TABLE OF CASES CITED IN THIS SUBMISSION

Appellate Body Report	*United States - Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, Report of the Appellate Body, WT/DS257/AB/R, adopted 17 February 2004.
Panel Report	*United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, Report of the Panel, WT/DS257/R, adopted 17 February 2004.
Canada – Aircraft	*Canada – Measures Affecting the Export of Civilian Aircraft*, Report of the Appellate Body, WT/DS70/AB/R, adopted 20 August 1999.

US – Canadian PbrP34.5 re21p6 Tw(t)4.4(o)-1(C)4.eo

TABLE OF ABBREVIATIONS USED IN THIS SUBMISSION

Alberta 21 May 2004 Pass-Through Questionnaire Response	Response of the Government of Alberta to the Department's 14 April 2004 Questionnaire Concerning Pass Through of

Manitoba 12 November 2003 AR Questionnaire Response	Response of the Government of Manitoba to the Department's 12 September 2003 Questionnaire (12 November 2003) (Exhibit CDA-47).
Norcon A	Response of the Government of British Columbia to the Department's April 14, 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Exhibit BC-PT-18 (Letter from Steptoe & Johnson to Akin, Gump, Strauss, Hauer & Feld (20 May 2004) attaching *Survey of Primary Sawmills' Arm's Length Log Purchases In the Province of British Columbia* (21 December 2001), filed with Letter from Steptoe & Johnson to USDOC (21 December 2001)) (Exhibit CDA-30).
Norcon B	Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Exhibit BC-PT-40 (*Supplemental Report on Survey of Primary Sawmills' Arm's Length Log Purchases In the Province of British Columbia* (14 September 2004)) (Exhibit CDA-15).
Norcon C	Norcon Forestry Ltd., *Survey of Primary Sawmills' Arm's Length Log Purchases in British Columbia* (15 March 2004), submitted with Letter from Steptoe & Johnson to USDOC (15 March 2004) (Exhibit CDA-31).
OFIA/OLMA 15 September 2004 Supp. Questionnaire Response	Response of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association on behalf of their members to the Department's 17 August 2004 Questionnaire Concerning Pass Through of Alleged Benefits (16 September 2004) (Exhibit CDA-49).
OFIA/OLMA 25 October 2004 Supp. Questionnaire Response	Response of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association on behalf of their members to the Department's 5 October 2004 2nd Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (26 October 2004) (Exhibit CDA-50).
Ontario 21 May 2004 Pass-Through Questionnaire Response	Response of the Government of Ontario to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004) (Exhibit CDA-48).
Preliminary AR Determination	*Notice of Preliminary Results of Countervailing Duty Administrative Review: Certain Softwood Lumber from Canada*, 69 Fed. Reg. 33,204 (Dep't Commerce, 14 June 2004) (Exhibit CDA-10).
SAA	"Statement of Administrative Action" in *Message from the President of the United States Transmitting the Uruguay Round Agreements, Texts of Agreements Implementing Bill, Statement of Administrative Action and Required Supporting Statements*, H.R. Doc. No. 103-316, vol. 1 at 656 (Exhibit CDA-1).
Saskatchewan 21 May 2004 Pass-Through Questionnaire Response	Response of the Government of Saskatchewan to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (May 21, 2004) (Exhibit CDA-39).
Saskatchewan 12 November 2003 AR Questionnaire Response	Response of the Government of Saskatchwan to the Department's 12 September 2003 Questionnaire (12 November 2003) (Exhibit CDA-42).
SCM Agreement	*Agreement on Subsidies and Countervailing Measures*
USDOC	United States Department of Commerce

Weyerhaeuser 16 September 2004 Supp. Pass-Through Questionnaire Response	Response of Weyerhaeuser Company to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (September 16, 2004) (Exhibit CDA-40).
Weyerhaeuser 26 October 2004 Supp. Pass-Through Questionnaire Response	Response of Weyerhaeuser Company to the Department's Second WTO Supplemental Pass-Through Questionnaire (26 October 2004) (Exhibit CDA-41).

I. INTRODUCTION

1. This case is about the failure of the United States to implement the recommendations and rulings of the DSB in respect of its obligation to demonstrate whether, and to what extent, an input subsidy passes through arm's-length sales of input products. Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement require the United States to demonstrate such a "pass through" as a precondition to imposing countervailing duties on downstream products produced from

B. DSB Recommendations and Rulings Concerning the US Failure to Demonstrate Pass-Through

17. The United States imposes countervailing duties on imports of certain Canadian softwood lumber products based on the USDOC determination that Canadian provincial stumpage programmes subsidize the production of softwood lumber. Stumpage programmes impose obligations such as the payment of fees, road construction and maintenance requirements, and fire protection and insect and disease control, in exchange for rights to harvest standing timber on public lands. Standing timber is harvested and processed into logs.[6] Logs may then serve as inputs for further processing in, *inter alia*, sawmills and pulp mills to produce a wide variety of forest products, including softwood lumber. These facts, as confirmed by the original panel and the Appellate Body, as well as by the panel in *US – Softwood Lumber III*, have not changed since the initiation of the US countervailing duty investigation.[7]

18. On the basis of these facts, the original panel found that the USDOC was required to conduct page pr18

cases, comprehensive data on sawmill-to-sawmill transaction volumes.[16] Annex I contains a detailed explanation of the volumes of record evidence submitted by Canadian provinces and industry associations. For example, British Columbia provided the USDOC with a survey demonstrating that 11.6 per cent of Crown logs consumed in B.C. sawmills were purchased from unrelated non-lumber-producing tenure holders.[17] The survey also demonstrated that an additional 6.2 per cent of Crown logs consumed in B.C. sawmills were purchased in
producing tenre holders.

in the amount of the countervailing duty imposed by 0.17 percentage points (*i.e.*, from 18.79 per cent to 18.62 per cent), which came into force on 10 December 2004.[24]

28. On 13 December 2004, the USDOC released the final results of its administrative review, which contained no pass-through analysis despite arguments and evidence supplied by Canadian respondents that would have enabled the USDOC to conduct one. The revised countervailing duty amount resulting from the administrative review came into force on 20 December 2004.[25] Accordingly, ten days after the final section 129 determination came into force, subsequent action of the USDOC rendered moot the minor pass-through adjustment resulting from it.

2. The Administrative Review

29. The United States uses a "retrospective" duty assessment system to periodically review the amount of any countervailing duty imposed as a result of an original final countervailing duty determination. Where no administrative review is requested by an "interested party", final assessment occurs at the amount of the countervailing duty established in the original determination. Where an administrative review is conducted, the USDOC reviews data for a period of approximately one year from the date of first imposition of final duties (the "period of review"). The revised amount of the countervailing duty "

transactions, the purchasing sawmill paid the government stumpage charge rather than the independent harvester.[29]

33. The USDOC issued the final results of its administrative review on 13 December 2004.[30] In its final results, the USDOC mirrored the approach it took in its final section 129 determination and reproduced its discussion of the same five "factors" as the basis for not conducting a pass-through analysis for any of the transactions in question.[31] It applied these factors to reject all record evidence provided by the Canadian respondents, and determined that each province "failed to substantiate its claim that logs entering sawmills during the [period of review] included logs purchased in arm's-length transactions."[32]

34. As mentioned, the amount of the countervailing duty established in the administrative review superseded the amount adjusted as a result of its section 129 determination ten days after the latter came into force, thereby rendering any purported "prompt compliance with recommendations or rulings of the DSB" under Article 21.1 of the DSU of no effect.

III. LEGAL ARGUMENT

35. The United States continues to violate its obligations under Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement on three fronts.

36. First, the USDOC failed in both the 129 determination and the final results of the administrative review to collect or analyze record evidence pertaining to log transactions between tenured sawmills. It offered no explanation in its determinations or questionnaires for its disregard of the DSB recommendations and rulings in this respect.

37. Second, in its section 129 determination, the USDOC failed to analyze whether, and to what extent, a subsidy pass-through occurred for the vast majority of independent harvester transactions identified in the record evidence, and failed to do so for all such transactions in its administrative review. To justify this failure in its section 129 determination, the USDOC claimed that such analysis may only be done on a company-specific, transaction-by-transaction basis. This claim is without basis, and fails to take into account the efforts of the Canadian respondents to provide the necessary information in the context of an aggregate case.

38. The USDOC also justified its failure to conduct a pass-through analysis in both its section 129 and administrative review determinations by claiming that unrelated parties do not operate at "arm's length" from each other if any one of five factors external to the transaction exists. There is no basis for the USDOC position under the GATT 1994 and the SCM Agreement, or in the findings of either the original panel or the Appellate Body. Its position also contradicts fundamental principles of economics. The USDOC is required to conduct a pass-through analysis, which involves comparisons to market benchmarks, where the direct recipient of an alleged benefit – the producer of the input product (in this case, logs) – is not the same entity as the indirect recipient of the benefit – the producer of the further processed product (in this case, softwood lumber). The United States may not now evade this obligation by disregarding transactions as being not at "arm's length" on the basis of an unfounded standard.

39. Third, even in the few instances in its section 129 determination where the USDOC considered log transactions, it nevertheless failed to conduct a proper analysis under Article 1.1(b) of

the SCM Agreement because most of the benchmarks it used did not reflect prevailing market conditions for logs in Canada.

40. Thus, for the vast majority of transactions in its section 129 determination and for all transactions in its administrative review, the USDOC conducted no pass-through analysis, and where it purported to conduct such analysis, it did so incorrectly. As a result, the USDOC continues impermissibly to presume a pass-through of the alleged input subsidy. In this dispute, the original panel and the Appellate Body have already confirmed that such a presumption is a violation of WTO obligations.

45. Nothing in the context or object and purpose of these provisions alters the fundamental obligation to demonstrate the existence and the amount of a subsidy with respect to a product before imposing countervailing duties on that product.[34]

46. Article 1.1 of the SCM Agreement sets out an exhaustive definition of "subsidy" that applies to this obligation.[35] Under this provision, there is no "subsidy" when a "benefit" has not been conferred upon a recipient.[36] The original panel, referring to the findings of the Appellate Body in *Canada – Aircraft*, found that the term "benefit" "implies some kind of comparison" and that the "marketplace" provides a basis for this comparison.[37]

47. In a pass-through context, the obligation on Members is to compare the transactions in question to the marketplace to determine whether, and to what extent, a benefit under Article 1.1(b) of the SCM Agreement is conferred.[38] As explained by the original panel, the results of such analysis may not be presumed:

> The heart of the pass-through issue is whether, where a subsidy is received by someone other than the producer or exporter of the product under investigation, the subsidy nevertheless can be said to have conferred benefits in respect of that product. If it is not demonstrated that there has been such a pass-through of subsidies from the subsidy recipient to the producer or exporter of the product, then it cannot be said that subsidization in respect of that product, in the sense of Article 10, footnote 36, and Article VI:3 of GATT 1994, has been found. Thus, we find that a pass-through analysis is required by these provisions … where there are such upstream transactions.[39]

---

[34] See Panel Report, at paras. 7.90-7.91 ("[B]oth of these provisions make explicit that there must be direct or indirect *subsidization* in relation to the manufacture, production or export of a *product* for a 'countervailing duty' in the sense of the [SCM] Agreement and GATT Article VI to be imposed on that product." [emphasis in original]. See also *US – Softwood Lumber III*, at paras. 7.75, 8.1(c), and *US – Countervailing Measures on Certain EC Products*, Panel Report, at paras. 7.41-7.44, as upheld in

48. Accordingly, where a subsidy is received by "someone other than the producer or exporter of the product under investigation", a Member must establish whether and to what extent the benefit to an upstream recipient passes to a downstream entity through the purchase of an input product.

49. The Appellate Body agreed. Drawing on the text of Article VI:3 of the GATT 1994, it found that a Member may not presume that a subsidy passes through transactions where "the producer of the input is not the same entity as the producer of the processed product".[40] The Appellate Body also explained in no uncertain terms that analysis under Article 1.1(b) of the SCM Agreement is required:

> Where a subsidy is conferred on input products, and the countervailing duty is imposed on processed products, the initial recipient of the subsidy and the producer of the eventually countervailed product, may not be the same. In such a case, there is a *direct recipient* of the benefit – the producer of the *input* product. When the input is subsequently processed, the producer of the *processed product* is an *indirect recipient* of the benefit – provided it can be established that the benefit flowing from the input subsidy is passed through, at least in part, to the processed product. Where the input producers and producers of the processed products operate at *arm's length*, the pass-through of input subsidy benefits from the direct recipients to the indirect recipients downstream cannot simply be presumed; it must be established by the investigating authority.

58. Second, in its section 129 determination, the USDOC disregarded all aggregate transaction and pricing data submitted by the Canadian respondents. The USDOC considered only information on a company-specific, transaction-by-transaction basis knowing that there were hundreds of thousands of eligible transactions made by thousands of companies.[46] The USDOC disregarded such evidence even though its investigation was undertaken on an aggregate basis precisely because there are thousands of companies involved.[47] The USDOC thus ignored entirely the original panel's views that company-specific data are not necessarily required to conduct pass-through analysis.[48] The USDOC stated only that, while the aggregate information provided by the Canadian parties is sufficient for certain analyses undertaken in the context of its aggregate case, "such data is not sufficient for the purposes of our pass-through analysis."[49]

59. Third, in both its section 129 and administrative review determinations, the USDOC applied a contrived standard to limit the number of Crown log transactions requiring analysis. In the USDOC view, a log transaction requires analysis only if it is at arm's length, and a transaction is at arm's length only where:

- the transacting parties are unrelated; *and*
- none of the external factors identified by the USDOC exists.[50]

60. While the USDOC did not contest that the Crown log volumes identified by the Canadian respondents satisfy this first condition, it nevertheless rejected nearly all remaining transactions in its

---

Province of Saskatchewan, Questions III, (D), (E) and (F), at VIII-4 (Exhibit CDA-9). See also Preliminary AR Determination, 69 Fed. Reg., at 33,208 (Exhibit CDA-10).

[46] See *e.g.*, B.C. September 15, 2004 Supp. Questionnaire Response, Narrative, at 5 and Norcon B, at 4 (Exhibit CDA-15).

[47] USDOC Memorandum from B.T. Carreau to F. Shirzad, *Issues and Decision Memorandum: Final Results of the Countervailing Duty Investigation of Certain Softwood Lumber Products from Canada* (21 March 2001), at 15 (Exhibit CDA-16) ("In the Initiation Notice, we stated that, due to the extraordinarily large number of Canadian producers, we anticipated that we would conduct this investigation on an aggregate basis consistent with section 777A(e)(2)(B) of the Act. No parties objected to this. [footnote omitted] For the purposes of this final determination, we have aggregated the subsidy information on an industry-wide basis. Specifically, we used the information provided by the [Government of Canada] and the Provincial governments and calculated one subsidy rate for the Canadian softwo

the transacting parties act in accordance with interests other than their own, nor do they align the parties' otherwise opposing objectives regarding the outcome of the transaction.[58] Accordingly, they do not obviate the need to demonstrate and quantify any alleged log subsidy pass-through.

64. In particular, record economic evidence demonstrated that the government regulations identified by the USDOC do not change the fact that transactions between unrelated parties occur in a market setting, and that a market absent of any form of government intervention is not a *sine qua non* for an arm's-length transaction.[59] Requirements by the government to supply, for example, say nothing about the subsequent negotiations and whether the transaction outcome is a market price. The evidence also demonstrated that the question of who remits the government stumpage fee is irrelevant; the mere payment of the fee by a downstream purchaser does not mean the upstream seller reduced the market value of its log by the amount of the stumpage subsidy.[60] This typical business arrangement, merely guaranteeing payment of base fees, logically has nothing to do with whether a transaction is at arm's length. Nor does the presence of non-cash components in a transaction (*e.g.*, payment through exchange of goods or services) imply that the harvester has accepted anything less than the market value of the log.[61]

65. As a result of its refusal to analyze log transactions as required by the findings of the original panel and the Appellate Body and by basic principles of economics, the USDOC impermissibly presumed that the alleged log input subsidy

in the administrative review. Accordingly, in both its determinations, occurring within days of each other, the United States failed to conform to its obligations concerning the imposition of countervailing duties.

3. As a Result of Its Failure to Conduct the Required Pass-Through Analysis, the United States Continues Impermissibly to Inflate the Amount of Countervailing Duties

ANNEX I: RECORD EVIDENCE

73. The Canadian respondents provided the USDOC with detailed evidence that could have been used to properly establish and calculate the amount of any benefit pass-through in both the section 129 proceedings and the administrative review. As explained, the United States rejected nearly all of the record evidence and instead simply presumed a full pass-through.

74. After initiating implementation proceedings under section 129, the USDOC issued a first questionnaire on 14 April 2004.[65] The Canadian respondents provided responses in accordance with the USDOC's directions on 21 May 2004. In providing their responses, the provinces relied on the definition of "affiliated person" under US law to certify whether the transacting parties were unrelated and the USDOC accepted all such certifications.[66]

75. After receiving responses to its first questionnaire, the USDOC issued two supplemental "pass-through" questionnaires on 17 August and 5 October 2004, requesting the provinces to collect large amounts of company-specific data.[67] The USDOC asked the provinces to collect the government tenure agreements applying to every independent harvester and sawmill involved in arm's-length log transactions.[68] The USDOC also requested information on all parties related to (*i.e.*, affiliated with) both the independent harvester and the purchasing sawmill, on who paid the stumpage fee related to the log in question, and on the contractual terms and pricing of each individual transaction that required a pass-through analysis.[69]

---

[65] Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO "Pass-Through" Questionnaire (April 14, 2004) (Exhibit CDA-3).

[66] See *e.g.*, Final 129 Determination, at 9 (Exhibit CDA-5) ("Based on the certifications and

76. The Canadian respondents provided as much information as was practicably available to them and emphasized that the USDOC could complete its pass-through analysis with the aggregate provincial data.[70] For example, in meetings and written submissions to the USDOC, British Columbia noted that the documentation relating to all log purchase agreements and tenure agreements would involve several truckloads of paper, and offered several alternative approaches, all of which were rejected. British Columbia nevertheless provided hundreds of pages of sample agreements, and offered to provide any additional samples requested by the USDOC. As outlined above, the USDOC rejected almost all record evidence submitted in the section 129 proceeding.

77. In relation to the administrative review, the USDOC initiated this segment of this proceeding on 1 July 2003, for the period from 22 May 2002–31 March 2003.[71] In its initial questionnaire issued on 12 September 2003, the USDOC requested the Canadian provinces to report the volume and value of Crown logs sold by independent harvesters to unrelated lumber producers, but solicited no information on sawmill-to-sawmill transactions.[72] The Canadian respondents provided the USDOC with evidence that confirmed that there was a significant volume of logs sold in such transactions and which therefore required a pass-through analysis.[73] The Canadian parties also provided additional information throughout the proceedings and during verification. The USDOC collected no additional information and issued no new questionnaires concerning pass-through. In the preliminary and final results of the administrative review, the USDOC refused to conduct a pass-through analysis using any of the information provided by the Canadian respondents.[74]

Ontario, Question 1, at 7; Alberta, Questions 5, 8, 10, at 9-10; Manitoba, Question 1, at 11; Saskatchewan, Question 1, at 13, Second Pass-Through Appendix, at 22-23 (Exhibit CDA-24).

[70] See *e.g.*, B.C. 15 September 2004 Supp. Questionnaire Response, Narrative, at 5 and Norcon B, at 4 (Exhibit CDA-15); B.C. 5 October 2004 Supp. Questionnaire Response, at BC-PT-22, Exhibit BC-PT-55 (Exhibit CDA-25). The public version of Exhibit BC-PT-55, which supplements the information provided in Norcon B, excludes business proprietary information as it is not susceptible to public summarization.

[71] *Initiation of Antidumping and Countervailing Duty Administrative Reviews and Request for Revocation in Part*, 68 Fed. Reg. 39,055 (Dep't Commerce 1 July 2003) (Exhibit CDA-26). On 16 January 2004, the USDOC extended the time for completion of the preliminary results. See *Certain Softwood Lumber Products from Canada: Extension of Time Limit for Preliminary Results of Countervailing Duty Administrative Review*, 69 Fed. Reg. 2,568 (Dep't Commerce 16 January 2004) (Exhibit CDA-27). Similarly, in the preliminary results the USDOC extended the amount of time available for the final results of the administrative review. See Preliminary AR Determination, 69 Fed. Reg. at 33,205 (Exhibit CDA-10).

[72] See Letter from USDOC to Embassy of Canada, *Countervailing Duty Administrative Review: Certain Softwood Lumber Products from Canada* (12 September 2003), attaching Questionnaire for the Province of Alberta, Questions III (J), (K), and (L), at III-6; Questionnaire for the Province of British Columbia, Questions III (K), (L), and (M), at IV-7; Questionnaire for the Province of Manitoba, Questions III, (D), (E) and (F), at V-5; Questionnaire for the Province of Ontario, Questions III, (K) and (L), at VI-6; and Questionnaire for the Province of Saskatchewan, Questions III, (D), (E) and (F), at VIII-4 (Exhibit CDA-9); and Preliminary AR Determination, 69 Fed. Reg. at 33, 208 (Exhibit CDA-10) ("During the underlying investigation, the

B. Alberta

81. Alberta used a computer database for the section 129 proceedings to identify the volume of softwood logs sold by: (1) harvesters who did not own sawmills; and (2) harvesters that did own sawmills but that did not supply these sawmills with Crown logs from their own tenure. Alberta provided this data to PricewaterhouseCoopers, who conducted a confidential survey of the recipients of these logs.[84] The confidential survey requested that the recipient sawmills identify whether each transaction was a purchase and whether the transaction involved an unrelated vendor using the definition of "affiliated" found in section 771(33) of the *Tariff Act of 1930*. PricewaterhouseCoopers then used the survey results to determine the volume of logs sold between unrelated parties.[85] The report contained confidential company-specific data on the total qualifying transactions for each company broken down by vendors without sawmills and vendors who were not selling from sawmill-related tenures.[86] Alberta demonstrated on this basis that there were some 730,618 cubic metres of arm's-length transactions between unrelated entities.[87]

82. Alberta also provided the USDOC in the administrative review with evidence that 2,399,893 cubic metres of logs were transferred to sawmills from unrelated parties in the period of review.[88] Furthermore, Alberta demonstrated that some 1,724,826 cubic metres of logs moved from unrelated parties to the 15 largest lumber-producing mills.[89] Alberta indicated that these data likely represented both cash sales and other forms of transactions (*e.g.*, log swaps). Alberta also provided evidence showing that a total of 1,513,171 cubic metres of logs were purchased in "cash transactions" by mills from unrelated entities, from both Crown and private sources.[90]

C. Saskatchewan

83. In the section 129 proceeding, Saskatchewan provided evidence that Forest Product Permit ("FPP") licensees that did not own sawmills sold some 81,403 cubic metres of logs, which represented approximately 4.9 per cent of the Crown harvest in the period of investigation.[91] Saskatchewan collected this evidence through "woodflow reports" maintained in six sawmills as a condition of their tenure.[92] These "woodflow reports" listed the source of all logs processed in these sawmills. Saskatchewan also requested that sawmills identify whethe

licensees. Saskatchewan and Weyerhaeuser also provided additional company-specific evidence to the USDOC in response to the supplemental questionnaires.[93]

84. Saskatchewan provided evidence concerning transactions between independent harvesters and unrelated sawmills in the administrative review. In particular, this evidence demonstrated that licensees that did not hold a license to operate sawmills harvested 173,766 cubic metres of Crown timber during the period of review.[94] Saskatchewan also submitted business proprietary evidence that demonstrated that at least 3.8 per cent of the softwood logs were sold by independent harvesters to unrelated sawmills.

D. Manitoba

85. Manitoba provided evidence during the section 129 proceeding that some 48,100 cubic metres or 8.7 per cent of timber harvested from Crown land was sold by Timber Sales Agreement ("TSA") licensees that did not own sawmills.[95] Manitoba requested that these TSA licensees provide certification of: (1) the volume of their Crown harvest; (2) the identity of the purchasing sawmills; and (3) whether they were related to the purchasing sawmills.[96]

86. In the administrative review, Manitoba demonstrated that "independent loggers," *i.e.*, those TSA licensees and Quota holders that did not own sawmills, harvested 61,583 cubic metres or 4.45 per cent of the total Crown harvest of logs in the period of review.[97]

E. Ontario

87. Ontario provided the USDOC with the requested pass-through data for the total value and volume of Crown timber entering the 25 largest sawmills from independent harvesters that accounted for 91.3 per cent of all Crown softwood timber in the section 129 proceeding.[98] Furthermore, these sawmills certified that these transactions occurred with unrelated tenure holders and provided the USDOC with the relevant certifications for specific sales. On this basis, Ontario determined that 17.75 per cent of Crown logs were sold at arm's length.[99] The Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association also provided extensive transaction specific

[93] Weyerhaeuser 16 September 2004 Supp. Pass-Through Questionnaire Response (Exhibit CDA-40); and Weyerhaeuser26 October 2004 Supp. Pass-Through Questionnaire Response (Exhibit CDA-41).

[94] Saskatchewan 12 November 2003 AR Questionnaire Response, at SK-34-35 (Exhibit CDA-42).

[95] Manitoba 21 May 2004 Pass-Through Questionnaire Response, Exhibit MB-S-38 (Exhibit CDA-43); as revised in Manitoba September 15, 2004 Supp. Pass-Through Questionnaire Response, Revised Exhibit MB-S-38 (Exhibit CDA-44).

[96] Manitoba 21 May 2004 Pass-Through Questionnaire Response, at MB-1 (Exhibit CDA-43). Tembec (Manitoba) the largest of the independent harvesters accounting for 51 per cent of this volume also completed the USDOC Pass-Through Appendix. See Response of Tembec (Manitoba) to the US Department of Commerce 17 August 2004 Supplemental Questionnaire "Pass-Through Appendix" (16 September 2004) (Exhibit CDA-45); and Response of Tembec (Manitoba) to the US Department of Commerce 5 October 2004 Second Supplemental Questionnaire "Supplemental Pass-Through Appendix" (25 October 2004) (Exhibit CDA-46). In its final section 129 determination, the USDOC wrongly excluded all of these transactions on the basis that they occurred outside the period of investigation. See Draft Section 129 Determination, at 12 (Exhibit CDA-6).

[97] Manitoba 12 November 2003 AR Questionnaire Response, Narrative at MB-16, Exhibits MB-S-2 and MB-S-4b (Exhibit CDA-47).

[98] See Ontario 21 May 2004 Pass-Through Questionnaire Response, Narrative at ON-2, Exhibit ON-PASS-1, Exhibit ON-PASS-3 (Exhibit CDA-48). The data provided to the USDOC were drawn directly from the TREES database maintained by the Ontario Ministry of Natural Resources ("MNR"). This MNR database was carefully examined and verified by the USDOC during the period of investigation, as it contains all the needed independent harvester and sawmill-specific sales data for this timeframe.

[99] *Ibid.* The 17.75 per cent is a subsequent revision to the 18.12 per cent referred to in the Ontario 21 May 2004 Pass-Through Questionnaire Response.

evidence, sales documentation, and other documents supporting the absence of pass-through of benefit in the data supplied by the Government of Ontario.[100]

88. In the first administrative review, Ontario provided evidence demonstrating that approximately 6,465,085 cubic metres (or 42 per cent of the total timber harvested from Crown land) was harvested by independent harvesters.[101] In addition, in response to the USDOC's request at verification, Ontario provided detailed evidence concerning the largest 25 sawmills in Ontario log purchases from unrelated tenure holders during the period of review.[102] As the USDOC verified, those 25 sawmills purchased 31 per cent or 4,391,708 cubic metres of Crown softwood logs from unrelated tenure holders.[103]

TABLE OF EXHIBITS

CDA-11 USDOC Memorandum from B.E. Tillman to J.J. Jochum, *Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber from Canada*, C-122-839 (13 December 2004).

CDA-12 *New Shorter Oxford English Dictionary* (Oxford: Clarendon Press, 1993) at 1985 ("offset").

CDA-13 Response of the Government of Alberta to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Narrative at AB-1 – AB-7.

CDA-14 Response of the Government of Alberta to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Narrative at 1.

CDA-15 Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Narrative at 5 and Exhibit BC-PT-40.

CDA-16 USDOC Memorandum from B.T. Carreau to F. Shirzad, *Issues and Decision Memorandum: Final Results of the Countervailing Duty Investigation of Certain Softwood Lumber Products from Canada*, (21 March 2001) at 15.

CDA-17 *Tariff Act of 1930,* § 771(33), *codified at* 19 U.S.C § 1677(33) (2000).

CDA-18 *New Shorter Oxford English Dictionary* (Oxford: Clarendon Press, 1993) at 114 ("at arm's length… (of dealings) with neither party controlled by the other")

CDA-19 *Black's Law Dictionary*, 6th ed. (St. Paul, Minn.: West, 1990) at 109 ("arm's-length transaction").

CDA-20 J.P. Kalt and D. Reishus, *Economics of Arms's Length Transactions and Subsidy Pass-Through*, submitted as Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Exhibit BC-PT-39.

CDA-21 J.P. Kalt and D. Reishus, *Statement for the First Administrative Review*, Attachment 1 to Letter from British Columbia Lumber Trade Council to USDOC (15 March 2004).

CDA-22 Letter from Weil, Gotshal & Manges to USDOC, *Certain Softwood Lumber from Canada: Comments on Draft Section 129 Determination* (26 November 2004).

CDA-23 Letter from USDOC to Embassy of Canada, *Certain Softwood Lumber Products from Canada: WTO Supplemental "Pass-Through" Questionnaire* (17 August 2004).

CDA-24 Letter from USDOC to Embassy of Canada, *Certain Softwood Lumber Products from Canada: Second WTO Supplemental "Pass-Through" Questionnaire* (5 October 2004).

CDA-25 Response of the Government of British Columbia to the Department's 5 October 2004 Supplemental Questionnaire Concerning Pass Through of Alleged

CDA-34 USDOC Memorandum from S. Moore to File, *Countervailing Duty Administrative Review of Certain Softwood Lumber from Canada: Verification of the Norcon Forestry Survey and the British Columbia Lumber Trade Council (BCLTC) Survey* (2 June 2004) at 9-12.

CDA-35 Response of the Government of Alberta to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004) at AB-2-3, Exhibit AB-S-75, Exhibit AB-S-76, and Exhibit AB-S-78.

CDA-36 Government of Alberta Verification Exhibit GOA-6, Amended Table 50 (18 April 2004).

CDA-37 Government of Alberta Verification Exhibit GOA-7, Amended Table 59.

CDA-38 Bearing Point, *Timber Damage Assessment (TDA) Table – 2003 Update* (17 October 2003), submitted in Response of the Government of Alberta to the Department's 12 September 2003 Questionnaire (12 November 2003), Exhibit AB-S-69.

CDA-39 Response of the Government of Saskatchewan to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Narrative at SK-1 – SK-5 and Exhibit SK-S-29.

CDA-40 Response of Weyerhaeuser Company to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (16 September 2004).

CDA-41 Response of Weyerhaeuser Company to the Department's Second WTO Supplemental Pass-Through Questionnaire (26 October 2004).

CDA-42 Response of the Government of Saskatchewan to the Department's 12 September 2003 Questionnaire (12 November 2003), Narrative at SK-34 – SK-35.

CDA-43 Response of the Government of Manitoba to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Narrative at MB-1, Exhibit MB-S-38.

CDA-44 Response of the Government of Manitoba to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Revised Exhibit MB-S-38.

CDA-45 Response of Tembec Inc**.** (Manitoba) to the Department's 17 August 2004 Questionnaire Concerning Pass Through of Alleged Benefits (16 September 2004), at 1-7.

CDA-46 Response of Tembec Inc. (Manitoba) to the Department's 5 October 2004 Second Supplemental Questionnaire Concerning Pass-Through of Alleged Benefits (25 October 2004), Narrative, at 1-2 and Attachments A and B.

CDA-47 Response of the Government of Manitoba to the Department's 12 September 2003 Questionnaire (12 November 2003), Narrative at MB-14 – MB-16, Exhibit MB-S-2 and Exhibit MB-S-4b.

CDA-48 Response of the Government of Ontario to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Narrative at ON-1 - ON-2, Exhibit ON-PASS-1 and Exhibit ON-PASS-3.

CDA-49 Response of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association on behalf of their members to the Department's August 17, 2004 Questionnaire Concerning Pass Through of Alleged Benefits (16 September 2004).

CDA-50 Response of the Ontario Forest Industries Association and the Ontario Lumber Manufacturers Association on behalf of their members to the Department's 5 October 2004 2nd Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (26 October 2004).

CDA-51 Letter from Hogan & Hartson to USDOC, Certain Softwood Lumber Products from Canada: Service of Government of Ontario Verification Exhibits on Petitioner's Counsel (6 April 2004).

CDA-52 Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Factual Submission (15 March 2004), Exhibit 9 (final version of Exhibit ON-STATS-1).

ANNEX A-2

RESPONSE OF CANADA TO THE REQUEST BY THE UNITED STATES FOR PRELIMINARY RULINGS AND REBUTTAL SUBMISSION OF CANADA

31 March 2005

TABLE OF CONTENTS

TABLE OF CASES CITED IN THIS SUBMISSION

Panel Report	*United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada*, Report of the Panel, WT/DS257/R, adopted 17 February 2004.
Appellate Body Report	*United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada*, Report of the Appellate Body, WT/DS257/AB/R, adopted 17 February 2004.
Australia – Automotive Leather II (Article 21.5 – US)	*Australia – Subsidies Provided to Producers and Exporters of Automotive Leather – Recourse to Article 21.5 of the DSU by the United States*, Report of the Panel, WT/DS126/RW and Corr. 1,

I. INTRODUCTION

1. In this submission, Canada addresses the arguments made by the United States in two parts. First, Canada responds to the request by the United States for a preliminary ruling that the final results of the administrative review fall outside the jurisdiction of the Panel in this dispute. Second, Canada rebuts the few assertions the United States makes in its first written submission.

2. For the reasons set out in this submission, Canada requests that the Panel reject the US request as being without merit, and determine that the final results of the administrative review are properly reviewable under Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU"). Canada also requests that the Panel reject the US assertion that the US Department of Commerce ("USDOC") conducted proper pass-through analyses.

II. RESPONSE OF CANADA TO THE REQUEST BY THE UNITED STATES FOR PRELIMINARY RULINGS

3. The request by the United States for a preliminarily ruling in this dispute is a request that the Panel insulate the US imposition of countervailing measures on softwood lumber from compliance under the WTO Agreement. The Panel should reject this request as being without legal basis, and as running contrary to the very purpose of the dispute settlement system.

4. First, the final results of the administrative review are properly before the Panel because they rendered the pass-through analyses and resulting adjustment provided in the section 129 determination non-existent. There is no support in the DSU for the US contention that a panel may not review, under Article 21.5, measures that undo claimed "measures taken to comply". Article 21.5 requires the Panel in this case to determine the "existence" of any measure taken by the United States to bring the imposition of its countervailing duty into compliance with the recommendations and rulings of the Dispute Settlement Body ("DSB") on pass-through.

5. Second, the administrative review results are within the jurisdiction of the Panel under Article 21.5 of the DSU because, like the section 129 determination, these results are inextricably linked to the recommendations and rulings of the DSB in this case. In both measures, the USDOC purports to bring its countervailing duty on softwood lumber into conformity with its obligations to conduct pass-through analyses; in both measures, its treatment of the pass-through issue and record evidence is nearly identical.

6. Third, the US request runs contrary to the very purpose of Article 21.5 compliance proceedings. If the US position were to prevail, Canada would be required to bring an absurd multiplicity of "new" dispute settlement cases on the same issue, involving the same claims, to secure the same recommendations and rulings from the DSB. Acceding to the request would preclude any "prompt settlement of situations" under Article 3.3, "positive solution to a dispute" under Article 3.7, or "prompt compliance" under Article 21.1 of the DSU. Acceptance of the US position would allow the United States to evade compliance with DSB rulings in perpetuity, frustrating the very purpose of the DSU.

A. Article 21.5 of the DSU Establishes a Broad Scope for Review

7. Article 21.5 of the DSU provides for expedited dispute settlement procedures to ensure full implementation of recommendations and rulings of the DSB:

> Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such

> dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel. . . .

8. The ordinary meaning of the phrase "measures taken to comply," read in context and in light of the object and purpose of Article 21 and of the DSU as a whole, provides the Panel with wide discretion to examine whether a Member has complied with the recommendations and rulings of the DSB. The Appellate Body in *Canada – Aircraft (Article 21.5 – Brazil)* confirmed that the scope of Article 21.5 is to be interpreted broadly:

> [T]he phrase "measures taken to comply" refers to measures which have been, *or which should be*, adopted by a Member to bring about compliance with the recommendations and rulings of the DSB.[1]

9. An Article 21.5 panel is therefore not limited to examining only those measures that an implementing Member claims to have been "taken to comply". As the United States itself has recognized, it is for the Panel alone to determine the "measures taken to comply".[2] It is also for the Panel to determine whether such measures exist and, if so, whether they are consistent with the implementing Member's WTO obligations.

B. The Final Results of the Administrative Review Are within the Panel's Jurisdiction of the Panel under Article 21.5 Because They Rendered Non-Existent Any Purported Compliance Achieved in the Section 129 Determination

10. In its request for a preliminary ruling, the United States fails to address the fact that the final results of the administrative review rendered non-existent, the limited pass-through analysis and resulting adjustment provided in the section 129 determination.

11. As explained in Canada's first written submission, the USDOC failed to perform appropriate pass-through analysis for the log transactions identified in the administrative review.[3] The USDOC therefore presumed, rather than demonstrated, the full pass-through of a benefit in arm's-length transactions.[4] Accordingly, on 20 December 2004, the date on which the final results of the administrative review came into force, the USDOC nullified the pass-through analysis and resulting adjustment it provided in the section 129 determination.[5]

12. It is an uncontested fact that the final results of the administrative review rendered ineffective the pass-through analysis and adjustment under the section 129 determination. Consequently, the final results of the administrative review are an integral part of the Panel's determination "as to the *existence* … of measures taken to comply" under Article 21.5 of the DSU.[6]

---

[1] *Canada – Aircraft (Article 21.5 – Brazil)*, at para. 36 [emphasis added]. ("[I]n principle, there would be two separate and distinct measures: the original measure which *gave rise* to the recommendations and rulings of the DSB, and the 'measures taken to comply' which are – or should be – adopted to *implement* those recommendations and rulings.") [emphasis in original]

[2] … 345.4(of rt)6 ibie 3cc

13. The Appellate Body in *EC – Bed Linen (Article 21.5 – India)* explained that the mandate of a compliance panel under Article 21.5 includes examining the existence of "measures taken to comply" and that such an examination is not limited to the factual circumstances or legal issues addressed in the original panel proceedings:

> We addressed the function and scope of Article 21.5 proceedings for the first time in *Canada – Aircraft (Article 21.5 – Brazil)*. (…) We explained there that the mandate of Article 21.5 panels is to examine either the "existence" of "measures taken to comply" or, more frequently, the "*consistency with a covered agreement*" of implementing measures. This implies that an Article 21.5 panel is not confined to examining the "measures taken to comply

19. As explained in Canada's first written submission, the treatment by USDOC of the pass-through issue in the final results of its administrative review is nearly identical to its section 129 pass-

22. In *Australia – Salmon (Article 21.5 – Canada)*, the panel was faced with a sub-national ban on certain imported Canadian salmon products, which was introduced subsequent to national measures that Australia declared were taken to comply. Australia argued that the sub-national ban was not a measure "taken to comp

> raised in the original proceedings, because a "measure taken to comply" may be *inconsistent* with WTO obligations in ways different from the original measure.[21]

25. The section 129 determination and the final results of the administrative review are inextricably linked to the DSB recommendations and rulings in this dispute because they both address the obligations of the United States to conduct pass-through analyses with respect to independent harvester and sawmill-to-sawmill log transactions for the same exports for the same period of time.[22] The mere fact that the administrative review might have been initiated under a distinct provision of US law does not excuse the failure by the USDOC, for example under Article 10 of the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement"), to "take all necessary steps to ensure that the imposition" of the US countervailing duty on softwood lumber "was in accordance with" the requirement to conduct pass-through analyses under "the provisions of Article VI of GATT 1994 and the terms of this Agreement".

D. The US Request to Exclude the Final Results of the Administrative Review from the Panel's Jurisdiction Ignores the Purpose of Compliance Proceedings

26. As a broader systemic matter, the US request for a preliminary ruling runs contrary to the very purpose of an Article 21.5 panel in its review of the imposition of countervailing measures.

27. The US request, taken to its logical conclusion, would require Canada to make a series of identical claims to address an unchanging issue under Article VI:3 of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") and Articles 10 and 32.1 of the SCM Agreement. The US obligation to demonstrate whether, and to what extent, alleged subsidies to log production pass through arm's-length log purchases *before* imposing duties on softwood lumber products would remain in dispute for each annual assessment review under Article 21 of the SCM Agreement during the potential five-year life (or longer) of the US definitive countervailing measure. Such a result would leave the DSB in the absurd sit9.90 TD0.0lpurducts w.1( )]TJ-16.90719.95616.90719 (esults of9C)D0.0lr

> [W]e also wish to express the agreement of the United States with the broad and inclusive approach the Panel has taken thus far in defining the scope of this proceeding. The Panel's approach is the only one consistent with the purpose of the WTO dispute settlement system as reflected in Articles 3 and 21 of the Dispute Settlement Understanding: the prompt settlement of disputes. Disputes could not be settled "promptly" if a defending party were permitted to thwart a thorough review of its WTO compliance by staging the introduction of details of new measures over a period of time, and then arguing that they must escape WTO scrutiny for a further period of time.[24]

30. In this dispute, the DSB ruled that the United States must demonstrate, rather than presume, that a subsidy passes through arm's-length log transactions. The United States defies this ruling when, in an administrative review of the amount of the countervailing duty that gave rise to the matter before the DSB, it performs none of the required analysis and continues to presume pass-through. The Panel should therefore reject the U.S. preliminary ruling request and find that the results of the first administrative review are properly before it in this proceeding.

III. REBUTTAL SUBMISSION OF CANADA

31. Canada established in its first written submission that in both the section 129 determination

A. The Five "Factors" Used by the USDOC to Disregard Arm's-Length Transactions Are Irrelevant to Whether Entities Operate at Arm's Length

37. Both the original panel and the Appellate Body confirmed that a Member may not presume that a subsidy passes through transactions where a subsidy is received by "someone other than the producer or exporter of the product under investigation" or where "the producer of the input is not the same entity as the producer of the processed product".[26]

38. Canada has demonstrated that the US softwood lumber subsidy calculations include amounts attributable to log purchases by sawmills from unrelated parties.[27] The Canadian respondents provided substantial record evidence concerning such purchases, which the USDOC rejected without having demonstrated that a pass-through occurred. The United States can point to no record evidence or analysis demonstrating that alleged stumpage subsidies passed through to the purchasing lumber producers; instead, it asserts only that "Commerce did not 'presume' pass-through".[28] Nevertheless, the USDOC continued to include that alleged stumpage subsidy amount in its softwood lumber subsidy calculations.

39. The reliance by the USDOC on its five "factors" to dismiss, without analysis, the majority of the transactions as non-arm's-length is not supported by the GATT 1994, the SCM Agreement, or basic economics. None of the "factors" identified by the USDOC as having "an impact on the disposition of the Crown logs sold by independent harvesters"[29] transform an arm's-length transaction into one that is not at arm's length. Nor can these "factors" otherwise be used to avoid conducting an analysis of log transactions.[30]

40. Basic economic principles dictate that domestic processing requirements do not affect the arm's-length nature of a transaction, as such regulations do not alter the opposition of economic interest between sawmill and harvester.[31] Indeed, if anything, such a requirement may provide the harvester greater market power because it would limit where a sawmill may acquire its inputs.[32] Thus, there is no basis to disregard transactions due to the presence of domestic processing requirements.

41. The USDOC's assertion that a transaction is not at "arm's length" where a log purchaser is responsible for the payment of stumpage fees is equally without support. An independent harvester will extract from a sawmill the *full market value* of what it provides to the sawmill (*i.e.*, the log), regardless of who "writes the check".[33] This fundamental economic principle is commonly found in introductory economic texts. Although the party writing the check may affect the observed log price, it will never affect the *value paid* by the sawmill for the logs.[34] Moreover, a contractual provision specifying the party responsible for remitting stumpage is no different than a provision specifying

---

[26] First Written Submission of Canada, at paras. 47-50.
[27] Canada First Submission, at paras. 3-5, 26.
[28] US First Submission and Request for Preliminary Rulings, at para. 33.
[29] Final Section 129 Determination, at 9 (Exhibit CDA-5).
[30] First Written Submission of Canada, at paras. 62-64.
[31] J.P. Kalt and D. Reishus, *Statement for the First Administrative Review*, Attachment 1 to Letter from British Columbia Lumber Trade Council to USDOC (15 March 2004), at 42-43, 48-51, 55 (Exhibit CDA-21); J.P. Kalt and D. Reishus, *Economics of Arms's Length Transactions and Subsidy Pass-Through*, submitted as Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental 4.2.1(1(xh1.6(4B)4(C))o)8((o)-CTJ/TD.2(e)2.2(e).7(i5 Det.8)9-1E)7.8(74.20)-3.526

which party is responsible for satisfying outstanding liens or governmental obligations that might affect a transaction.

42. Finally, in an industrial context it is common for a buyer of goods or services to provide equipment, expertise or materials as part of a transaction. The essence of an arm's-length transaction is that the seller is able to extract from the buyer the value of what the seller provides. Accordingly, these transactions remain at arm's length even if the buyer provides goods or services used by the seller – whether cash, material, credit extended or other consideration.[35]

43. Moreover, the United States cannot be excused from its obligation to conduct the required pass-through analysis on the pretense that transaction-specific information, which was not reasonably required to perform the analysis, was not available. Given that the investigation and review were conducted on an aggregate basis, it is particularly incongruous for the United States to refuse to

> sawmills is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.[43]

51. The Appellate Body, therefore, upheld the conclusions of the original panel that a pass-through analysis was required for all arm's-length

TABLE OF EXHIBITS

TABLE OF EXHIBITS

ANNEX A-3

ORAL STATEMENT OF CANADA

21 April 2005

I. INTRODUCTION

1. We are here today because the Dispute Settlement Body has ruled that a subsidy on harvested timber – that is, logs – does not necessarily pass-through to the softwood lumber manufactured from those logs. This is so where the producer sells the logs to an unrelated entity who turns the logs into lumber. In these circumstances, before the United States may apply countervailing duties to the softwood lumber manufactured from those logs, it has an obligation under Article VI:3 of the GATT and Articles 10 and 32.1 of the SCM Agreement to establish that the benefit of the subsidy has passed-through from the producer of the logs to the producer of the lumber.

2. The United States' compliance obligations in this case were uncomplicated. Before it applied countervailing duties to lumber made from logs acquired in such arm's-length transactions, it had an obligation to conduct a pass-though analysis to determine whether the benefit of any subsidies on those logs passed through to the lumber. By agreement with Canada, the United States had ten months in which to conduct that analysis.

3. Instead of complying, the United States has gone to great lengths to avoid the obligations flowing from the DSB's ruling. At the end of the ten months the United States issued a revised countervailing duty determination under section 129 of its *Uruguay Round Implementation Act*. The United States did conduct a pass-through analysis for a small fraction of the transactions that were the subject of the DSB's ruling, but for the overwhelming majority of transactions it did no pass-through analysis. Instead, it invented an elaborate threshold test which it used to exclude most arm's-length transactions from any pass-through analysis. The test the United States invented to exclude arm's-length transactions from pass-through analysis has no basis in WTO law. It defies basic principles of economics and is even contrary to the criteria for arm's-length transactions under the United States' own law.

4. On the basis of its flawed threshold test, the United States has also sought to evade its obligations by claiming that it lacked the necessary information to do a pass-through analysis. As Canada will show, it supplied the United States with all the information it needed and went to great lengths to comply with its requests. The United States' onerous additional demands involved information that was irrelevant to a pass-through analysis, did not come until most of its reasonable period of time to comply had expired, and would have imposed an impossible evidentiary burden on Canadian respondents in the process.

5. The United States also failed to perform any pass-through analysis for other sales of logs, those to companies that produced both logs and lumber. Nothing in the adopted findings of the panel or the Appellate Body licensed the exclusion of these transactions.

6. In all of these instances, the United States simply assumed that the entire benefit passed through from the logs to the softwood lumber and included the full amount of that benefit in its duty calculations on the lumber. In the original case, the DSB ruled that the United States' presumption of pass-through was inconsistent with its obligations under the GATT and the SCM Agreement. The United States has repeated its presumption of pass-through in the determinations challenged here and they are similarly inconsistent with its WTO obligations.

consider in any way certain sawmill-to-sawmill transactions; and finally, claimed that information necessary to conduct pass-through analyses was otherwise deficient.

15. The issue of "pass-through" arises in this

possible influence of "government-mandated restrictions and other factors".[6] The United States maintains that an "arm's length" transaction is defined by more than "mere affiliation".[7] In so doing, it ignores even the arm's length standard set out in its own law, and which it has routinely used.[8]

22. Through an exercise in *ex post facto* rationalization, the United States argues that Commerce's so-called factors are justified by a three-pronged test, custom-tailored for this dispute.[9] First, a transaction must be between unrelated parties. Second, one party to the transaction must not "effectively control" the other. Third, both parties must have "roughly equal bargaining power".

23. Canada does not contest the first of these requirements. It is the only part of Commerce's arm's length test that is warranted, based on the findings and conclusions of the original panel, as upheld by the Appellate Body.[10]

24. The second requirement of the US test is no different than the first. "Effective control" is already covered in the US statutory definition of "affiliated parties", which Commerce incorporated in its questionnaires. The only transactions for which Canadian respondents claimed that Commerce should do a pass-through analysis were those between parties that were not "affiliated". That statutory definition covers a wide range of relationships between parties to a transaction, ranging from family relationships, to direct or indirect ownership of an organization, and expressly includes any situation where one person "controls" any other person. According to the statute, the term "control" refers to situations in which a person "is legally or operationally in a position to exercise restraint or direction over the other person".[11] Commerce did not contest, but rather confirmed, that the definition of "affiliated parties" was applied properly in this case.[12]

25. The third requirement – "roughly equal bargaining power" – is pure fabrication, tailored for this case to justify Commerce's use of so-called factors to reject transactions. Nowhere is it found in the analysis of the original panel or the Appellate Body. Moreover, were "roughly equal bargaining power" a requirement for arm's-length transactions, almost any transaction anywhere could be rejected by investigating authorities on that basis alone. One party to a transaction will often have greater bargaining power than the other, but this does not mean that the terms of the transaction do not reflect a market outcome.

26. Fundamentally, by rejecting transactions on the hypothesis that their outcome might somehow be "affected" by market conditions, Commerce conflates the obligation to conduct a pass-through analysis, which would demonstrate the existence and amount of a pass-through, with the task of identifying transactions to which that obligation applies.[13]

27. Moving to the five factors themselves, we have detailed in our written submissions why they are irrelevant to whether a pass-through analysis is required. I therefore propose to make just three points today.

---

[6] *Ibid.*, at para. 20.
[7] *Ibid.*, at paras. 16-17.
[8] First Written Submission of Canada, at para. 62, footnote 54 (citing SAA at 928; Exhibit CDA-1).
[9] Second Written Submission of the United States, at para. 16.
[10] First Written Submission of Canada, at paras. 47-49.
[11] *Ibid.*, at para. 60, footnote 51, citing to section 771(33) of the *Tariff Act of 1930* (19 U.S.C. § 1677(33)) (Exhibit CDA-17).
[12] First Written Submission of Canada, at paras. 60, 74; Second Written Submission of the United States, at para. 15, footnote 18.
[13] *See, e.g.*, Third Party Submission of China, at paras. 26-27.

28. First, the United States makes the telling concession that its "additional factors" are not "exclusively arm's-length issues".[14] The factors in question here regard who paid the stumpage fees, and whether transactions involved a fibre exchange agreement.

29. As a matter of basic economics, neither factor is an "arm's length" issue at all. The issue of who remits the government stumpage fee says nothing about whether the alleged input subsidy passed through to the purchaser. A contractual provision assigning to the buyer the obligation to pay a debt owed by the seller does not affect the value of the good sold. The value of a log is determined by the supply and demand for that log.[15] Moreover, what the United States calls the "vehicle by which the Crown bestows the subsidy"[16] has been found in this case to be the provision by government of standing timber to timber harvesters. Therefore, the US argument that the government provided the alleged stumpage subsidy directly to sawmills, where they paid the stumpage fee on behalf of the harvester, is not supported by the facts. Standing timber is provided to the upstream timber harvester, not the downstream sawmill. These facts do not suddenly change simply because the purchasing sawmill might remit the government stumpage on behalf of the upstream stumpage holder.

30. Similarly, a barter arrangement in the form of a fibre exchange agreement merely provides that the buyer is paying the consideration owed to the seller in goods rather than in cash. Indeed, barter is perhaps the oldest form of market transaction. This factor is

IV. COMMERCE Failed TO CONDUCT ANY ANALYSIS WHERE THE PURCHASING SAWMILL HELD A STUMPAGE CONTRACT

34. I turn now to address another instance in which Commerce impermissibly presumed a pass-through.

35. Commerce limited its questionnaires to only a select subset of sawmill-to-sawmill transactions, denying a pass-through analysis where the purchasing sawmills held tenure.

36. As justification here, the United States claims that the Appellate Body reversed, rather than upheld, the original panel's conclusi

49. Given Commerce's failure to request transaction-specific evidence, it should have either removed the arm's-length volumes that had been identified from the numerator or used the sawmill-specific information submitted by some provinces to conduct pass-through analyses. Instead, Commerce chose to rely on its "factors" to once again impermissibly presume a full pass-through of the alleged stumpage subsidy.

B. Commerce's Accusation that Canada Withheld Evidence is Without Merit

50. So, as I have outlined, the United States had everything it needed to conduct its analysis. It now accuses Canada, however, of being unprepared to support its pass-though claims with evidence. Why? Because Canada did not provide transaction-specific information for each of the five "factors" in response to supplemental questionnaires issued six to eight months into the reasonable period of time. This information was unnecessary and irrelevant to a pass-through analysis. Given the timing of the questionnaire and the type of information sought, this information was also impossible to provide.

51. A large portion of the evidence Commerce complains it did not receive was irrelevant and unnecessary for conducting a pass-through analysis.[35] As Mr. Cochlin has explained, tenure agreements, wood supply commitment letters, payment of stumpage fees by the log purchaser, log purchase agreements and fibre exchange agreements are not relevant to whether a transaction is conducted at arm's length.

52. In many instances, the amount of information requested by Commerce was impossible to provide. For example, British Columbia was expected to retrieve, copy and submit more than 3,000 tenure agreements that were scattered over dozens of district forestry offices.[36] This would have amounted to upwards of 60,000 pages of documents. Canada notified Commerce on multiple occasions of the impossibility of complying with this request, offered numerous sample agreements, and otherwise sought a reasonable alternative. Only after nearly five months did Commerce agree to modify its demands, requesting "excerpts" from all agreements in the province containing certain specified provisions. Commerce's "compromise" would have required British Columbia to locate and manually review all tenure agreements in the province to identify the relevant excerpts, and submit reams of complete tenure agreements, in a little over two weeks.

53. Further, Commerce solicited none of the transaction-specific pricing data that it now asserts are so "essential" for a pass-through analysis in its first questionnaire. Instead, Commerce waited until more than half of the reasonable period of time had elapsed before requesting these data in its supplemental questionnaires and pass-through appendices.[37] Commerce also waited until this time to request information on three of its five "factors", including copies of log purchase agreements and fibre exchange agreements for every arm's-length transaction in the provinces during the period of investigation.[38] In addition, Commerce demanded that the Canadian respondents identify every transaction where a sawmill paid stumpage on behalf of an independent harvester.

54. The pass-though appendices used to collect information from companies on affiliation, pricing data and the "factors" contained more than twenty-four pages of questions and attachments. The supplemental questionnaires directed the provinces to distribute the appendices to *all independent harvesters and sawmills* that were involved in arm's-length transactions. In the case of British Columbia, this would have required the distribution of the appendices to 3,000 independent

[35] *Ibid*., at paras. 75-76.

[36] Ibid., at para. 76 (citing to BC September 15, 2004 Supp. Questionnaire Response, Narrative, at 5 and Norcon B, at 4 (Exhibit CDA-15)).

[37] *Ibid*., at para. 75.

[38] *Ibid.*

harvesters and 175 sawmills operating in that province. If British Columbia had provided Commerce with the required nine copies and produced the other twenty copies required for the service list, *without responses*, this would have amounted to *almost two million, two hundred and ten thousand pages of information*. If the independent harvesters and sawmills had filled out the questionnaires, Commerce would have received *millions more pages of documentation.* As I am sure you will agree, it is hardly reasonable to expect British Columbia to manage the printing and submission of millions of pages of documents in under two months; in fact, it borders on the absurd.

55. Finally, as we explained earlier, Commerce was given more than enough data to conduct a pass-through analysis. The United States has not offered a single valid reason for refusing to use most of this information.

VI. CONCLUSION

56. In conclusion, the United States presumed a pass-through in violation of its WTO obligations. Commerce's presumption of a pass-through covers the vast majority of log transaction volumes identified in the section 129 proceedings, and all transaction volumes identified in the administrative review. Canada has explained that Commerce was not justified in rejecting the log transactions that it did, whether by: first, applying a new "arm's length" threshold test; second, claiming that the Appellate Body reversed the original panel findings and conclusions with respect to certain sawmill-to-sawmill transactions; or third, claiming that information was missing or deficient.

57. In both its section 129 determination and its administrative review, Commerce once again necessarily and impermissibly presumed pass-through.

58. Canada therefore requests that the Panel:

- *Find* that the US imposition of countervailing duties in respect of the Crown log transactions identified in this dispute is inconsistent with Article VI:3 of the GATT and Articles 10 and 32.1 of the SCM Agreement;

- *Recommend* that the United States bring its measures into conformity with its obligations under those provisions; and

- *Suggest*, in accordance with Article 19.1 of the