered portion of a province's harvest." There is no hint that any "adjustment" might need to go the other way, accounting for the differences between what tenure holders in Canada must pay to satisfy their public obligations, contrasted with the costs borne by governments on public lands in the United States.

I.B. Market-Based Pricing

Summary Of The Comment

U.S. public forests could not meet the standards the Department seeks to impose on Canada.

Comment

The Bulletin presumes that "auctions" necessarily constitute "free and open competition," yet goes on to impose numerous conditions on auctions, recognizing that not all auctions meet this criterion. The core difficulty with the presumption is that the conditions the Department wants to impose are an apparent response to the known weaknesses and inadequacies of timber auctions on public lands in the United States.[1] Hence, again, the Department wants Canada to meet standards that are not met in the United States.

[1] *See* Case Brief of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association, NAFTA USA-CDA-2002-1904-03 at 6-21 (Aug. 2, 2002); *see also* "Forest Service: Barriers to Generating Revenue or Reducing Costs," *GAO Chapter Report*, (GAO/RCED 98-58, Feb. 13, 1998) at 5, (submitted as attachment 3 to Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 31, 2001), P.R. Doc. 628).

I.B.1. Reference Prices

Summary Of The Comment

The Bulletin recognizes that private timber markets within a province are a proper source of reference prices. However, the Department must eliminate the fiction of a "causal link" for the Bulletin, which appears designed to limit private market prices to Québec.

Comment

The central difficulty in the Department's notion of "reference prices" is the reliance on "independently functioning markets." First, there is the contradiction between a preference for timber markets and the concession that the markets determining demand are downstream product markets, not timber markets at all. Second, there is the notion that reference prices can emerge from markets whose supply, demand, and price have no effect on one another for the same goods. Third, the Department repeats the assumption that "open and competitive auctions" are necessarily the source of "fair market value" results. Still, and with all those problems arising from the two sentences of the first paragraph, there is also an acknowledgment that reference prices may come from "robust and competitive markets for the sale of standing timber or logs harvested from private lands within the province." As the WTO panel recited, such conditions may be found in every province in Canada, [1] and are especially strong throughout eastern Canada, including the Atlantic Provinces, Ontario and Québec.

[1] *United States-Preliminary Determinations with Respect to Certain Softwood Lumber from Canada, Report of the WTO Panel,* WT/DS236/R, paras. 7.54, 7.56 (Sep. 27, 2002).

The Department amplifies support for domestic provincial private markets in the subsequent paragraph. It endorses the proposition that market size does not matter, which was the core point made by Ontario during the investigation.[2] It promises to apply a "rule of reason," which should make at least the Ontario and Québec private markets more than acceptable for reference prices. Both establish "fair market prices," but neither is wholly independent of all other markets. To the contrary, they necessarily interact, particularly within their own jurisdictions, with provincial stumpage. It should not, and could not, be otherwise as long as there is the information flow the Bulletin elsewhere demands.

The Department also in this section promotes the utility of domestic private market benchmarks within Canadian provinces provided they reform practices and policies that may impede market responsiveness. Canadian provincial governments, especially Ontario and Québec, must take this proposition to mean that the implementation of reforms on appurtenancy, minimum cut requirements, mill closure restrictions, and minimum processing requirements must make their private markets more than merely eligible as the sources of reference prices for crown stumpage.

The Department must rethink its approach to some of these requirements because the Bulletin does not account accurately for their effects. In addition, they are catalogued because of an assumption about their application in Canada. Minimum cut requirements are nowhere enforced; minimum processing requirements have an

[2] *See* Charles River Associates, *An Analysis of the Appropriateness of Relying on Ontario's Private Timber Studies*, Case No. C-122-839, at 8-9 ("CRA Study") (submitted as volume 3 of supplemental questionnaire response of Government of Ontario, Case No. C-122-839, (Dec. 17, 2001), P.R. Doc. 602; *see also* Case Brief of the Government of Ontario, Case No. C-122-839 at 13-19 (Feb. 25, 2002), P.R. Doc. 772.

important conservation value and may limit potential oversupply; and long-term tenures do not require adjustments, unless similar but opposite adjustments were made for the public expenditures supporting private forestry activities in the United States. Nevertheless, in all the Department is committing in this section to embrace domestic private markets within provincial jurisdictions provided policies and practices that may impede market responsiveness are addressed and reformed.

The Department has created in this section a fiction about a "causal link" that appears designed to limit to Québec the use of a private market for reference prices. Québec's stumpage system requires tenure holders to shop for stumpage first in the private market, and to use crown stumpage only after the availability of private resources is exhausted. This relationship is, by definition, not functioning independently. To the contrary, the private market is positioned by law to hold tenure holders hostage for inflated prices, but for prices not inflated so much as to put the entire supply required by a mill out of reach. Thus, the private seller of stumpage is acutely aware of what a tenure holder might have to pay, and can afford, for crown stumpage, and prices his private stumpage accordingly. The public price is then designed, with adjustments, to match the private price.

Theoretically, the "causal link" in Ontario is in reverse. The private Ontario market is a "marginal" market because lumber producers seek it out when they need additional supply.[3] For this additional supply, they typically pay more than they pay the crown, although over the course of a year the prices generally equilibrate.[4]

[3] *See* CRA Study at 5.

[4] *See id.* at 5-6.

Consequently, the price outcomes in Ontario and Québec are the same, even as the "causal link" runs in opposite directions, rendering the concept meaningless.

The "causal link" cannot be a reasonable criterion for judging whether viable, robust private markets operate within jurisdictions and can supply reference prices for crown stumpage. Private and public markets within jurisdictions can never function "independently" of one another. But such private markets do operate as markets, and do produce market prices.

I.B.1.a. Number of Participants in the Reference Market

Summary Of The Comment

The Department should remove from the Bulletin the arbitrary requirement that producers who source "virtually all" of their timber from crown tenure cannot be considered as participants in the private market. The inclusion of such private market participants would in no way invalidate the private markets. Their exclusion, by contrast, appears designed to prevent private markets in most provinces from being used for reference prices in contravention of U.S. obligations under the SCM Agreement.

Comment

The premise here is the view of conventional economics: a functioning market is one where no single actor or group of actors has "market power" sufficient to influence sales prices. The Bulletin also recognizes that there is no reliable or consistent way to assure, for any given transaction, that no such market power will be exercised. So, the Bulletin requires only that the market be "contestable," open to willing participants. Yet, the Bulletin then adds a qualification that cannot possibly succeed anywhere in Canada without a radical change in crown ownership (or without acceptance of the misleading theories about auctions).

The Bulletin posits that producers who source "all" or "virtually all" of their wood fiber from crown tenure cannot be considered as participants in the private market. There is no reasoning offered, merely a repetition of the theory that to be counted a private market participant "a sizable share of the furnish for their mills" must come from private sources.

There are several problems with this theory. Across Canada, most timber (ninety percent or more) is in crown hands and will remain that way for the foreseeable future. Necessarily, major producers will purchase most of their timber from the primary owner. A market of small producers, which is what the rule in this section seems to require, will not fairly translate prices for a market of large producers, and exclusion of the major producers will also narrow significantly the field in the private market itself because they typically are significant participants in the private market. Their engagement in the private market in no way invalidates the private market's viability, except in the view of the Bulletin.

The language here, as elsewhere in the Bulletin, is also slippery. In the course of a single paragraph, qualifying participants in the private market should not source "all," "virtually all," or a "sizable share" of the furnish for their mills. How much any of these measures may be is left to the Department's discretion.

This qualification is pernicious because it seems arbitrarily designed to make private markets in the provinces largely unavailable as reference markets. A large lumber producer may routinely participate in the private market as a precondition for obtaining crown timber (Québec), or as marginal but essential supply because of a shortage of crown timber (Ontario). Neither condition erodes in any way the fact that the large producer is competing with other producers, large and small, for private timber. The market is no less "contestable" because producers obtaining most of their timber from crown tenures participate.

The Bulletin asserts that market participants obtaining most of their timber from private sources constitute "stronger [] evidence that the reference market is open,

competitive and functioning independently of the administered portion of a province's harvest and would, as a consequence, serve as an adequate reference point for assessing stumpage on provincial lands." Yet, whether private timber is purchased as a precondition or as marginal supply should make no difference. Both purchases are inevitably in reference to the "administered portion" of the harvest, as any markets for the same goods, anywhere, are influenced to some degree by each other. Still, both involve purchases in competitive markets.

The difficulty here, as elsewhere in the Bulletin, is in the creation of artificial and abstract criteria that have connection neither to the law nor to reality. Markets do not function as the Bulletin would like to have them function, and the Bulletin would like to make the Canadian softwood lumber industry an exemplar of markets that otherwise do not exist for any products, anywhere, when there is some government ownership of a good.

Inherent in the Bulletin's ideology, nowhere more apparent than in this section, is the desire to overcome the legal agreements of signatories to the Uruguay Round by creating exaggerated and artificial standards. As the WTO Panel in this very case observed, the U.S. pursuit of a "theoretical market free of government interference," may be admirable as economic theory, but it is not the standard of the world order.[1] The law provides that "the only qualifier used to the 'market conditions' in question is that they be 'prevailing.'"[2] Regrettably the Department is trying to use

[1] *United States-Preliminary Determinations with Respect to Certain Softwood Lumber from Canada, Report of the WTO Panel,* WT/DS236/R, para. 7.50 (Sep. 27, 2002).

[2] *Id.*

negotiations with Canada, outside the multilateral forum that produced the rules it does not like, to create a new and unique standard.

I.B.1.b. Quality of Information

Summary Of The Comment

The quality of information from U.S. public forests that the Department used in the lumber investigation suffered from serious defects. The Bulletin should not impose obligations on Canadian private markets, in order for those private markets to be used as reference prices, that cannot be met in the United States.

Comment

Very conspicuously, in the *Lumber IV* investigation, the Department made almost no comparisons of Canadian crown stumpage to private timber prices or transactions in the United States.[1] Even as the Department pledged in its preliminary determination that it would continue to seek private transactional prices,[2] the final determination remained without them.

The market for standing timber in the United States is predominantly private. The largest producers own their own timber and do not have to buy much, but nevertheless there is substantial private buying and selling.

Private parties transacting timber in the United States apparently do not like making prices public. They prefer to keep private transactions private.

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[1] Some Maine prices were used, but the Maine sellers themselves reported to Commerce, on the record, that their private prices were "not a pricing tool" and were "not used as one by private landowners in Maine." Letter from Maine Forest Service, Department of Conservation to Department of Commerce (Dec. 20, 2001) (attachment to Letter from Melissa Skinner to all interested parties, Case No. C-122-839 (Feb. 20, 2002)), P.R. Doc. 752.

[2] "Although we maintain that stumpage rates from state lands are an appropriate benchmark under these circumstances, we intend to continue examining sources for timber prices from private lands in the United States for use in the final determination." *Notice of Preliminary Affirmative Countervailing Duty Determination, Preliminary Affirmative Critical Circumstances Determination, and Alignment of Final Countervailing Duty Determination With Final Antidumping Duty Determination: Certain Softwood Lumber Products From Canada*, 66 FR 43186, at 43196 (Aug. 17, 2001).

Consequently, despite pretensions that it was using U.S. prices instead of Canadian prices because it requires the prices of commercial markets undistorted by government participation in the market, the Department used for its final determination in this case government prices from government sales of government-owned timber.

The quality of the information from U.S. government sales of standing timber is known to be seriously flawed, and its application for comparisons to Canadian public stumpage even more so.[3] The U.S. data tend to be dated; sales dates do not correspond to harvesting dates; no downstream market signals are involved; there is no public information about any particular transactions (hence there is no systematic information on U.S. auctions as to numbers of bidders, reservation prices, dissemination of information about species and prices prior to auction). There are profound disagreements over appropriate conversion factors for U.S. and Canadian measurements of fiber quantity, and no agreement of any kind for qualitative comparisons, arising especially from the lack of information about U.S. auctions and sales.

Despite this paucity of information in the United States, and especially the absence of data for the private transactions that dominate the market, the Bulletin calls on Canadians keen to use private market benchmarks to produce near-perfect information, and even suggests how – "internet pages, trade publications, or other similar sources of public information." Where private American buyers and sellers would (and do) keep the information on their transactions secret, Canadians are to socialize all information: "it would be particularly important for any private owner of

[3] *See e.g.*, Case Brief of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association, NAFTA USA-CDA-2002-1904-03 at 6-21 (Aug. 2, 2002).

standing timber to have access to current information on prices others are receiving or similar stands in assessing the amount he or she intends to charge." This statement undoubtedly is true, no less so in the United States than in Canada. But whereas this standard is neither required nor met in the United States, the Bulletin would make it required in Canada.

There are trade publications in the United States that estimate prices as trendlines based on periodic telephone samples. There is no reason why Canadians should be required to exceed this standard of information in making their private markets viable benchmarks for public prices.

The Bulletin calls for a "reservation price" for Canadian private transactions, even as there is none in the public U.S. transactions the Department relied upon in the investigation and proposes elsewhere in the Bulletin to rely upon in the future.

Neither Canadians nor Americans sell timber "blind," without making stands of trees for sale available for inspection. The Bulletin's promise, therefore, that "the Department will examine whether potential buyers in the reference market have the opportunity to survey the timber or there are commercial services available that will survey the timber" is a condition of no particular consequence.

I.B.1.c. Direction of the Causal Link

Summary Of The Comment

It does not matter whether a buyer in the private market has entered the private market before, at the same time or after seeking supply from the public forests. The appropriate test is set forth in the following example from the Bulletin: “firms or individuals with significant long term tenures” should not be permitted to exercise market power. In the applicable pricing model to convert private market prices into public stumpage, such tenure holders “cannot artificially force down prices in the private market to lower stumpage charged on the administered portion of the harvest.”

Comment

This section of the Bulletin appears to be invented in order to limit acceptance of domestic private markets in Canada as benchmarks to Québec. Even Québec, however, could not meet the standard: “The province must demonstrate that the prices established in the reference market are determined independently (*i.e.*, independent of any influence from distortions associated with provincial administered timber policies or the effects from pricing of stumpage on long-term tenures on provincial land).” In Québec, tenure holders must first exhaust private supplies before they can harvest crown stumpage. The prices that emerge from these transactions then set the adjusted public prices. However, no private seller is ignorant of the public, published price from the prior year, nor is he ignorant of the overall market demand. Therefore, even as he may to a limited degree hold a buyer hostage to a price, he is bounded by reasonable expectations of what the buyer is willing and able to pay the crown. There can be no complete independence of the markets.

This condition applies equally to purchasers of all the furnish for their mills, or only a small proportion. Both, in the end, must balance what they can pay for raw material, whatever the source, with what the downstream market will pay back.

For a similar reason, it matters not whether the buyer is being held hostage on the front end because he cannot access crown stumpage before exhausting private sources of timber, or on the back end because the additional timber may make the decisive difference in producing enough volume for profit. All potential sources of supply influence the price for all potential sources of supply. Consequently, the grand invention of this section of the Bulletin is unsound economically: "More to the point, in any attempt to translate prices established in an independently functioning market to stumpage charged on the administered portion of a province's timber, the Department will want to ensure that it is the prices found in private or otherwise independently functioning markets that is dictating the prices on the administered portion of the harvest (*i.e.,* that causality runs from auction sales or private markets to administered sales), rather than the reverse." The use of "independently functioning markets" twice in the same sentence betrays the problem: no matter how many times the phrase is used, it cannot acquire more meaning.

The example following the theory in this section is much less ambitious than the theory itself. It requires only that "firms or individuals with significant long term tenures" should not be permitted to exercise market power, and that, in the applicable pricing model to convert private market prices into public stumpage, such tenure holders "cannot artificially force down prices in the private market to lower stumpage charged on the administered portion of the harvest." This is an unobjectionable description of a

functioning market. Were it meant to qualify the theory that precedes it, it would present no peculiar problem for the use of private markets as benchmarks and would effectively remove the otherwise apparently intended bias. The Department needs to clarify that the example, not the "theory," governs this section, and that the concern is about market power, not a "causal link" or direction..

I.B.1.d. Barriers to Entry or Exit in the Market

Summary Of The Comment

The Department should clarify that this section applies to trade in logs from private lands, not public lands. Were this section to apply to logs from public lands, the U.S. public lands that the Bulletin proposes for reference prices also would be invalid under this section.

Comment

The Department should clarify its intentions in this section. It appears that the section addresses international trade in logs from private lands, but not public, and objects to mill ownership requirements for bidding on private timber, but not public. An attempt to make these propositions applicable to crown timber would run afoul of the WTO's conclusions about log export restrictions,[1] and of provincial conservation policies. Limitation to "the market to be used as a reference point" generally would avoid these problems.

Notably, there are log export restrictions on most of the public lands in the United States that a section of the Bulletin proposes as options for reference markets. The Department should also clarify, therefore, whether its proposed use of U.S. public lands as reference markets requires the elimination of log export restrictions on those lands.

[1] *United States - Measures Treating Export Restraints as Subsidies, Report of the WTO Panel*, WT/DS194/R (Aug. 28, 2001).

I.B.1.e. Safeguards Against Collusive Behavior

Summary Of The Comment

The Bulletin should not seek to impose an obligation upon Canadians regarding collusive behavior that is not met in the United States.

Comment

Collusive and uncompetitive behavior in U.S. auctions is well known,[1] which presumably is why the Bulletin is preoccupied with preventing it in Canada. The Bulletin calls upon Canadians to guarantee, through law and enforcement, that Canadian private markets, and especially auctions, will be free of such collusion. Again, the standard for Canadian conduct should not exceed the standard in the United States.

[1] Oral bids continue for single-bidder U.S.F.S. timber sales despite the potential for collusion and despite GAO recommendations for sealed written bids. *See* "Forest Service: Barriers to Generating Revenue or Reducing Costs," *GAO Chapter Report*, (GAO/RCED 98-58, Feb. 13, 1998) at 44 (submitted as attachment 3 to Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 31, 2001), P.R. Doc. 628). Testimony at a House of Representatives Committee hearing in 1992, noted that the U.S.F.S. timber sale appraisal method "encourages bidders to skew their bids, particularly in situations where the higher value species is actually under-priced, to avoid paying the real value for the sale." *Review of the Forest Service's Timber Sales Program: Hearing Before the Environment, Energy, and Natural Resources Subcommittee of the Committee on Government Operations, House of Representatives*, 102d Cong. 2d Sess. 33 (1992) at 34.

I.B.2.a. Transparency in the Functioning of the Market Used as a Reference Point for Market Prices

Summary Of The Comment

The Department should not demand a standard of transparency from Canadians that does not exist in the United States.

Comment

The central proposition of this section does not appear to be materially different from the prior discussion regarding the **quality of information**. It is unobjectionable, except for the double standard it demands when declaring what the Department will require of Canadians. This time, the Bulletin specifically demands that "information about individual transactions is accurately reported and publicly available," which is exactly what, as the Department well knows from its own investigation, does not exist in the United States.

I.B.2.b. Application of Prices Observed in Independently Functioning Markets to Stumpage Set on the Administered Portion of a Province's Harvest

Summary Of The Comment

This section points out a serious flaw in the use of U.S. pricing data – the inability to verify. The Department needs to confirm, therefore, that in this section it is not trying to set, yet again, an impossibly high standard where sufficient information is unobtainable and therefore no satisfactory comparison can be made. The Department also needs to contemplate alternatives, particularly delivered log costs instead of stumpage, because of the problems presented by the need for adjustments.

Comment

The core challenge of this section is whether U.S. price information will be "verifiable." The Bulletin elsewhere proposes the use of U.S. prices as reference markets, but here demands that "the province collects information from private market participants in a rigorous, systematic, and verifiable manner and regularly publishes this information." Provincial governments may well meet this requirement for domestic private markets, but have no way to meet it in the United States. Indeed, a central legal failure of the final determination in this case is the absence of verified information for any of the benchmarks used by the Department.

This section is also concerned with adjustments, and demands that they "be kept to a minimum necessary, and must be fully and economically justified, and transparent." This requirement is advanced both to avoid "over- or under-valuation of timber," and to reduce what otherwise promises to be "tremendous information

requirements." This concern, and the concern for verifiable information, should lead to three conclusions only marginally contemplated elsewhere in the Bulletin.

First, the absence of private transactional information from the United States, and the apparent impossibility of verifying U.S. information (the Bulletin places the burden of verification of reference markets on the Canadian provinces), should mean that U.S. prices, whether from public or private transactions or auctions, cannot be used reliably or consistently. No matter what U.S. prices may be used, as long as they involve sales at the stump they will never be reliably verifiable.

Second, the use of delivered log costs would be substantially preferable and more reliable than timber or log costs because required adjustments would be minimized. The use of delivered log costs would be preferable whether from public or private sources, from within Canadian jurisdictions or across jurisdictions. Verification should be possible utilizing independent verifiers, whether in the United States or in Canada.

The main emphasis of this section is that reliable comparisons require substantial information. The law, however, requires comparison between public and private prices within the same jurisdiction, and only the law can determine whether public ownership and sale of a resource involves a subsidy. The Department needs to confirm, therefore, that in this section it is not trying to set, yet again, an impossibly high standard where sufficient information is unobtainable and therefore no satisfactory comparison can be made. And the Department should take note that it could reduce informational needs substantially by comparing delivered log costs instead of stumpage.

I.B.2.c. Comparability of Obligations Imposed on Purchaser

Summary Of The Comment

Obligations imposed on purchases of crown stumpage must be taken into account and evaluated reliably to ensure a proper and fair comparison of private to public prices.

Comment

The Bulletin recognizes that purchasers of private timber typically are not encumbered with the same obligations as purchasers of crown stumpage. The obligations must be evaluated and translated reliably in order to compare public and private prices. The Bulletin suggests no reason why this requirement cannot be met, and there is none.

II. Examples of Market-Based Timber Sales

Summary Of The Comment

The Department's examples of market-based timber sales contravene the requirement of the SCM Agreement that "adequate remuneration" be assessed in reference to prevailing market conditions in the country of provision. The Department, through the device of the Bulletin, is evading the international obligations of the United States and infringing upon Canadian sovereignty by requiring Canadian provinces to sell goods in a particular manner.

Comment

Despite a promise of "a series of examples of how the Department would apply its policy guidance in the context of a specific market," the Bulletin provides only two models for what the Department considers market-based timber sales. One requires auctions of provincial timber, and is based on assumptions derived from economic theory and contradicted by U.S. practice. The other requires the use of the results of flawed American auction prices. Neither, therefore, satisfies the requirements of international obligations, to use for reference markets the prevailing market conditions within the jurisdiction where there are alleged subsidies. Instead, one requires dramatic alteration of domestic markets, and the other repudiates using for reference prices domestic markets entirely.

The premise for the Department's examples is repeated expressly from Part I: "market reference prices must come from open, competitive, independently functioning markets and ensure that provinces receive adequate remuneration for all

provincial timber." As the Bulletin at this point repeats this mantra, so it is appropriate to repeat and detail what is wrong with it.

The WTO panel found that Article 14(d) of the SCM Agreement, regarding the determination of adequate remuneration in relation to prevailing market conditions, "does not in any way require the 'market' conditions to be those of a hypothetical undistorted or perfectly competitive market."[1] Yet, the Bulletin would find that, as long as a government does not receive fair market value – as defined in the Department's hypothetical perfect market – it is conferring a subsidy and, as to softwood lumber from Canada, it will continue to be subject to countervailing duties. Hence, the Department, via the Bulletin, is rewriting the legal standard of adequate remuneration and setting a requirement, uniquely for Canadian softwood lumber, not met by any other product from any other country, and not met in the sale of softwood lumber in the United States.

The legal standard for adequate remuneration does not dictate how a government must sell a good. Instead, it dictates how to measure whether the sale of the good yields adequate remuneration for the government. The Department, through the device of the Bulletin, would change this relationship fundamentally, dictating in detail how Canadian provinces are to sell goods. No such regime applies to any other governments for softwood lumber, nor for any other goods.

This attempt to write fair market value into the law, and thereby to dictate how foreign governments are to conduct their business, is nothing less than a full invasion of Canadian sovereignty. It concludes that Canadian provincial governments

[1] *United States—Preliminary Determinations with Respect to Certain Softwood Lumber from Canada, Report of the WTO Panel,* WT/DS236/R, para. 7.50 (Sep. 27, 2002).

do not conduct their business according to international rules because they do not sell goods in the manner the United States would require of them, even when the U.S. requirement is inconsistent with international obligations.

Article 14(d) of the SCM Agreement, achieved with the agreement of some 140 countries, was not written to invade any country's sovereignty. It sets a legal standard that requires governments to compare the prices they receive from the sale of a good -- fully adjusted for whatever obligations or conditions they may impose on buyers, and for whatever circumstances of sale may arise because of government ownership of the good -- to the prices the same buyer might pay were he to buy the same or an equivalent good from a private seller. That is also the standard in U.S. law.[2]

Article 14(d), and U.S. law, set this standard according to the availability of a purchase from a private seller in the same market where the government is selling the good. The Department, however, has adopted the view, expressly rejected by both WTO panels, that the home market must be "undistorted by government intervention," meaning by the very existence of the government as a seller of the good. The need for Article 14(d) and its equivalent U.S. provision arises entirely because the government is a seller of the good, and often a dominant seller, yet the Department would now conclude that the legal provisions are inadequate to their task because governments distort markets. For this reason, the Bulletin attempts to install "fair market value" into the law, in place of "adequate remuneration." Because fair market value can never be

[2] *See* 19 U.S.C. § 1677(5)(E)(iv) ("For purposes of clause (iv), the adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service being provided or the goods being purchased in the country which is subject to the investigation or review. Prevailing market conditions include price, quality, availability, marketability, transportation, and other conditions of purchase or sale."); *see also* 19 C.F.R. § 351.511(b) ("The Secretary will normally seek to measure the adequacy of remuneration by comparing the government price to a market-determined price for the good or service resulting from actual transactions in the country in question.").

achieved, according to this theory, as long as the government is present in the market, the determination of adequate remuneration becomes entirely dependent on alternative scenarios: either governments offer goods in perfectly operated auctions where government's role is nothing more than as manager of the auctions, or the prices at which governments sell their goods are compared to prices from somewhere else where the government is not present to create any distortions.

II.A. Auctions of Provincial Timber

Summary Of The Comment

The Department should clarify in the Bulletin how much of a province's timber being sold at auction will satisfy the measure of a "substantial portion," that the amount should correspond to statistical validity rather than ideological purity, and that the Department will determine the amount before it initiates a changed circumstances review and will not revisit that determination during the course of the review.

Comment

The Bulletin advances a theory that public auctions necessarily yield fair market value, despite evidence on the record of the investigation of softwood lumber from Canada that led to the current countervailing duties that public auctions in the United States rarely if ever yield such results.[1] The Bulletin boldly requires, moreover, that to satisfy requirements for a changed circumstances review through auctions in Canada (instead of by relying on prices from U.S. auctions), a province must be "selling a substantial portion of [its] own timber at auction " while eliminating all of the alleged constraints that inhibit responses to changing market conditions. There are no indications as to what a "substantial proportion" would be, except to suggest in a subsequent section that, "Tenure reforms undertaken by Province A result in the need for all, or virtually all, market participants to obtain a significant share or their fiber from the reference market or competitive log markets on an ongoing basis."

[1] *See* Case Brief of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association, NAFTA USA-CDA-2002-1904-03 at 6-21 (Aug. 2, 2002); *see also* "Forest Service: Barriers to Generating Revenue or Reducing Costs," *GAO Chapter Report*, (GAO/RCED 98-58, Feb. 13, 1998) at 5, (submitted as attachment 3 to Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 31, 2001), P.R. Doc. 628).

The Department needs to clarify that it would initiate a changed circumstances review for a province committing to auction some of its own timber only when it agrees that the proportion of timber subject to auction is "substantial," and that the Department will reject any challenge to that conclusion in the course of a changed circumstances review. The Department needs further to clarify that a “significant share” does not mean half or more, because such a requirement would mean that “Province A” must auction more than half its province-owned timber. And the Department needs to clarify that its expectation here – that tenure holders are expected to participate in the new market mechanism of auctions – is consistent with the notion that tenure holders are not supposed to participate in the market mechanism in the proposed alternative of private market transactions. For these propositions to be consistent, tenure holders should be expected to participate in auctions, or private transactions, as the case may be, and as opportunities present themselves.

II.A.1. Example of Auction Sales

Summary Of The Comment

The Department should not create a standard for Canadian auctions that the United States could not meet. The Department also should acknowledge with respect to fiber swaps that it is requiring an abandonment of long-established practices in the forest industries.

Comment

Apparently aware of the inadequacies of U.S. auctions as models for Canadian provinces, the Bulletin attempts to correct for these inadequacies by creating requirements for auctions to be held in Canada that do not exist in the United States. Decisions in the United States as to how much timber to auction, of what types, and when, are unrelated to market conditions or concerns for operating an "open, competitive and independently functioning market." In the Canadian auctions to be created, however, "a sufficient volume of timber and a representative sample of transactions to permit the auction prices to serve" these criteria (and therefore to be "statistically reliable") are prerequisites to their acceptability as a "reference point for setting stumpage prices on the administered portion of the harvest." There are to be no barriers to eligibility for bidding; there is never to be collusive bidding; there is always to be perfect information held by both buyers and sellers through the regular publication of prices; there are to be deadlines for harvesting by auction winners; there is never to be an insufficient number of bidders; there is always to be complete transparency. Canadian auctions are to be, verifiably, everything U.S. auctions are known not to be,

and more.[1] Presumably, should Canadian auctions fall short of this standard, they could be found to yield inadequate remuneration and therefore to confer countervailable subsidies.

The Bulletin rejects fiber swaps and demands that log markets operate "on the basis of price." There are many and complex reasons why forest products industries often rely on fiber swaps, in the United States as well as Canada, including proximity and accessibility of different and preferred species and reciprocal needs for lumber and woodchips. Therefore, the Department needs to clarify that its intention here is not merely to assure an adequate volume of price-based transactions in order to manage reference markets, but instead seeks to overturn historical and conventional practices in the forest products industries.

[1] *See* Case Brief of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association, NAFTA USA-CDA-2002-1904-03 at 6-21 (Aug. 2, 2002); *see also* "Forest Service: Barriers to Generating Revenue or Reducing Costs," *GAO Chapter Report*, (GAO/RCED 98-58, Feb. 13, 1998) at 5, 44 (submitted as attachment 3 to Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 31, 2001), P.R. Doc. 628). *See also Review of the Forest Service's Timber Sales Program: Hearing Before the Environment, Energy, and Natural Resources Subcommittee of the Committee on Government Operations, House of Representatives*, 102d Cong. 2d Sess. 33 (1992) at 34.

II.A.2. Analysis

Summary Of The Comment

The Department needs to clarify exactly what the requirements are for a province to obtain revocation of the order for the province (*i.e.,* is there an effects test?; does the province have to eliminate log export restrictions on public lands?).

Comment

The Bulletin indicates that, before the countervailing duty order could be revoked for "Province A," the province that would convert some "substantial portion" of its crown harvest to public auctions, Province A would already have "met" "all the conditions outlined above and those discussed elsewhere in the Policy Bulletin." Hence, according to the "analysis," Province A will have had to have implemented complete reform and a complete auction system: "Province A would have introduced and implemented a system of auctions that were (sic) sufficient to establish market prices." Furthermore, "market prices" will have had to have been established prior to revocation of the order, because Province A must have "ensur[ed] that the province received adequate remuneration on all timber sales."

The Department needs to clarify whether these requirements constitute an effects test whereby the countervailing duty order will not be revoked until Province A has demonstrated that its new system is producing prices that the Department, through its new standard of "fair market value," considers adequate remuneration. The Department needs also to clarify its reference in this section to "other changes," which appear to be expressly additional to the catalogue of policy reforms and implementation of an auction system. There is no indication what these "other changes" might be, and

Province A therefore would appear to be subject to some additional but unnamed requirements before the countervailing duty order would be revoked.

Although in the section on **Barriers to Entry or Exit in the Market** reference to log export restrictions was confined to logs originating on private lands, in this section there is a reference that appears to encompass logs originating from the crown: "A subsidiary benefit of eliminating the minimum processing requirements and permitting purchases of the province's logs by buyers from outside the province, Province A would expand the opportunities for arbitrage between markets in different jurisdictions and thereby preclude the ability of producers in Province A to benefit from changes in provincial policies without the competitive benefit of those changes in policy flowing to competitors in other jurisdictions." As the Rocky Mountains tend to limit timber movement from British Columbia eastward, and Province A appears to be the Province of British Columbia, this statement appears to require British Columbia to open access to its crown logs for companies in the United States.

The Department needs to clarify whether Province A will satisfy the conditions necessary for revocation of the countervailing duty order without eliminating restrictions on the export of crown logs. The Department should further clarify whether it would impose such a condition on a Canadian province without requiring concomitant U.S. reform. Logs originating from timber in state and federal forests bordering British Columbia cannot be exported. The Department would appear to be keeping the U.S. markets closed and protected while opening Canadian markets for Americans to acquire Canadian natural resources.

The Bulletin requires Province A to "reinforc[e] the operation of log markets." It also stipulates that "all market participants have to participate in the auction system or competitive log markets for a sizable portion of their fiber." Yet, the Bulletin also specifies that log markets "would not be used as a reference point for setting stumpage." The Department needs to clarify the extent to which a market participant is expected to participate in auctions as compared to log markets as a condition for the province to qualify for revocation of the countervailing duty order.

II.B. Comparison with Prices Established in Markets in Other Jurisdictions

Summary Of The Comment

The record of the lumber investigation shows that data from the U.S. public forests are not reliable. Even were those data reliable, it is not possible to adjust for every variable that would affect price comparability between U.S. and Canadian public stumpage. Moreover, two WTO panels already have ruled that such comparisons are contrary to the SCM Agreement.

Comment

The Bulletin proposes, as the lone alternative example for the institution of auctions within a province, reliance on "prices generated in a market outside its jurisdiction." Although the Bulletin refers to "auctions from public lands or private markets," the only systems effectively countenanced in the Policy Bulletin involve auctions or, potentially but equivocally, Québec's private market. And the only established auctions in jurisdictions adjacent to any Canadian provinces are in the United States.

The prices upon which the Bulletin proposes to rely, then, when not relying on government run auctions in Canada, are prices from the government sale of goods in the United States. Reliance on these prices depends on the following fallacies: (1) that these auctions satisfy the Department's theories of perfection; (2) that the goods being purchased are reliably comparable; (3) that it is possible to establish reliable and universally applicable adjustments for conditions and circumstances of sale; and (4) that government ownership of the good in the United States is of no consequence.

There is ample record evidence, derived from studies of the General Accounting Office and the United States Forest Service, that auctions in the United States forests are considerably less than perfect.[1] The Bulletin hints at relying, further, on auctions on state and county lands in the United States, about which little or nothing is known empirically, but there is no reason to presume that they will be more reliable as activities of perfect markets than the auctions on federal lands.

Conspicuously, the Bulletin does not suggest that the test to be applied has any relationship at all to the purpose of the test created in Article 14(d). Public prices in Canada are not to be compared, in the Bulletin's scheme, to private prices in Canada or anywhere else. Instead, they are to be compared to public prices in the United States, on the theory that, because these prices are derived from auctions, they must produce fair market value. This need to find fair market value would not arise, of course, were the law not being rewritten to revise the standard from adequate remuneration, comparing the price a buyer would pay a private seller to the price he pays the government. Under the new standard, there must be a perfect sale, not a legal or legitimate comparison.

There are very significant differences among trees as one moves from north to south on the North American continent. Typically, with exceptions for micro-climates, trees take longer to grow in the north, are smaller, and may be hardier. They are also more remote for harvesting, and present greater challenges to access and

[1] *See* Case Brief of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association, NAFTA USA-CDA-2002-1904-03 at 6-21 (Aug. 2, 2002); *see also* "Forest Service: Barriers to Generating Revenue or Reducing Costs," *GAO Chapter Report*, (GAO/RCED 98-58, Feb. 13, 1998) at 5, 44 (submitted as attachment 3 to Letter from Baker & Hostetler LLP to the Department of Commerce, Case No. C-122-839 (Dec. 31, 2001), P.R. Doc. 628).

transport. They typically are not the same species. Hence, the goods being compared between Canada and the United States are not the same, and they are not being sold under the same conditions.

Governments in the United States subsidize the U.S. timber industry in many ways. They often make vast tracts of forest available free or close to free in the name of forest fire control (witness President Bush's "Healthy Forest Initiative") or some other public policy imperative of the moment; they build roads at public expense to be used by timber companies, and they assume responsibility for silviculture and regeneration of the forest. They bear the expense of forest fires, and they provide the protection of the forest from disease. They do all the planning for forest development.

By contrast, Canadian governments have shifted all these burdens onto the Canadian timber industry. Private parties pay for roads, forest fires, insect control, silviculture, planning. And because Canadian companies bear these expenses, the prices they pay for timber cannot be fairly compared with the prices U.S. companies pay in the United States, even were it possible sensibly to adjust for huge differences in harvesting conditions and hauling distances, and for differences in the trees themselves. The Bulletin, in the section on **Comparability of Obligations Imposed on the Purchaser**, suggests that there should be a fair accounting of these differences, but does not repeat the suggestion when offering examples. The Department should clarify its commitment to take full account of all differences in obligations when attempting comparisons across jurisdictions. Of course, the use of delivered log costs instead of stumpage would reduce the number of needed adjustments and other difficulties of comparison.

Were these impediments to comparison not enough, the trees at issue in both countries are government owned because the Bulletin does not contemplate the use of private transaction prices in the United States. Governments adjust access to forests according to varying public policy priorities, which fluctuate depending on the government of the moment. One government may want to protect old growth, or assure multiple and diverse uses of the resource, or to protect the habitat of a particular species or animal; another government may want to stimulate economic activity in the forests. By constructing a system of comparison across sovereign borders, the Bulletin would expose the public policy choices of one government to the preferences of another, and the industry in one jurisdiction would have the availability of resources dictated by the public policy preferences of the government in another jurisdiction. Only, in this case, the impact is to be unidirectional: U.S. public policy choices will dictate prices in Canada, as U.S. prices are to be Canada's benchmarks.

II.B.1. Example of Prices Established in Markets in Other Jurisdictions

Summary Of The Comment

The Bulletin should be revised to allow explicitly for the use of delivered log costs for the comparisons. The Bulletin describes a market to be used for comparison that does not exist, either in Canada or in any bordering jurisdictions in the United States.

Comment

This section calls upon "Province B" to "rel[y] on prices from the sale of standing timber in open, competitive markets in an adjacent jurisdiction, or jurisdictions, to establish the reference point for setting stumpage on the administered portion of its harvest." It should be apparent, however, that standing timber comparisons, across or within jurisdictions, present numerous and probably insurmountable obstacles because of the range and type of adjustments required to approximate a fair comparison. There is no provision here for the use of delivered log costs for comparison, instead of prices derived from the sale of standing timber, but there should be. Yet, there is an explicit expectation that "any adjustments should be kept to the minimum necessary." Delivered log costs would provide much more reliable benchmarks, and would minimize adjustments.

The description of the "independently functioning markets for standing timber in the other jurisdiction, or jurisdictions" is of markets that nowhere exist, apparently leaving to the Department's discretion whether a given market might be acceptable. Certainly there are no known available data from U.S. sales of standing timber where there is "publication of price information to all market participants" (price

information in the United States is available through private services on an estimated basis); the markets "include appropriate safeguards against collusive bidding;" and the markets "provide a representative range of prices for standing timber comparable to that sold in Province B" (certainly there are no such known data for standing timber sold in the Province of Ontario, which appears to be "Province B"). Hence, the Bulletin proposes for Province B a reference market that does not exist, and its qualification for use with Province B must therefore depend on the Department's discretion and willingness to reject empirical challenge. As in the case of Province A, the Department needs to clarify whether it will be flexible with these criteria and reject challenges to its application of U.S. prices when the markets from which they come do not satisfy the criteria enunciated in this paragraph. Any flexibility, moreover, should not be applied to the detriment of Province B. For example, an unrepresentative range of prices should not be used in order to raise prices in Province B.

II.B.2. Analysis

Summary Of The Comment

This section is ambiguous as to whether private market prices within Province B could be used as a reference price, when this reference price could be applied and, if introduced after the changed circumstances review, whether the Department would retain a role in the transition to an internal private market benchmark.

Comment

The Bulletin requires Province B to "reinforce[] the operation of the private market for standing timber within the province," but allows only that the province's private market might somehow become "reference points it might use to set stumpage at a later date." This intended date is apparently much "later," because changes and improvements in the private market are "not directly relevant to the question of whether Province B" satisfies conditions "necessary to pursue a changed circumstances review." Instead, "The key issue for Province B under the facts set out in the example is likely to be the transparency it can introduce into the means by which it translates prices from auctions of standing timber in the adjacent jurisdiction to stumpage charged for comparable sales of timber on the administered portion of the province's harvest."

The Department needs to clarify whether this statement is intended to preclude the suggestion in the previous section, that there could be recourse to prices "from private markets," and that private market improvements are irrelevant to revocation of the countervailing duty order for Province B. The Department needs to further clarify, in light of its suggestion that Province B's private market could be the "reference points it might use to set stumpage at a later date," whether the Department

presumes some role to play, after revocation of the order, in Province B's transition to a domestic benchmark for setting crown stumpage.

II.C. Other Timber Sales Methods Designed to Achieve Adequate Remuneration

Summary Of The Comment

The special considerations the Department proposes for a hypothetical provincial industry dominated by one firm should be applied broadly to all provinces and companies.

Comment

The Department hypothesizes conditions where a single integrated forestry firm dominates a provincial forest industry. In this example, the Department proposes to consider only market reforms and some unexplained assessment of whether that firm pays adequate remuneration. The Department eschews an "independently functioning market" for a benchmark because of the forest resource's "remote location" and the "bio-physical characteristics of the forest resource."

There are significant forest resources in every Canadian province that are very remote and that have unique bio-physical characteristics. Should the Department be willing to compromise all of the potentially Draconian, abstract requirements in the Bulletin in order to accommodate this one company, then it should be prepared to exercise flexibility in favor of all Canadian provinces and companies. There is no plausible rationale for one completely exceptional case.

III. Changed Circumstances Review

Summary Of The Comment

The Department asks Canadians to accept through the Bulletin methodologies that twice have been found inconsistent with the SCM Agreement and also are inconsistent with the plain language of U.S. law. In return, the Bulletin provides no assurances that the order would be revoked were Canadians to make every change required of them, and no assurances that the Department would not initiate a new investigation were the orders to be revoked.

Comment

The premise of a changed circumstances review is the persistence of a countervailing duty order. The present order exists only because the Department has violated its international obligations and its own governing statute by determining adequate remuneration according to benchmarks outside Canada. The Department is anxious to institute this Bulletin so that it might overcome the law through Canadian acquiescence and the Department's own avoidance of legal conclusions.

The Bulletin calls upon every provincial government in Canada to abandon the legal standard of adequate remuneration, replace it with fair market value, and then desert the principle of comparison of government sales to private sales with the installation of auctions or comparisons to auctions, including especially government auctions. Recognizing implicitly the defects in U.S. auctions, the Bulletin then confers upon the Department the exclusive authority to determine when the stringent conditions of market perfection are achieved.

Canadian parties reasonably expect to prevail in the legal appeals of the Department's final determination of the countervailing duty order. For this Bulletin to have effect, Canadian parties are to abandon their rights to legal judgments as to appropriate standards for the government sale of goods in favor of the Bulletin and the Department's discretion.

The Bulletin does not promise outcomes or rewards for Canadian provincial changes or adaptations, reserving instead to determine whether the Department is satisfied with provincial performance. Even then, there is no promise that no legal action might again be initiated by the Department against Canadian softwood lumber products should, for some reason or in some way at some point some provincial action might incur the displeasure of the Department or some portion of the U.S. industry.

III.A. Timing

Summary Of The Comment

The Department should clarify that provinces cannot submit requests "at any time" because there are very substantial preconditions.

Comment

The Bulletin declares that a province "may submit a request for a changed circumstances review at any time," but the Department will not initiate a review until the province has been able to provide documentation in no fewer than seven categories. Hence, the Department should clarify that provinces cannot realistically submit requests "at any time" because there are very substantial preconditions to initiation.

III.B. Content of Request

Summary Of The Comment

The evidentiary requirements of the Bulletin, were they to be enforced literally, would make it unlikely that any province could submit a successful request for a changed circumstances review. Allowing a province to use delivered log costs for its comparisons could remedy many of the evidentiary difficulties that otherwise would arise. The Department needs to clarify whether it requires fulfillment of an “effects” test before it would initiate a changed circumstances review.

Comment

A changed circumstances review request requires completion, not initiation, of provincial changes. Laws and regulations must be submitted that demonstrate the elimination of policies and practices, not proposals or intentions for change.

According to this section of the Bulletin, a province must prove that it has fully implemented all legal changes such that all of the practices identified elsewhere in the Bulletin, including those that serve conservation purposes, have been eliminated. Provinces must prove that the proposed reference markets satisfy the criteria of market perfection indicated elsewhere in the Bulletin. For Province A, instituting auctions, it may be possible to satisfy this criterion, albeit only if a "sizable portion" or "all" or "virtually all" or some acceptable variant thereof of the crown's harvest is being auctioned. For Province B, this requirement probably can never be met, as there are no U.S. markets that satisfy the Bulletin's criteria.

The summary of evidentiary requirements makes no references to "independently functioning" markets, instead referring only to markets that are "open and competitive." The Department should clarify whether its intention here is to modify the requirement enunciated elsewhere, so that there is a more realistic set of criteria. Private markets in Ontario and Québec, for example, probably could satisfy the criteria as enunciated in the second bullet of this section, whereas neither likely could satisfy the criteria as enunciated elsewhere in the Bulletin.

The evidentiary requirements inevitably fret about adjustments arising from comparisons of prices for standing timber. The substitution of delivered log costs for standing timber would reduce this evidentiary difficulty substantially.

The Department needs to clarify, with reference to the penultimate bullet in the description of required evidence, whether any province can apply for a changed circumstances review before it can document that it has instituted significant policy reform; changed its laws and regulations; implemented an entirely new stumpage pricing system; and has received prices for standing timber that reflect all these changes such that prices on the administered portion of the harvest are "consistent with the range of prices observed in other open and competitive markets for timber sales of similar species, quality, and market conditions." The Department thus needs to clarify whether it requires fulfillment of an effects test before it will consider even launching a changed circumstances review for eventual revocation of the countervailing duty order.

The need for this clarification is amplified by the subsequent section of the Bulletin. There, the Department requires of provinces "substantial, *verifiable* evidence demonstrating, in accordance with this Policy Bulletin and as required by U.S. law, that

the provincial timber sales system has been revised and *is operating* so as to ensure that the province receives adequate remuneration within the meaning of the U.S. countervailing duty law." (emphases added)

III.C. Evidentiary Standard

Summary Of The Comment

The Department must make an unequivocal pledge in the Bulletin that should Province B implement the Bulletin's requirement that Province B set its stumpage prices based on U.S. auctions, as appropriately adjusted, the Department will revoke the countervailing duty order as to Province B.

Comment

In an investigation, the evidentiary burden is on the Department. Its final determination can stand only when supported by substantial evidence that it has been required to gather. The Bulletin hastens to point out that in a changed circumstances review, the burden of proof shifts to the provinces.

This shift in burden is particularly notable because in the legal appeals of the Department's final determination, the burden of proof remains with the Department. Hence the Bulletin is being used here not only as a device to rewrite the law, but also to overcome the Department's evidentiary failures in the investigation. The Department relied in the investigation on U.S. evidence that it did not, and apparently could not, verify. Now it would require Province B to rely on U.S. evidence, and bear the unbearable burden of verification.

This burden shifting is especially notable because it effectively makes and withdraws a pledge. The Bulletin pledges to revoke the countervailing duty order for Province B provided Province B changes practices and commits to reference markets in the United States. But the Bulletin also requires that those markets satisfy conditions

they are already known not to satisfy, and the Bulletin requires verifiable information where the Department already knows that verification is unlikely or impossible.

Even were the Department of good will and intention in its creation of the Province B option, it could not escape the reality that it acknowledges obliquely and in passing in the next section, **Conduct of the Review**. There the Department announces that it "will, upon request by an interested party, hold a public hearing." It thus acknowledges that a changed circumstances review is adversarial, and that Province B is exposed to the infirmities of the pledge.

The Department needs to clarify that, notwithstanding that U.S. timber markets do not live up to the Department's ideal as described in the Bulletin, and that U.S. data are likely not subject to verification, it will nevertheless revoke the countervailing duty order for Province B should that province implement the recited policy and practice changes and set stumpage for the administered portion of its harvest according to auction prices for comparable standing timber, subject to appropriate adjustments, from the United States. Nothing short of such a formal pledge could be relied upon by Province B in view of the numerous contradictions in the Bulletin.

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III.D. Conduct of the Review

Summ**ary Of The Comment**

Revocation of the order pursuant to the Bulletin is likely to be years away for any province.

Comment

The Department recites correctly the essential terms of its regulations governing changed circumstances reviews, but offers not even a hope that reviews might be conducted on a faster track for qualifying provinces. Thus, provinces appear to be on notice not to expect revocation of an order in fewer than 270 days from the time they apply, and they are on notice from the previous sections that they need not apply before they have reformed, legislated, implemented and assigned prices to the crown harvest that demonstrate that all their reforms have had the desired price effects.

III.E. Effective Date of Revocation

Summary Of The Comment

The Department should clarify that it will initiate a changed circumstances review before obtaining price results for a province's reforms but, in such a case, the effective date of revocation would be when the prices are confirmed, rather than the date of initiation.

Comment

The Department acknowledges that it is requiring complete satisfaction of changed circumstances before initiating reviews, and therefore would make effective revocation of the countervailing duty order retroactive to the date of the application. However, the Department also warns that, should the review not conclude that all was in order at the time of the application, the revocation will not be retroactive, and will be effective only as of the date when the Department is persuaded that all reforms "took effect." The Department should clarify here what it means: that a province could apply for a changed circumstances review before obtaining price results from its reforms, with such results arriving during the course of the review. The review could proceed, but revocation of the order would be effective only as of the date when the prices were confirmed.

IV. What Is Missing

Summary Of The Comment

The Bulletin ignores the antidumping order, while requiring changes to Canadian practices that would make the Canadian industry more vulnerable to dumping actions on a continuing basis. It is also silent on the disposition of cash deposits and administrative reviews during the pendency of the countervailing duty order.

Comment

There is no mention in the Bulletin of the antidumping order. The Bulletin nakedly expects, indeed requires, Canadian lumber production costs to increase through implementation of the requirements of the Bulletin. Such cost increases inevitably will impact the Department's antidumping calculations. Indeed, the current antidumping action arguably is the product, entirely, of the managed trade created by the Softwood Lumber Agreement of 1996, to be exacerbated by new artificial trade restraints, presumably in the form of some interim agreement while the requirements of the Bulletin are implemented, and then by the impact of the Bulletin itself. The Bulletin's failure to address the dumping allegations and dumping action leaves Canadian industry totally exposed and vulnerable to dumping actions on a continuing basis.

The Bulletin is silent about accumulating cash deposits, and about administrative reviews, during the pendency of the countervailing duty order, which must remain in place for there to be changed circumstances reviews. The statute dictates deadlines for the beginning and completion of administrative reviews to set countervailing duty rates and to liquidate entries. The implied schedule for changed circumstances reviews would mean completion of more than one administrative review

before revocation of the order for any provinces. The Department needs to clarify how, within the law, it intends to collect, manage, and dispose of cash deposits