As delivered

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

(WT/DS236)

Oral Statement of the United States of America at the First Meeting of the Panel

April 24, 2002

1. Thank you, Mr. Chairman, and members of the Panel. The United States appreciates this opportunity to present its views on the issues in this dispute, some of which go to the very heart of the disciplines established in the WTO *Agreement on Subsidies and Countervailing Measures* ("Subsidies Agreement").

2. Although some of the facts of this case are technically complex and can be confusing, in the end the issues are simple. The preliminary record below indicates that the Canadian provincial governments provide timber to lumber producers. The record also indicates that the provincial governments provide that timber at less than market prices. Under Article 1 of the Subsidies Agreement, that is not theory, that is a subsidy. Canada exports almost $7 billion of that subsidized lumber to the United States annually, which is more than half of Canada's total annual production of lumber and represents approximately 35% of the U.S. market for lumber.

3. The United States' countervailing measure is not a demand that Canada's forestry practices mimic the United States. It is a demand that the U.S. industry not pay the price for Canada's social and economic policies. Article 5 of the Subsidies Agreement states that "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 . . ." When one

Member causes injury to the domestic industry of another Member through the use of *any* subsidy, the injured Member has the right to take countervailing measures. The United States' preliminary decision to exercise that right was fully warranted in this case.

4. In our oral presentation, the United States will focus on only the principal arguments raised by Canada. We will, of course, be pleased to answer any questions the Panel may have.

Preliminary Subsidy Determination

5. The United States will turn first to Canada's challenge to the Commerce Department's preliminary determination that the Canadian provincial stumpage programs provide a subsidy to the Canadian softwood lumber industry.

6. Article 1.1 of the Subsidies Agreement defines a subsidy as a financial contribution by the government that confers a benefit. Thus, there are two elements to a subsidy: financial contribution and benefit.

Financial Contribution

7. With respect to the first element, the Commerce Department preliminarily determined that the system of timber contracts administered by the provincial governments in Canada constitutes a financial contribution within the meaning of Article 1.1(a)(1) of the Subsidies Agreement. Although Canada focuses on the complexities of these arrangements, none of those complexities alters the fundamental fact that these provincial programs provide timber to lumber producers.

8. Financial contribution, as defined in Article 1.1(a)(1) of the Subsidies Agreement, includes, under subparagraph (iii), the provision of "goods or services other than general

infrastructure." The Commerce Department preliminarily determined that the provincial governments in Canada provide a good through various types of timber contracts, which we collectively refer to as provincial "stumpage" programs. A brief review of some essential facts concerning the provincial stumpage programs demonstrates that the Commerce Department's preliminary finding was well-founded.

9. As noted in our first submission, over 90% of the forested land in Canada is held by the provincial governments. The timber on that land is what we refer to as Crown timber. Each province administers a system of contracts called tenures or licenses that allow the tenure holder or licensee to harvest the Crown timber. For ease of discussion we will refer to these instruments collectively as timber contracts.

10. Canada has stated that the provincial governments have stumpage programs to fulfill a variety of social, economic and forest management goals. However, such goals have no bearing on the question of whether Canada provides a subsidy through its stumpage programs. To the contrary, governments typically provide subsidies to advance various social and economic policies. The government's reasons for making a financial contribution are irrelevant under the Subsidies Agreement. As the European Communities (EC) has also noted, the Subsidies Agreement looks only to whether the government's financial contribution provides a benefit to the recipient. It is therefore from the perspective of the recipient that we examine subsidies under the Agreement.

11. There is no dispute that lumber producers participate in provincial timber contracts for one reason and one reason only – to obtain timber. Moreover, the definitions discussed in the

United States' submission leave no doubt that timber is a good within the ordinary meaning of Article 1.1(a)(1)(iii). As the EC has noted, from the reference in Article 1.1(a)(1)(iii) to goods and services other than "general infrastructure," it follows *a contrario* that any specific immovable object may be a covered good. (I would refer the Panel here to paragraph 26 of the U.S. submission. We did not rely on the definition of "property," but on the definition of "good.") Nevertheless, Canada argues that when the provinces issue these contracts they are not providing a good – timber – to the lumber producers. The thrust of Canada's argument is that the provincial timber contracts merely grant the lumber producers the *right to take* timber off the land. In Canada's view that does not constitute providing timber. Neither the Subsidies Agreement nor the facts of this case support Canada's claim.

12. In considering this issue, it is useful to review the essential facts concerning provincial timber contracts. Although there are some variations across the provinces, the core elements of all timber contracts are the same, that is, the lumber producer obtains the right to cut timber in a specified area in exchange for an administratively set fee, the "stumpage" fee, and the assumption of certain forest management obligations associated with the harvesting operations. The lumber producer knows the specific area in which it will be able to harvest and knows the timber, that is, the species and quality of the trees. The producer pays stumpage fees only for the volume of timber actually harvested. The lumber producer is therefore obtaining a specifically identified good – timber. From these facts alone, it should be obvious that, regardless of what Canada calls them or how complex Canada may make them appear, these arrangements are, in substance and purpose, contracts for the sale of timber. I would also note here that Canada states

that the stumpage fee is not a fee paid for the timber but is simply a tax. If so, this opens the question of what is the price paid for the timber. Perhaps it is zero.

13. Moreover, as the United States explained in its submission, the ordinary meaning of "provide" includes "make available." Thus, the fact that a lumber producer has to go get the timber off the stump is irrelevant. As the EC has noted, the economic consequences of providing a good or providing a right to a good are exactly the same. To treat them as distinct would invite circumvention of the subsidy disciplines and seriously undermine their purpose.

14. Given the ample evidence that the provinces are providing lumber producers with timber, Canada's only hope is that the Panel will read into the Subsidies Agreement an exemption for all extraction and harvesting rights. However, there is no support in the text for such an exemption, and a panel may not read into the Agreement what is not there. There is no safe harbor. Each case must be judged on its own merits. In this case, the facts are unquestionably sufficient to support the Commerce Department's preliminary determination that the Canadian provinces are providing a good – timber; therefore, a financial contribution exists.

Benefit

15. Having established a sufficient basis for the preliminary finding of a financial contribution, the next question is whether there is a benefit. I would simply note at the outset that the United States has not and does not argue that auctions are the only means to determine prices, as Canada suggests. The Commerce Department preliminarily determined that the provincial governments provide timber for less than adequate remuneration, within the meaning of Article 14(d) of the Subsidies Agreement, thereby conferring a benefit. Canada claims that the

Commerce Department's methodology for calculating the subsidy benefit was inconsistent with the Subsidies Agreement in several respects. Although the United States has rebutted all of those claims in its submission, it may be helpful to highlight a few points and clarify some facts.

Cross-Border Benchmark

16. The benefit from the provision of goods is not a theoretical market distortion. As the Appellate Body has confirmed, a benefit is conferred when the government's financial contribution places the recipient in a more advantageous position than would have been the case absent the financial contribution. Moreover, the Appellate Body has recognized that the marketplace provides an appropriate basis for comparison to identify the trade-distorting potential of a government's financial contribution. In the underlying investigation, the Commerce Department preliminarily determined that no market benchmarks existed in Canada. The Department therefore used stumpage prices in U.S. states with comparable forests, adjusted to reflect prevailing market conditions in Canada. Canada claims that the Commerce Department's preliminary decision to use those prices to measure the benefit from provincial stumpage programs is inconsistent with Article 14(d) of the Subsidies Agreement.

17. Article 14(d) states that: "The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale)." Canada ignores most of that language and argues, in effect, that Article 14(d) says: "The adequacy of remuneration shall be determined in the country of provision or

purchase." The treaty interpreter, however, must give meaning to all the words in the Agreement.

18. Consistent with the findings of the Appellate Body, an appropriate benchmark is one that represents what the recipient of the goods would pay absent the subsidy. The United States believes that, if there is a domestic price untainted by the subsidy, that price would normally provide the most appropriate benchmark. However, we agree with the EC that world market prices can constitute part of the "market conditions in the country of provision." As the EC points out, the relevance of world market prices is recognized in item (d) of the Illustrative List of Export Subsidies in Annex I of the Subsidies Agreement. Thus, where the domestic market does not provide an appropriate benchmark, world market prices may be used to measure the subsidy benefit.

19. Therefore, the question is not whether Article 14(d) permits a Member to use something other than a domestic benchmark price, but rather when it is appropriate to do so. The facts, as discussed in the preliminary determination, more than adequately support the Commerce Department's preliminary decision to do so in this case. We will take a moment briefly to review those facts.

20. As noted previously, 90% of the forested land in Canada is held by the Crown. The market for timber is therefore dominated by the provincial governments. While they are not the sole provider, at 90% the impact of the governments' administratively set prices on the very small residual market is virtually inescapable. Nevertheless, the Commerce Department did request information on private prices in each of the provinces. Only three of the provinces

responded to that request, and the Commerce Department determined that the prices they provided were not market-based. For example, Quebec provided private prices from an annual survey. However, the record contained statements by a Quebec official and a Canadian forestry expert acknowledging that private timber prices in the province are suppressed by the overwhelming market power of low-cost Crown timber.

21. When viewed as a whole, the governments' dominance of the market, the absence of private price information for much of Canada, and the evidence of price suppression in the private market provided more than a reasonable basis to support the Commerce Department's preliminary determination that the private market in Canada could not provide a market price that was unaffected by the very trade distortion that Article 14(d) is intended to identify.

22. The EC questions why, if private prices in Canada are distorted by the provincial stumpage programs, the U.S. prices would not be similarly distorted by those programs. The answer is that the market for Crown timber and logs is effectively closed to producers outside Canada. Thus, Canadian stumpage programs are not part of the market conditions in the United States and therefore cannot distort the U.S. market. In contrast, the vast majority of the U.S. stumpage and log market is open to, and used by, Canadian lumber producers. Thus, it does represent part of the market available to Canadian producers.

23. Moreover, the U.S. stumpage and log prices are market based. The U.S. market is dominated by private timber sales and the small amount of government sales are made through competitive, public auctions. Therefore, while the evidence indicates that private prices in

Canada are distorted, the U.S. prices remain a valid benchmark to measure what Canadian producers would pay for timber, absent the governments' financial contribution.

24. It is evident why Canada would insist that the United States use prices in Canada despite the evidence of a market overwhelmingly dominated and dictated by the provincial governments. Canada would, in effect, require the United States to measure the governments' prices against prices that reflect the very distortion that we are attempting to measure. Article 14(d), however, does not require such an obviously flawed and circular methodology.

Benefit Calculation - Indirect Subsidies (Pass-Through)

25. Canada also argues that certain aspects of the Commerce Department's methodology in the preliminary determination overstated the amount of the subsidy. As explained in the United States' submission, the Commerce Department determined the total amount of the subsidy provided to Canadian producers of the subject merchandise based on aggregate data from the provincial governments. The Department then divided the total subsidy by total sales of the subject merchandise to obtain the subsidy rate. Canada claims that the Commerce Department's calculation improperly assumed that benefits to tenure holders passed through to lumber producers. The United States does not, as the EC suggests, concede that this is the case. Some clarification of the facts is necessary to better understand the basis for the Commerce Department's subsidy calculation and shed light on the flaws in Canada's claim.

26. First, I would point out that an input subsidy under Article 1.1(a)(1)(iii) is a direct subsidy. Under Canada's interpretation, all financial contributions through the provision of a good are transformed into an indirect subsidy under Article 1.1(a)(1)(iv). In reading Canada's

submission, one could get the impression that there are three distinct industries in Canada: loggers, lumber producers and remanufacturers. That is not the case. The vast majority of the Crown softwood timber is harvested under timber contracts held by integrated producers, i.e., lumber mills have provincial tenures to obtain the timber that they process into lumber and, in some cases, remanufactured products.

27. It is also important to bear in mind that the subsidy benefit calculation was based solely on the portion of the Crown harvest that actually goes into sawmills to produce lumber. The record evidence at the preliminary determination indicates that the overwhelming portion of that timber is harvested under timber contracts held by the lumber mills.

28. To understand the evidentiary basis for the preliminary subsidy calculation, it is important to understand how the Canadian stumpage programs operate. Otherwise, some of the underlying data can be misleading. For example, some wood processing facilities produce forest products that are not within the scope of the underlying investigation, such as plywood mills. The Commerce Department did not include timber that goes to such facilities in the calculation of the total subsidy. Therefore, data on the proportion of the harvest that goes to *all* entities that own and operate a wood processing facility is irrelevant.

29. The vast majority of the timber contracts in Canada are directly between the provincial governments and Canadian forest products producers, which we refer to generally as wood processing facilities. In most instances in fact, only wood processing facilities, such as sawmills that produce lumber, are eligible to obtain a timber contract. For example, the Quebec Forest Act states that: "No one except a person authorized to construct or operate a wood processing plant is

qualified to enter into" a Timber Supply Forest Management Agreement, which is the major type of timber contract in Quebec (Forest Act § 37). Similarly, in British Columbia all but a very small portion of the harvest is covered by timber contracts that, by law, are available only to companies that own or operate a wood processing plant in Canada. The information submitted by Ontario also states that, generally, timber contracts are only available to companies that have a wood processing facility in Canada or a contract to supply the timber to such a facility. Moreover, record evidence indicates that the so-called "independent" log markets in some of the provinces are, in fact, composed of log-swapping by the large tenure holders. Thus, Canada's alleged middleman between the provincial governments and the lumber producers is largely a myth.

Benefit Calculation - Denominator

30. Canada also claims that the Commerce Department should have included non-subject merchandise in the calculation of the subsidy. The subsidy calculation consists of a numerator, which is the total benefit to the subject merchandise, and a denominator, which is the total sales of the subject merchandise. On this point, the United States would refer the Panel to paragraph 58 of our submission on the exclusion of Maritime lumber from the scope of the investigation. This was an exclusion for certain products, not producers.

31. Canada argues that the Department was required to use different bases to calculate the numerator and the denominator. Specifically, Canada argues that the calculation of the benefit (that is, the numerator) must exclude Maritime lumber, but the denominator must include the Maritime lumber. As the United States explained in its submission, Canada's reasoning rests on

fundamental misconceptions about the scope of the investigation and would, in fact, result in a countervailing duty rate less than the subsidy found to exist with respect to the subject merchandise.

32. Ironically, while on the one hand Canada claims that the Commerce Department was required to calculate the numerator and denominator on different bases, on the other hand Canada claims that the Commerce Department improperly calculated the subsidy rate on one basis and applied it on another. Specifically, Canada argues that the Commerce Department calculated the subsidy on the basis of the total value of first milled lumber products, but then applied the subsidy rate to the entered value of subject merchandise.

33. Canada's claim ignores the fact that the Department's calculation and application of the subsidy rate was entirely consistent with the record before the Department at the time of the preliminary determination. Although Canada subsequently clarified the information it had provided, an investigating authority is not required to predict the future. As previous panels have stated, the consistency of an authority's decisions must be assessed based on an objective assessment of the facts before the authority at the time the decision was made. I would also clarify that it is not based on the facts "used" by the investigating authority, but on the facts "before" the investigating authority. Under the proper standard of review, the facts demonstrate that the preliminary determination is entirely consistent with the United States' obligations under the Subsidies Agreement.

Critical Circumstances

34. Canada's second group of claims relate to the Commerce Department's imposition of retroactive provisional measures pursuant to its preliminary determination that critical circumstances exist within the meaning of Article 20.6 of the Subsidies Agreement. Canada's claim rests on an interpretation of Article 20.6 that would render the retroactive remedies provided for a nullity. It is beyond dispute that the general principles of treaty interpretation preclude such a reading of the Agreement.

35. The general rule in Article 21 that provisional measures and definitive duties are applied prospectively is expressly made "subject to the exceptions set out in [Article 20]." Nothing in the text of Article 20.1 limits the applicability of those exceptions to definitive countervailing duties. It is in interpreting the language of Article 20.1 that the United States has commended to the Panel the reasoning of the *Hot Rolled* panel. While it is true that the Subsidies Agreement does not contain a counterpart to Article 10.7 of the Antidumping Agreement, the *Hot Rolled* panel explained that Article 10.7 is a timing mechanism that allows imposition of certain precautionary measures. We are not asserting the right to take precautionary measures here, but just the right to take provisional measures as allowed by Article 17 of the Subsidies Agreement.

36. Article 20.6 defines a set of exceptional circumstances that warrant retroactive relief. Under the text of Article 20.1 those exceptional circumstances apply to provisional measures. Accordingly, the Panel should find that the United States' retroactive imposition of provisional measures was consistent with the Subsidies Agreement.

Reviews

37. Finally, Canada claims that various provisions of U.S. law are inconsistent with its obligations under the Subsidies Agreement because they preclude reviews in aggregate cases. As explained in our submission, under established WTO jurisprudence, a Member's law violates that Member's WTO obligations only if the law *mandates* action that is inconsistent with those obligations. If the law provides discretion to authorities to act in a WTO-consistent manner, the law, as such, does not violate a Member's WTO obligations.

38. U.S. law provides the Commerce Department with ample discretion to conduct expedited and administrative reviews in all cases, including aggregate cases. I take issue with Canada's statement that Section 751 of the Act does not provide such discretion. That is not in fact the case. Section 751 provides that the Department must review the order at least once every 12 months upon request. Nothing in the regulations cited by Canada limits that discretion. Thus, U.S. law does not mandate action that is inconsistent with the United States' WTO obligations. The United States is therefore entitled to the presumption that it will implement its obligations in good faith.

39. I would like to make a few additional points about Canada's characterization of U.S. law. First, it is not unusual for the United States to delay codification of obligations until we obtain more experience. In our submission, we cited to a Supreme Court case that says that the absence of regulations does not limit statutory discretion.

40. Moreover, the preambular language that Canada cites addresses administrative reviews, not expedited reviews, and preambular language has no binding effect. In addition, rules governing voluntary respondents have no bearing on the rules governing administrative reviews.

41. Finally, Canada refers to Article 21.2 and *British Steel*. I would simply note that Article 21.2 refers to reviews of the need for continued imposition of the duty, not assessment rates. The issue in *British Steel* was whether the companies had received any subsidies or the subsidies had been extinguished. Article 21.2 is limited solely to the determination of whether a continued duty is warranted and, if not, to terminate it. This is a prospective inquiry, and fundamentally different from an assessment review.

Conclusion

42. That concludes the United States' oral presentation, which we hope the Panel finds useful in understanding and resolving the issues presented. Thank you for undertaking that task.