United States - Preliminary Determinations with Respect to Certain Softwood Lumber from Canada

WT/DS236

SECOND WRITTEN SUBMISSION OF THE UNITED STATES OF AMERICA

May 17, 2002

I. INTRODUCTION

1. Over the course of this proceeding, the issues have been focused and the facts clarified. If there was ever a doubt, the United States has now demonstrated that the Canadian provincial governments provide timber to lumber producers – that is a financial contribution under the WTO *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement").

2. The United States and the European Communities ("EC") also share the view that, in appropriate circumstances, the benefit from the government's provision of a good may be measured by comparison to commercially available world market prices, consistent with Article 14(d) of the SCM Agreement. Even Canada agrees that the use of import prices may be appropriate in certain circumstances. Therefore Article 14(d) does not prohibit the use of world market prices in appropriate circumstances.

3. There has, however, been much debate over whether the Commerce Department's recourse to such prices in this case was appropriate. In the end, as discussed below, the evidence demonstrates that the Commerce Department's use of U.S. stumpage prices commercially available to Canadian lumber producers was entirely consistent with the SCM Agreement.

4. The United States has also amply rebutted Canada's claim that the Commerce Department inflated the amount of the subsidy benefit by failing to take into account so-called "independent loggers." The Commerce Department's preliminary determination that the Canadian provincial stumpage systems provide a subsidy to lumber producers was therefore entirely consistent with U.S. obligations under the SCM Agreement.

5. Thus, we come full circle to where we began. "No Member should cause, through the use of any subsidy . . ., adverse effects to the interests of other Members, i.e. . . . injury to the domestic industry of another Member."[1] When one Member causes injury to the domestic industry of another Member through the use of *any* "specific" subsidy, the injured Member has the right to take countervailing measures. The U.S. right to impose provisional measures to counteract the injurious effects of billions of dollars of imports of subsidized Canadian lumber should therefore not be denied.[2]

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[1] Article 5, SCM Agreement.

[2] The United States notes that, on May 16, 2002, the U.S. International Trade Commission notified the Commerce Department of its final determination that there is a threat of material injury to the U.S. industry from imports of softwood lumber from Canada. Consistent with Article 20.4 of the SCM Agreement, all cash deposits or bonds posted during the provisional measures period will be refunded, and entries during that period will not be subject to countervailing duties. While the United States recognizes that termination of the measures at issue does not preclude the Panel from making findings regarding the consistency of the measures, we note that recommendations are unnecessary. *See Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products*, WT/DS207/R, Report of the Panel, 3 May 2002, para. 7.124.

II. ARGUMENT

A. The Commerce Department's Preliminary Determination that the Canadian Provincial Governments Provide a Good to Lumber Producers Is Consistent with Article 1.1(a)(1)(iii) of the SCM Agreement

6. It should be beyond dispute that the provincial governments are providing a good – timber – to lumber producers, within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement. This conclusion is inescapable under any definition of "good"[3] in any language.[4] It should also be beyond dispute that when a government gives a company the right to take a good, whether it is the right to take widgets from a government warehouse or timber from government land, the government is "providing" that good within the meaning of Article 1.1(a)(1)(iii).[5] The Canadian provincial governments give tenure holders the right to take timber off Crown land and, thus, give them the timber itself. The only logical conclusion is that, in doing so, the provincial governments are providing a good within the meaning of Article 1.1(a)(1)(iii).

7. Canada's attempts to obfuscate this simple fact rely on logically flawed arguments, and ignore the basic principles of treaty interpretation reflected in Article 31 of the *Vienna Convention on the Law of Treaties*. For example, Canada asks the Panel to infer from the use of the phrase "imported goods" in Article 3.1(b) of the SCM Agreement and the word "products" in Parts III and V of the SCM Agreement, that "goods" can only mean traded goods that fall within the GATT 1994 Article II schedules. The fact that "products" are goods and "imported goods"

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[3] *See* U.S. First Written Submission, para. 26 (discussing the ordinary meaning of "goods").

[4] *See* Canada First Response to Panel Questions, para. 10. As Canada notes, the word "goods" in Article 1.1(a)(1)(iii) is translated as *biens* in French and *bienes* in Spanish. In French, *biens* means "possession, property, assets, wealth, goods (and chattels); fortune." *Harrap's French Dictionary* 82 (1982) (Exhibit U.S.-37). By contrast, *produits*, which is used in Article 3.1(b) of the SCM Agreement, means "product; produce." *Id.* at 593 (Exhibit U.S.-38). Similarly, in Spanish, *bienes*, which is used in Article 1.1(a)(1)(iii), means "[p]roperty, fortune, riches, land." *The New Revised Velazquez Spanish and English Dictionary* 105 (1985) (Exhibit U.S.-39). *See also Wiley's English-Spanish Spanish-English Legal Dictionary* 374 (2nd ed. 1997) (defining *bienes* as "property, assets, estate, goods") (Exhibit U.S.-40). By contrast, the Spanish word *productos*, used in Article 3.1, means "[p]roduct, something produced, as grain, fruit, metals; production." *The New Revised Velazquez Spanish and English Dictionary* 537 (1985) (Exhibit U.S.-41). Canada argues that Members intended that "goods" be given the narrower meaning (*produits, productos*) throughout the Agreement. Logically, however, the explicit choice of the broader term in Article 1.1(a)(1)(iii) is evidence of an intent to sweep more broadly in defining financial contribution. In contrast, the *produits/productos* translation is appropriate in the context of Article 3.1(b), which is concerned with incentives against the use of "imported" goods.

[5] "Provides" is defined as, among other things, to "supply or furnish for use" or "make available." *The New Shorter Oxford English Dictionary* 2393 (1993) (Exhibit U.S.-5).

are goods does not, however, logically give rise to the inference that nothing else can come within the meaning of "goods."[6]

8. To sustain its strained interpretation, Canada simply ignores the most relevant aspect of the ordinary definition of "goods" in the source it relies upon, which is the inclusion of "growing crops, and other identified things to be severed from real property."[7] Moreover, Canada's attempt to narrow the ordinary meaning of "goods" would render superfluous the only express limitation in the text itself, i.e., the exclusion for "general infrastructure."[8] If "goods" were intended to be read as narrowly as Canada suggests, it could never encompass *any* infrastructure (e.g., a building, road, etc.), let alone general infrastructure. "Goods" must include some infrastructure, otherwise the specific exclusion in Article 1.1(a)(1)(iii) is superfluous. Thus, the very existence of that express limitation demonstrates that the Members intended "goods" to be read in accordance with its ordinary meaning and therefore to include things other than those listed in the GATT 1994 tariff schedule.

9. In addition, Canada's arguments are premised on the notion that the only thing at issue here is an intangible "right" granted by the provincial governments, which Canada then proceeds to totally divorce, analytically, from the object of the right granted. Under Canada's theory, form is everything: what something is called (e.g., an "exploitation right") is more important than what it actually is.[9] In Canada's truncated analysis, if the government has granted a right, the inquiry stops, regardless of what the "right" entitles the holder of the right to do. By ignoring substance, Canada concludes that, while granting a right may constitute a financial contribution, it can never constitute the provision of a good.[10] However, as the *Export Restraints* panel stated:

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[6] This would be the logical equivalent of saying that, because office buildings are buildings and warehouses are buildings, houses cannot also be buildings.

[7] *Black's Law Dictionary* 701-02 (7th ed. 1999) (Exhibit CDA-17). *Compare* Canada First Response to Panel Questions, para. 6 (citing the same definition of "goods" in *Black's Law Dictionary*).

[8] The Appellate Body has cautioned that "an interpreter is not free to adopt a reading that would result in reducing whole clauses and paragraphs of a treaty to redundancy or inutility." *See United States Standards for Reformulated and Conventional Gasoline*, WG/DS2/AGR, Report of the Appellate Body, adopted on 16 May 1996, p. 15.

[9] *See* Canada First Response to Panel Questions, para. 20.

[10] *Id*. The United States notes that Canada's assertion that the granting of certain rights might constitute revenue foregone, but never the provision of goods, appears to confuse the issue of "financial contribution" and "benefit." In particular, this appears to be another attempt by Canada to measure the benefit from the provision of a good on the basis of the cost to the government, rather than the benefit to the recipient. The sale of any asset is a potential source of revenue, including the sale of a good. Thus, the sale of any asset, including a good, for less than

> We believe, in particular, that the appropriate way to conceive of a "financial contribution" is purely as a transfer of economic resources by a government to private entities in the market, without regard to the *terms* of the transfer.[11]

10. Thus, it is in fact the "right," i.e., the terms under which the provinces transfer timber to lumber producers, that is irrelevant. To determine whether there is a financial contribution, the treaty interpreter should look at the reality of what actually occurs. In the case of provincial tenures, what actually occurs is that the provincial governments grant tenure holders the right "to take" a tangible good – timber – off the land. The right "to take" is, in fact, the mechanism (or terms) by which the government "provides" the timber, i.e., places the timber at the disposal of the lumber producer.[12] The provincial governments are therefore providing goods within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement.

11. Canada concedes that offering steel producers the opportunity to load and haul (i.e., "to take") iron ore from a government stockpile would constitute the provision of goods.[13] In reality, there is no meaningful difference between giving lumber producers the right to take trees off Crown land and giving steel producers the right to take iron ore from a government stockpile. While Canada may disagree, the United States is confident that the steel producers and the lumber producers would not.[14]

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market price does, in one sense, entail foregone revenue. It is, however, obvious that treating every sale of an asset as falling within Article 1.1(a)(1)(ii) (revenue foregone) would render Article 1.1(a)(1)(iii) superfluous. The specific example of revenue foregone found in the text of Article 1.1(a)(1)(ii), i.e., fiscal incentives such as tax credits, provides guidance on how to distinguish between the concepts of "revenue foregone" and "less than adequate remuneration." In the case of revenue foregone, there is no "market" counterpart to taxes; the benefit is equal to the revenue foregone. In contrast, the benchmark for the sale of assets (goods) is market value, i.e., adequate remuneration. A proper analysis of a financial contribution must therefore take into account the specific facts of each case. It is the view of the United States, for the reasons discussed above, that giving tenure holders the right to take timber from Crown land constitutes the provision of a good within the meaning of Article 1.1(a)(1)(iii).

[11] *United States – Measures Treating Exports Restraints as Subsidies*, WT/DS194/R, Report of the Panel, adopted 23 August 2001, para. 8.40, fn. 135 (emphasis in original).

[12] Canada points out that a "profit a prendre" is "a right to enter into another's land and to take something off that land." *See* Canada First Written Submission, fn. 10. Even under Canadian law, therefore, stumpage "rights" involve the provision of a good.

[13] *See* Canada First Response to Panel Questions, para. 20.

[14] Moreover, the United States disagrees with Canada's assumption that a property right itself can never, under any circumstances, constitute a good within the meaning of Article 1.1(a)(1)(iii). The ordinary meaning of "goods" encompasses all "*property* or possessions." *The New Shorter Oxford English Dictionary* 1116 (1993) (emphasis added) (Exhibit CDA-18). The term "property" includes "[t]he right to possess, use, and enjoy a

12. The reality of the provincial tenure systems is readily apparent. The evidence demonstrates that companies obtain tenures for the sole purpose of obtaining timber, not to manage the forest. Tenure holders acquire nothing under the tenure but timber, and pay stumpage fees only on the amount of timber actually harvested.[15] These facts leave no doubt that through the tenure systems the provincial governments are "providing" a "good" – timber.

B. The Commerce Department Properly Measured the Benefit from Provincial Stumpage Systems Under Article 14(d) of the SCM Agreement

13. Canada has made several claims with respect to the Commerce Department's measurement of the benefit from provincial stumpage systems. In this section, the United States will address Canada's claims concerning the Commerce Department's selection of a market benchmark for stumpage.[16]

1. The Use of Commercially Available World Market Prices Is, in Appropriate Circumstances, Consistent with Article 14(d) of the SCM Agreement

14. As discussed in the U.S. prior submissions, Article 14 of the SCM Agreement sets forth guidelines for determining the benefit conferred by a financial contribution. Prior panel and Appellate Body reports have defined a benefit as some form of advantage that would not otherwise be available in the marketplace, absent the financial contribution.[17] The guidelines in

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determinate thing (either a tract of land or a chattel). . . [and] [a]ny external thing over which the rights of possession, use, and enjoyment are exercised . . . . In its widest sense, property includes all a person's legal rights, of whatever description." *Black's Law Dictionary* 1232 (7th ed. 1999) (Exhibit U.S.-42). It is possible, therefore, that the granting of certain rights could itself constitute the provision of a good.

[15] In this regard, the United States notes that, in each of the provinces, ownership of the trees passes to the tenure holder when the trees are harvested. For example, Ontario and Quebec legislation explicitly provides that the Crown owns the trees until the trees are harvested. In other provinces, the nature of the legal right to access lands to take timber (termed by Canada as a *profit à prendre*) similarly does not convey ownership of the trees until they are harvested. *See* U.S. First Response to Panel Questions, para. 13; Interior Alliance Indigenous Nations Amicus Curiae Submission, p. 7.

[16] Canada's claim that some portion of the benefit did not accrue to producers of the subject merchandise is discussed below in section II.C. With respect to the remaining claims (the use of "first mill" data and inclusion of Maritime lumber in the calculation), the United States will, at this time, rely on its prior submissions.

[17] *See Canada Aircraft – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/R, Report of the Panel, as affirmed by the Appellate Body, adopted 20 August 1999, para. 9112; *Canada Aircraft – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, Report of the Appellate Body, 2 August 1999, para. 157.

Article 14(d) should therefore be interpreted to achieve an appropriate comparison of the financial contribution to the marketplace, i.e., a comparison that would identify the artificial advantage resulting from the government's financial contribution.

15. Article 14(d) does not purport to address every conceivable scenario in which a benefit must be determined. For instance, some types of financial contributions are not addressed at all in Article 14 (e.g., grants and debt forgiveness). Thus, authorities have the discretion to develop appropriate methodologies. It is the view of the United States that an appropriate methodology is one that is consistent with the guidelines in Article 14, considered in light of the object and purpose of Article 14 to compare the financial contribution to what would be available to the recipient in the market absent the financial contribution.

16. With respect to the provision of a good, Article 14(d) of the SCM Agreement states that the comparison should be made "in relation to prevailing market conditions for the good [] in question in the country of provision . . . ." There is no dispute that the basis for the comparison described in Article 14(d) is the prevailing market conditions in the country under investigation. What constitutes prevailing market conditions is also described in Article 14(d), i.e., "price, quality, availability, marketability, transportation and other conditions of purchase or sale." Where the United States and Canada disagree is in defining what constitutes the universe of permissible market benchmarks that could be used to measure the adequacy of remuneration "in relation to prevailing market conditions" in the country under investigation, consistent with Article 14(d).

17. As the EC stated: "[t]he expression 'market conditions in the country of provision' in Article 14(d) of the SCM Agreement is sufficiently broad to allow the consideration of world market prices."[18] In particular, as noted above, the concept of commercial "availability" is expressly incorporated in Article 14(d). The use of "commercially available" world market prices is also expressly sanctioned in item (d) of the Illustrative List of Export Subsidies, and has been endorsed by the Appellate Body.[19] Prevailing market conditions in the country of provision may therefore encompass prices commercially available on the world market to purchasers in the

[18] *See* EC Third Party Submission, para. 23.

[19] *See* Annex I to the SCM Agreement; *see also Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*, WT/DS103/AB/RW, Report of the Appellate Body, adopted 3 December 2001, para. 83.

country under investigation.[20] Commercially available world market prices can therefore be used as a market benchmark, in appropriate circumstances, consistent with Article 14(d).

18. As the EC points out, the issue therefore is not whether Article 14(d) permits the use of commercially available world market prices (such as U.S. stumpage prices) *per se*, but rather whether it was appropriate to do so in this case.[21] The facts discussed below demonstrate that the Commerce Department's use of commercially available U.S. stumpage prices was appropriate in this case and therefore consistent with Article 14(d) of the SCM Agreement.

2. There Is No Evidence of a Market Benchmark in Canada

19. When considering the entire universe of potential market benchmarks, the United States agrees that prices within the country under investigation should be used whenever possible.[22] Use of prices within the country under investigation is, however, not always possible. The obvious example, which the EC noted, is the case of a government monopoly for the good in question.[23] In such a case there is no "market" benchmark price. That example is no different in principle from the circumstances of this case. The provincial governments control 85 to 95 percent of the market for timber. There is extremely limited information on non-government prices and the evidence indicates that non-government prices are suppressed by government prices. There is therefore no "market" benchmark price in Canada that could measure the benefit. That conclusion is not based on theory, it is based on the record evidence.

20. First, only three provinces provided any private price data in response to the Commerce Department's questionnaire. Canada's claim that there was "extensive evidence" related to private markets in those provinces is simply not supported by the record.[24] The limited data

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[20] *See Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products,* WT/DS103/R, WT/DS113, Report of the Panel, as modified by the Appellate Body, adopted 27 October 1999, para. 7.47; *see also* EC Third Party Submission, paras. 25-26.

[21] *See* EC Third Party Submission, para. 30 (noting that if the United States correctly dismissed the price information in Canada, the use of world market prices may serve as an alternative benchmark).

[22] *See 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 Fed. Reg. 43186, 43193-94 (August 17, 2001) (explaining benchmark hierarchy in the Commerce Department regulations at 19 C.F.R. § 351.511(a)(2)) (Exhibit CDA-1).

[23] *See* EC Third Party Submission, para. 18.

[24] *See* Canada First Response to Panel Questions, para. 64.

provided by the provinces was inadequate for purposes of establishing a market benchmark. For example, as the United States explained in its response to the Panel's questions, Alberta stated that it does not have any data on private timber used in sawmills. The so-called "extensive" data provided by Alberta was a two-page excerpt from a KPMG survey, which contained a single estimated stumpage value derived from some price data for log sales. Moreover, Alberta acknowledged that the estimated value was based on information that did not distinguish between private and *Crown* timber.[25]

21. Ontario and Quebec submitted market surveys. However, the Ontario survey was flawed in several respects (e.g., it provided no information on quality or grade). Moreover, there was substantial evidence on the record, including statements by an official in Quebec's Ministry of Natural Resources, that government prices suppressed private prices in the provinces. In fact, one Canadian group said that "downward pressure on the price of private wood is built into the system."[26] The influence of a dominant owner has been recognized in other markets as well. A study of stumpage trends in South Australia notes:

> Of the total [productive forest land] . . . [a]bout 70 per cent of the resource is publicly owned. The percentage of the publicly owned resource was even higher in the past. Hence it is likely that stumpage for public pine logs has held a dominating influence on stumpage for similar logs sold by private growers in [South Australia].[27]

22. The remainder of the evidence that Canada cites consists of evidence that does not actually pertain to private prices. That evidence instead largely pertains to whether the provinces recover their costs and earn a profit when they sell timber.[28] The government's profitability is, however, not the issue. It is now well settled that the cost to the government is irrelevant in measuring benefit.[29] Moreover, the purported fact that the provincial governments made a profit does not establish that they sold Crown timber at market prices. The information provided therefore does not address the relevant inquiry, i.e., whether provincial prices for timber are more

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[25] *See* U.S. First Response to Panel Questions, paras. 30-31.

[26] *Id.* at para. 37; *see also id.* at paras. 33-34, 36.

[27] *See* ANU Forestry, *Stumpage trends in South Australia* (March 2001) (Exhibit U.S.-48).

[28] *See* Canada First Response to Panel Questions, para. 64.

[29] *See Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/R, Report of the Panel, as modified by the Appellate Body, adopted 20 August 1999, para. 5.37.

advantageous than those that would have been available to lumber producers on the market absent the provincial governments' financial contribution.[30]

23. As the above analysis of the record demonstrates, there was insufficient evidence of "market" prices in Canada to form a benchmark. As the EC asked, "which other benchmark should be used in [such a case]?"[31] The United States agrees with the EC that, in the absence of market prices in Canada, the use of other prices commercially available to Canadian lumber producers on world markets is a reasonable alternative.[32] As demonstrated below, stumpage prices for comparable timber in the United States are commercially available to lumber producers in Canada.

3. U.S. Stumpage Prices Are Commercially Available to Canadian Lumber Producers

24. Canada agrees that some prices commercially available on the world market, specifically import prices, can provide a benchmark consistent with Article 14(d).[33] Canada argues, however, that it is impossible for there to be import prices in this case. Canada does not claim that Canadian producers cannot or do not harvest timber in the United States, or that U.S. timber cannot be imported into Canada. Canada simply reverts to its argument that the provincial governments are providing a "right," not timber, and that a "right" cannot be imported.[34] Once again, in Canada's view, form is all that matters. As the United States has amply demonstrated

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[30] *Id.* at para. 9.112. Canada also cites to British Columbia's sales under the Small Business Forest Enterprise Program ("SBFEP"). The Commerce Department rejected these auction prices because most potential bidders are excluded. Because the market for SBFEP timber is segmented, i.e., it is wholly separate and detached from the vastly larger market for Crown timber, there is no opportunity for price arbitrage. With respect to Quebec, Canada's description of arbitrage is a misleading tautology – it focuses on the alleged price arbitrage between private log prices and private stumpage prices. This is completely irrelevant to the potential for arbitrage between the overwhelming public supply of timber and the smaller private supply of timber. The private and Crown timber markets are also separated. Because Crown tenure holders consistently harvest below their annual allowable cut, and control the vast majority of the province's timber, private timberland owners have very little market power. Consequently, there is virtually no arbitrage in the form of private prices affecting public prices. Quite to the contrary, it is the public prices that influence the private prices.

[31] *See* EC Third Party Submission, para. 31.

[32] *Id.* at para. 30.

[33] *See* Canada First Response to Panel Questions, para. 29 (acknowledging that prices for imports of the good in question can constitute a market benchmark consistent with Article 14(d)).

[34] *Id.*

above, the provincial governments are not merely providing rights, they are providing timber. U.S. timber can be, and in fact is, imported into Canada.

25. More importantly, Canadian lumber producers can and do purchase U.S. timber on the stump for harvesting and import into Canada. The SCM Agreement states that "commercially available means that the choice between domestic and imported products is unrestricted and depends only on commercial considerations."[35] Canadian lumber producers have virtually unrestricted access to U.S. stumpage for import into Canada.[36] U.S. stumpage is therefore commercially available to Canadian lumber producers.[37] Because U.S. stumpage prices are commercially available to Canadian lumber producers, they fall within the universe of benchmarks that can be considered for purposes of measuring the benefit from provincial stumpage, consistent with Article 14(d) of the SCM Agreement.

26. In fact, based on commercial considerations, U.S. stumpage prices are the most reasonable world market prices to use because the terrain, topography and species mix for U.S. timber in border states are most comparable to those in Canada, and because the record shows that Canadian companies do in fact purchase U.S. timber. In fact, virtually all of Canada's timber imports come from the United States.

27. Furthermore, it is reasonable to conclude that U.S. stumpage prices represent appropriate market-based benchmark prices to measure whether provincial prices confer an artificial advantage. The observed price difference for Canadian and U.S. stumpage does not reflect differences in inherent market characteristics in Canada versus the United States. Rather, it reflects the fact that the Canadian system precludes price arbitrage for timber. There is a fully integrated North American *lumber* market that coexists with a largely segregated North American *timber* market. Canada exports over half of its total lumber production to the United States, but only three percent of its timber production. The United States exports little lumber to Canada,

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[35] Annex I to the SCM Agreement, fn. 57.

[36] Log export restrictions in the United States affect a very small portion of the total U.S. timber supply, i.e., public land west of the Mississippi.

[37] In *Canada Dairy*, the panel deemed irrelevant the fact that Canadian milk processors did not in fact import milk from outside of Canada. The panel noted that "fluid milk *could be imported from the United States* (given its proximity) to Canada" and that "one can assume that imports of fluid milk are, in principle, technically and commercially viable." *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*, WT/DS103/R, WT/DS113/R, Report of the Panel, as modified by the Appellate Body, adopted 27 October 1999, para. 7.54 (emphasis added).

but exports nearly six times as much timber.[38] The low volume of timber trade between the two countries is the result of domestic processing requirements in Canada that limit the flow of Canadian logs southward, and the advantageous stumpage prices in Canada inhibit the flow of U.S. logs northward. The segregated timber market in North America allows for virtually no price arbitrage in timber markets across the border.

28. The unusual nature of the situation in the North American market is evident when compared to the substantial amounts of lumber and timber exports from other countries with

[38] U.S. Department of Agriculture, *Canada Solid Wood Products Annual 2001*, p. 15 (Exhibit U.S.-43). Canada exported 49 million cubic meters (nearly $6.4 billion dollars) in softwood lumber to the United States in 2000, representing 90 percent of Canadian exports and 55 percent of total Canadian softwood lumber production. *See* U.S. Department of Agriculture, *Canada Solid Wood Products Annual 2001*, p. 5 (Exhibit U.S.-43); U.S. International Trade Commission, *Softwood Lumber from Canada*, USITC Pub. No. 3426, p. IV-2 (May 2001) (Exhibit U.S.-44). Virtually all softwood lumber that the United States imports comes from Canada. Canadian imports accounted for approximately 35 percent of the total softwood lumber consumed in the United States in 2000. U.S. International Trade Commission, *Softwood Lumber from Canada*, USITC Pub. No. 3426, p. IV-2 through -4 (May 2001) (Exhibit U.S.-44). By way of comparison, U. S. lumber exports to Canada amounted to approximately 769,000 cubic meters (about $137 million) in 2000. *See* Center for International Trade in Forest Products, available at http://www.centrafor.org/RESEARCH_TAB/research_expdata.htm (Exhibit U.S.-45); U.S. Department of Agriculture, *Canada Solid Wood Products Annual 2001*, p. 5, 14 (Exhibit U.S.-43).

By contrast, the timber trade between the two countries is very limited and highly concentrated. Almost 90 percent of U.S. log exports to Canada consists of exports from the northeastern United States (primarily Maine) to southern Quebec. The cross-border trade between Quebec and Maine is unique in several respects. It is primarily an east-west trade between western Maine and southeastern Quebec. Many of the Quebec "border mills" are located in areas that have been cleared for farmland in this part of southern Quebec, and they rely almost exclusively on the heavily forested areas just across the border in Maine for their wood fiber. For a variety of geographical reasons, including the direction of river flows and the natural topography, it is cheaper for most Maine landowners to transport logs to southern Quebec than to traverse the thick Acadian forest in northern Maine to other mills in New England. Finally, there are close family and business inter-relationships between Maine and Quebec that go back for generations, and several Canadian mills own huge tracts of land in Maine.

major timber and lumber industries.[39] More importantly, the data indicates that U.S. stumpage prices are comparable to prices in Australia, New Zealand, Finland and Chile.[40]

29. The Commerce Department's use of prices for comparable U.S. timber that is commercially available to lumber producers in Canada was therefore appropriate in this case. Moreover, in establishing the market benchmark, the Commerce Department took into account other market conditions prevailing in Canada for timber, such as species, quality and tenure obligations.[41] The market benchmark that the Commerce Department used in the Preliminary Determination was therefore consistent with Article 14(d).

C. The Commerce Department Properly Calculated the Total Amount of the Subsidy to Producers of the Subject Merchandise

30. Canada alleges that the Commerce Department improperly assumed that the benefit from a financial contribution to one entity accrued to another entity. These allegations pertain to three

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[39] There is a vibrant international trade in timber, and statistics for a number of countries with large forest product industries show that timber and lumber exports are often at comparable levels. The principal wood product export of the United States is timber. In 1997, the United States exported 11 million cubic meters of logs worldwide compared to 7 million cubic meters of lumber. In the same year, the EC exported 43 million cubic meters of timber and 44 million cubic meters of lumber; Russia exported 18 million cubic meters of timber and 4.8 million cubic meters of lumber; and Chile exported 1.7 million cubic meters of timber and 1.2 million cubic meters of lumber. U.S. International Trade Commission, *Conditions of Competition in U.S. Forest Products Trade*, USITC Pub. No. 3246, pp. E-13, G-7, G-44, H-4 (October 1999) (Exhibit U.S.-46).

[40] A Canadian market research company published a report in 1998 comparing stumpage prices and logging costs around the world. This report demonstrates that stumpage prices (in U.S. dollars/cubic meter) in Canadian provinces were: $5 (Alberta); $6 (Ontario); $9 (Quebec); $15 (Interior B.C.) and $18 (Coastal B.C.). U.S. stumpage prices ranged from $30 (U.S. Inland) to $49 (U.S. South). Stumpage prices in Chile, New Zealand and Australia ranged from $22 to $25. While direct comparisons with the data on the record of this case are impossible, the data is useful for showing average price trends. *See Timber & Lumber Costs: Who's Got the Competitive Advantage Now?*, available at www.woodmarkets.com.pdf.98 (Exhibit U.S.-47).

The United States also identified additional data for Australia and Finland, two major timber- and lumber-producing countries. The Australian Private Forestry Council provides stumpage prices (in U.S. dollars/cubic meter) for radiata pine ranging from $9.29 to $43.10, with an average of $27.87. ANU Forestry, *Stumpage trends in South Australia* (March 2001) (Exhibit U.S.-48). Data from the Finland investment authority demonstrates that 1998 stumpage prices for pine logs (in U.S. dollars/cubic meter) was $38. *Investment Prospects in the Mechanical Wood Industry in Finland*, p. 9 (Exhibit U.S.-49). Again, while it is not possible to make a direct comparison with record data in this case, the data show that, in general, U.S. timber prices are comparable to other world market prices. Furthermore, as is true in the United States, private ownership of harvestable lands predominates in Europe, Chile, Japan and Korea. *See* Exhibit U.S.-50.

[41] *See* Exhibits U.S.-27 and U.S.-28.

distinct situations: (1) logs harvested by one sawmill and then sold in arm's-length transactions to other sawmills; (2) lumber sold in arm's-length transactions to companies that produce remanufactured lumber products; and (3) timber harvested by independent loggers who sell at arm's-length to lumber mills. In each case, the allegations do not withstand close scrutiny.

31. In the first two situations, all of the alleged recipients of the financial contribution and the benefit are producers of the subject merchandise. As discussed previously, in an aggregate case no further analysis of these situations is necessary to perform the aggregate calculation. The numerator (total benefit to the subject merchandise) is properly matched to the denominator (total sales of the subject merchandise). The precise amount of the benefit received by a specific producer would only be determined in a company-specific review.[42]

32. Canada's claim with respect to the third situation rests on the assertion that the provincial governments provide a significant volume of Crown timber to independent loggers who then sell the timber at arm's-length to lumber mills.[43] In response to the Panel's questions on this issue, the parties have provided record evidence concerning the operation of provincial tenures, and, in particular, the restrictions that the provinces impose on who may acquire a tenure and what the tenure holder may do with the harvested timber. While it is not the Panel's task to conduct a *de novo* review of those facts, a careful analysis of this evidence demonstrates that it does not support Canada's claim that lumber producers acquire a significant volume of timber from independent loggers.

33. First, as the United States has previously demonstrated, the potential volume of timber provided by so-called "independent" loggers is small. Canada's "evidence" to the contrary relies in large part on confusing or irrelevant statistical data. For example, Canada claims that "large numbers of harvesters" are independent loggers.[44] The number of harvesters is, however, irrelevant. The issue is not how many independent loggers there are, but rather whether they

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[42] *See* U.S. First Response to Panel Questions, para. 46.

[43] The United States disagrees with Canada's assertion that, where the harvester and the lumber producer are two different entities, it is necessary to establish a financial contribution to both. *See* Canada First Response to Panel Questions, para. 75. As stated by the panel in *Lead and Bismuth II*: "a 'financial contribution' does not have to be bestowed directly on a company in order to confer a 'benefit' on that company. For example, one company may be found to 'benefit' from a 'financial contribution' conferred on another company." *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, WT/DS138/R, Report of the Panel, 23 December 1999, para. 6.58, fn. 69; *see also* EC Oral Statement, para. 6 (citing to *Brazil - Aircraft* and stating "that, in particular, there is no requirement of identity between the recipient of a 'financial contribution' and the 'benefit' thereby conferred").

[44] *See* Canada First Response to Panel Questions, para. 61.

provide a significant *volume* of Crown timber to lumber producers. Moreover, it is irrelevant if the harvester is "independent" if the mill owns the license (or is tied to the license contractually, as in Ontario).[45]

34. The record demonstrates that the vast majority of the Crown softwood sawlog harvest is, in fact, under tenure to sawmills.[46] This fact is obscured by Canada's province-specific data. For example, instead of estimating the volume of softwood sawlogs harvested by independent loggers in British Columbia, which is the relevant data, Canada estimates the volume of "timber" harvested by companies "not owning sawmills." "Timber" includes hardwood as well as softwood, and pulpwood as well as sawlogs. Moreover, it is completely irrelevant that some portion of the Crown timber was harvested by a tenure holder owning a pulpmill rather than a sawmill, if that timber was not used to make subject merchandise. The relevant fact is that more than 83 percent of the British Columbia Crown softwood timber harvest is provided under tenures that require the tenure holder to own a sawmill.[47]

35. Canada's statements with respect to the potential universe of "independent loggers" in Quebec are perhaps the most difficult to understand because they are almost entirely irrelevant. The issue is the percentage of the *Crown* harvest of softwood sawlogs that is provided to lumber mills by independent harvesters. In Quebec, 99 percent of the Crown harvest is provided under Timber Supply and Forest Management Agreements ("TSFMA"). The Quebec Forest Act states that "[n]o one except a person authorized under Title IV to construct or operate a wood processing plant is qualified to enter into" a TSFMA.[48] The harvest from Federal lands, which is minuscule (less than 1 percent), and private lands is irrelevant to the benefit calculation, as is the fact that there are 40,000 registered woodlot owners.[49] Given the TSFMA requirements, it is virtually impossible to have a significant percentage of independent loggers harvesting Crown timber in Quebec.[50]

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[45] *See* U.S. First Response to Panel Questions, paras. 3 (British Columbia stated that, for the most part, loggers operate as employees or contractors), 5 (Ontario stated that the typical license directs that the harvest be used to supply the licensee and other mills with commitments to receive wood from that area).

[46] *Id*. at paras. 1-9.

[47] *Id*. at para. 2.

[48] *Id*. at para. 4.

[49] *See* Canada First Response to Panel Questions, paras. 54-55.

[50] Canada notes that Petitioners stated that integrated U.S. forest products companies commonly value logs sold to related lumber divisions at market prices. Based on that statement, Canada argues that prices between related parties in Canada may also be at arm's-length. In the United States, however, integrated companies ordinarily

36. Similarly, in Saskatchewan, more than 86 percent of softwood sawlogs were harvested by tenure holders that own sawmills and process their own timber, and in Manitoba, approximately 95 percent of the softwood sawlogs were provided directly to sawmills.[51] Alberta also stated that "[a]ll forms of commercial tenure own and operate sawmills."[52]

37. Second, to the extent there may be a small portion of Crown timber harvested by entities that do not own processing facilities, transactions between those entities and the lumber mills are not at "arm's-length." An "arm's-length transaction" is one that is "negotiated by unrelated parties, each acting in his or her own self interest; the basis for a *fair market value* determination."[53] The term "fair market value" is, in turn, defined as "[t]he amount at which property would change hands between a willing buyer and a willing seller, *neither being under any compulsion to buy or sell* and both having reasonable knowledge of the relevant facts."[54] Thus, a truly arm's-length negotiation is one where neither party is under any outside control or influence, either from the party with whom they are bargaining, or other parties.[55]

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conduct their timberland and lumber operations as separate businesses and vigorous, and open markets in both timber and logs enable companies reliably to determine market prices for logs. By contrast, the vast majority of Canadian timber is provided by the provinces directly to lumber companies, and no independent log market exists. In fact, in the limited circumstances in which Canadian logs are sold freely, i.e., when they are exported, the price is much higher than the domestic price. Thus, it cannot be assumed that integrated lumber companies in Canada value log transfers or swaps at market prices simply based on the practice of such companies in the United States.

[51] *See* U.S. First Response to Panel Questions, paras. 7-8.

[52] *Id.* at para. 6.

[53] *Black's Law Dictionary* 100 (5th ed. 1979) (emphasis added) (Exhibit U.S.-34).

[54] *Id.* at 537 (emphasis added) (Exhibit U.S.-34). This is consistent with the "arm's-length" concept under Canadian law as well, which recognizes that certain transactions between unrelated persons may nevertheless be non arm's-length transactions "depending on all the circumstances." *See* IT-419R, Providing the Meaning of Arm's Length: Section 251 and 252 of the Income Tax Act, para. 15 (August 24, 1995) (Exhibit U.S.-35). Under Canadian law, "[f]ailure to carry out a transaction at fair market value may be indicative of a non-arm's-length transaction." *Id.* at para. 19. Canadian law notes that "[t]he key factor is whether there are separate economic interests which reflect ordinary commercial dealing between parties acting in their separate interests." *Id.*

[55] The notion that "arm's-length" transactions involve transactions between parties acting free from outside influences is supported by the language of footnote 59 of the SCM Agreement, which recognizes that, for tax purposes, the concept of "arm's-length" transactions refers to "transactions between *independent* enterprises . . . ." (emphasis added).

38. Canada claims that tenure holders are free to sell their logs to unrelated mills.[56] In fact, the record evidence demonstrates the contrary. For example, Quebec indicated that there were essentially no arm's-length transactions involving Crown timber sold by independent loggers to sawmills.[57] Moreover, the record establishes that all of the provinces generally require that Crown timber be processed in a mill within the province. Each province also imposes other restrictions that impede a harvester's ability to negotiate freely and that compel the harvester to sell to particular customers. For example, in Ontario, as a condition of the license, tenure holders are required to sign "wood supply agreements," in which they agree to supply specific quantities of wood to specific mills.[58] The licenses also provide that the Ministry of Natural Resources can direct excess log production to specific mills.[59] In British Columbia, major licensees are required by law to process their logs or an "equivalent volume" of wood in their mills.[60] Similarly, in Alberta, all licenses on the record specify a particular fixed volume that must be processed in a specific mill.[61] Moreover, the evidence shows that the so-called independent loggers often operate as employees or contractors for tenure holders.[62] In addition, Canada's claim of significant "sales" by independent harvesters includes transactions that are, in fact, "swaps."[63]

39. In light of this evidence, the only reasonable conclusion is that there are no true arm's-length transactions for Crown timber between independent loggers and lumber mills. There is therefore no basis for Canada's claim.

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[56] *See* Canada First Response to Panel Questions, para. 34.

[57] Questionnaire Response of the Government of Quebec, GOQ - Log Export Restrictions Narrative and Exhibits 1-12, p. 8 (June 28, 2001) ("Because TSFMA holders are allocated a volume of timber from the public forest for the express purpose of supplying their wood to processing mills, there is little interest in exporting or selling timber rather than processing it.") (Exhibit U.S.-36).

[58] Questionnaire Response of the Government of Ontario, Sample Section 26 SFL, p. 4, section 3.0 (June 28, 2001) (Exhibit U.S.-23).

[59] *Id.* at vol. 4, Exhibit ON-GEN-34, p. 7 (Exhibit U.S.-51).

[60] *See* U.S. First Response to Panel Questions, para. 2.

[61] *Id.* at para. 6.

[62] Questionnaire Response of the Government of British Columbia, vol. 15, p. BC-LER-45 (June 28, 2001) (Exhibit U.S.-52).

[63] Swap transactions involve two mills that are required to process all the timber they harvest or an "equivalent quantity" in their mill. Periodically, these mills harvest certain species and sizes that are not optimal for the requirements of their mills and product mix. The mills therefore agree to swap equivalent amounts of logs to optimize their mill operations. These are not sales.

D. The Preliminary Critical Circumstances Finding Is Consistent with the SCM Agreement

40. As fully discussed in the U.S. prior submissions, Canada has failed to make a *prima facie* case that the Commerce Department's preliminary critical circumstances finding was inconsistent with the SCM Agreement.[64] The Commerce Department's imposition of provisional measures in this case on merchandise entered during the 90-day period prior to the publication of the Preliminary Determination was in fact fully consistent with the text of Article 20 of the SCM Agreement, as well as with its object and purpose.

41. Article 20.1 expressly provides that the prospective application of provisional measures and final duties is "subject to the exceptions set out in this Article." Article 20.6 provides such an exception, stating that a Member may assess final, definitive duties retroactively for a period "not more than 90 days prior to the date of application of provisional measures" if critical circumstances are present. As discussed in the U.S. prior submissions, retroactive provisional measures (including suspension of liquidation and cash deposits or bonds) are essential to enable a Member to avail itself of the special remedy provided under Article 20.6.[65] It is therefore the view of the United States that a Member may impose retroactive provisional measures if there is a reasonable basis to believe or suspect at the time of the preliminary determination that critical circumstances exist.

42. With respect to Canada's remaining critical circumstances claims, the United States will, at this time, rely on its prior submissions.

E. U.S. Laws Governing Reviews Are Consistent with the SCM Agreement

43. No reviews have been requested, much less denied, in this case because the United States has not yet imposed definitive countervailing duties. Canada simply claims that the U.S. laws governing such reviews are inconsistent with the SCM Agreement. Under established WTO jurisprudence, however, a Member's law breaches that Member's WTO obligations only if the

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[64] *See* U.S. First Written Submission, paras. 85-101; U.S. First Oral Statement, paras. 34-36; U.S. First Response to Panel Questions, paras. 51-62.

[65] *See* U.S. First Written Submission, paras. 88-92; U.S. First Response to Panel Questions, paras. 55-58. *See also United States – Antidumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/R, Report of the Panel, as affirmed by the Appellate Body, adopted 23 August 2001, para. 7.155 (finding that Members have broad authority to take measures to preserve the right to retroactive relief in antidumping cases when the Member has reasonable cause to believe or suspect that critical circumstances exist and noting that "measures of a purely conservatory or precautionary kind . . . serve the purpose of preserving the possibility of later deciding to collect duties retroactively . . . .").

law *mandates* action that is inconsistent with those obligations. If the law provides discretion to authorities to act in a WTO-consistent matter, the law, as such, does not breach a Member's WTO obligations.

44. For the reasons fully discussed in the U.S. prior submissions, the U.S. laws that Canada challenges clearly do not mandate action inconsistent with U.S. WTO obligations. U.S. law instead gives the Commerce Department broad discretion to conduct reviews in a WTO-consistent manner.[66]

III. CONCLUSION

45. For the reasons set forth above, the United States requests that the Panel reject Canada's claims in their entirety.[67]

[66] *See* U.S. First Written Submission, paras. 105-116; U.S. First Oral Statement, paras. 38-41; U.S. First Response to Panel Questions, paras. 63-65.

[67] Canada asserts violations of Articles 10 and 32.1 of the SCM Agreement, which are dependent on the more specific claims addressed herein. The dependent claims are therefore also without merit for the reasons stated above.