

## ANNEX A

### Parties Responses to Questions – First Meeting of the Panel

<b>Contents</b>		<b>Page</b>
Annex A-1	Responses of Canada to questions posed in the context of the first substantive meeting of the Panel	A-2
Annex A-2	Responses of the United States to questions posed in the context of the first substantive meeting of the Panel	A-13

## ANNEX A-1

### RESPONSES OF CANADA TO QUESTIONS POSED IN THE CONTEXT OF THE FIRST SUBSTANTIVE MEETING

(21 May 2002)

1. *In situ* natural resources are not “goods” within the meaning of the SCM Agreement. Accordingly, the right of exploitation of such resources does not come within the meaning of “provision of goods” in Article 1.1(a)(1)(iii). This does not mean that the consequences flowing from real property rights in general, and resource exploitation rights in particular, cannot come within the scope of other parts of Article 1.1.

A land grant, or the grant of a building, may come within Article 1.1. However, such a grant would not constitute the provision of “goods”. Land, as an asset, is often a source of revenue. A land grant, therefore, can constitute the foregoing of revenue that the owner might expect from its rental or sale. Whether a 99-year lease comes within the terms of Article 1.1 depends on the terms of the lease and, as mentioned above, the prevailing legal regime for leasing of publicly-owned land.

Finally, for the purpose of Article 1.1, real property rights such as those in land, leases or *in situ* natural resources are no different from property rights in patents or copyrights (or other intangibles). It is not that the “granting” of these rights in each instance can never amount to a financial contribution, but that such grants do not amount to the provision of “goods”.

2. (a) Yes. The term “goods” in Article 1.1(a)(1)(iii) has the same meaning and scope as “products” used elsewhere in the SCM Agreement and the WTO Agreement. The ordinary meaning of “goods” is “tangible or movable personal property other than money; (especially) articles or items of merchandise (goods or services)”.

The context for this term in the SCM Agreement is highly instructive as to its scope and confirms the ordinary meaning of “goods” as tradable items with an actual or potential customs classification.

- First, in Part II, Article 3.1(b) refers to “the use of domestic over imported *goods*.” Evidently, “goods” refers to tradable items: rights to *in situ* natural resources cannot be “imported” or “used”.
- Second, Parts III and V of the SCM Agreement refer to “products”. There is no indication anywhere in the text that the “product” or “imports” referred to in these Parts is different from the “goods” referred to in Article 1 or 3.

Other agreements in the WTO Agreement are also particularly useful as context.

- First, countervailing measures are provided for in Article VI of the GATT 1994, as an exception to Article II. Therefore, the coverage of Part V of the SCM Agreement and that of Article II of the GATT 1994 must be the same.
- Second, the interpretative note to Annex 1A of the *Marrakesh Agreement* provides a rule of conflict between the GATT 1994 and the covered agreements. The logical conclusion of the note

is that the agreements set out in Annex 1A apply to the same products, or “goods” as those subject to the GATT 1994.

- Third, Article 1 of the TRIMs Agreement (TRIMS) provides that the TRIMs “applies to investment measures related to trade in *goods* only.” Article 2 requires that, “... no Member shall apply any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994.” The unambiguous implication is that the “goods” referred to in Article 1 of the TRIMs are the same as the “products” covered by Articles III and XI of the GATT 1994.
- Fourth, the *Agreement on Implementation of Article VII of the GATT 1994* refers to imported or exported “goods”. There is no indication that the term has a different meaning in this agreement than the same word in other agreements in Annex 1A, or indeed the term “product” in the GATT 1994.
- Fifth, the *Agreement on Rules of Origin* also refers to “goods” in the context of Articles I, II, III, XI and XIII of the GATT 1994.

Finally, nothing in the object and purpose of the SCM Agreement suggests that the term “goods” in Article 1.1 should be read as anything other than tradable items with an actual or potential customs classification. To the extent that there is a concern that certain forms of government largesse may not be captured by definition of “goods”, the Panel may consider the following:

- First, as the panel in *United States – Export Restraints* noted, Article 1.1(a)(1) does not cover *all* government actions that may affect the market, but only those that fall within the definition of “subsidy”.
- Second, land or lease grants may well be covered by other provisions in Article 1.1(a)(1). It is not, however, necessary for this Panel to define the precise scope of that Article to arrive at the conclusion that real property rights are not “goods”.

The Spanish and French versions of the WTO Agreement are useful in confirming the meaning of the term “goods”. In both texts, the word “goods” is translated into both “bienes” and “productos” as well as “biens” and “produits” in the Spanish and French versions, respectively. For the purposes of the other two official versions of the SCM Agreement, the term “goods” in Article 1.1 has the same meaning and scope as “products”.

The Appellate Body also uses the terms “goods” and “products” interchangeably as reflected in their decisions in both *EC – Bananas* (para. 221) and *Canada – Autos* (para. 140).

**(b)** No. A building that is affixed to the land is not “goods” for the purposes of Article 1.1 of the SCM Agreement. Such a building would be real property.

**(c)** Heading 0602 covers “live trees ... of a kind commonly supplied by nursery gardeners or florists for planting or for ornamental use.” Live firs of small dimensions that are fully transportable are properly considered as goods since they fall under the Harmonized System. Fully-grown live firs in the form of standing timber are not “goods” for the purposes of the WTO Agreement.

**(d)** The fact that “services” are mentioned in the first half of Article 1.1(a)(1)(iii) does not in any way affect the scope of “goods”. Goods are those tradable items that come or may come under the coverage of the GATT 1994, while services are those economic activities that would fall within the scope of the GATS. Other assets or property – such as intellectual property rights – do not fall within Article 1.1(a)(1)(iii) at all.

3. Where a private party produces a product from natural resources in which it has property interests, the “goods” so produced are not provided by government. Where, however, a lorry-full of iron-ore is delivered by the government to a processor, this constitutes the provision of goods. If the government produces the iron ore and offers it to a steel producer willing to load and haul the ore to its mill the government would also be providing goods. However, granting exploitation rights to a resource that is part of the land and that cannot be traded, does not constitute the provision of goods.

4. Under the Canadian constitution, provinces have title to the majority of public property and exercise exclusive jurisdiction to legislate in relation to the development, conservation, and management of non-renewable natural resources and forestry resources.

5. Yes. The text of Article 14(d) unambiguously requires that a Member determine the adequacy of remuneration “in relation to prevailing market conditions for the good or service in question in the country of provision”. The ordinary meaning of “prevail”, read in context, is “exist”. The reference to “prevailing market conditions” is, therefore, to conditions that actually exist in the country of provision. There is nothing in the context, object and purpose or the negotiating history of Article 14 that would permit reading this as “in another country”.

Further contextual evidence may be found in the Accession Protocol of China. The Protocol specifically permits the use of “methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks.” If Article 14(d) permitted Members to consider conditions outside “the country of provision”, this exceptional treatment would not have been necessary.

Market benchmarks can also still exist where there is a government monopoly. For instance, if the government’s monopoly was over domestic production of the goods in question then the government price could be compared to the price of imports of the same good. Even where there are no imports, remuneration is “adequate” where the government operates on a market basis. All of the provinces submitted substantial and unrebutted, factual evidence and economic analyses demonstrating that they were acting in a manner consistent with market principles.

6. The requirements for entering into tenures vary substantially, but before tenures are granted, provinces will require a demonstration of forest management expertise and financial capabilities sufficient to undertake required obligations. Subject to the qualifications, there are no limitations on who can enter into these agreements.

The responsibilities that a long-term tenure holder must agree to undertake generally include: sustainable forest management, forest management, development and operational planning, public consultations, silviculture prescriptions, construction or maintenance of wood processing facilities, preparation of forest inventories, pest and disease control, timber cruises, scaling, firefighting and forest research activities.

In most cases, tenure holders are free to sell their logs to unrelated sawmills. There are generally no requirements either by statute or by the terms of tenures that require tenure holders to sell to specific mills or to sell at specific prices or under specific terms and conditions.

7. The log price data provided to Commerce prior to the PD is described by province below. Logs are highly heterogeneous and prices differ by species, size and quality. As with stumpage rates, any comparison of average prices must at a minimum include adjustments for these characteristics. As well, log prices reflect the value of a delivered good; that is, they include the cost of harvesting and transporting the good as well as all tenure obligation costs borne by the harvester. Accordingly, log prices are not the same as stumpage rates

B.C. is home to the most organized log exchanges in Canada. B.C.'s information is summarized in the following table:

	<b>Volume (m<sup>3</sup>)</b>	<b>Value (\$)</b>	<b>Average Value (\$/m<sup>3</sup>)</b>
Vancouver Log Market (2000/2001)	6,559,073	655,366,782	99.92
Log transactions in BC Interior (1999)	11,309,545	782,088,207	69.15
Vernon Log Yard (2000/2001)	54,907	3,632,694	66.16
Revelstoke Log Yard (2000/2001)	28,754	3,157,601	109.81

The VLM is an informal arrangement amongst the log supply departments of various coastal B.C. licencees, the log buyers for small companies or their agents, and the traders employed by log brokers who buy and sell logs. The VLM does not distinguish between logs originating from privately owned, federally owned or provincially owned land.

There is no similarly organized log market in the interior of B.C.. It consists of a series of small, separate local markets. The Vernon log yard was established in March 1993 and obtains its logs from timber sales harvested in local districts from a variety of tenure arrangements. The Revelstoke log yard is extremely small and the logs sold through it are mainly high-value cedar sawlogs.

Alberta provided survey information it collects in the ordinary course of business on average log prices paid by purchasers. The following table shows the calendar year volume and value (FOB purchasing mill) of these transactions. This data does not break out private land sourced logs from logs harvested on provincial lands and also does not provide information on species type or quality.

Excerpted from Table 32 - Exhibit AB-LER-5 Volume and Value of Domestic Arm's-length Log Sales from Survey

	<b>Total Softwood Log Harvest m<sup>3</sup></b>	<b>Total Arm's-length Transaction Softwood Log Volumes m<sup>3</sup></b>	<b>Percent Arm's-length Transaction Softwood Log Volumes</b>	<b>Arm's-length logs sales prices (FOB purchasing mill) \$/m<sup>3</sup></b>
2000	14,168,657	884,552	6.24%	50.40

In its initial questionnaire response, Ontario provided Commerce with the results of a survey and a report done by the independent accounting firm of KPMG. The first schedule in the survey itemized the costs of SPF (spruce, jack pine and fir) logs from Crown lands delivered to the mill gate. KPMG reported that total weighted average costs of delivered SPF logs cut from Crown land of \$50.42 m<sup>3</sup>. The second schedule in the survey reported purchases of timber in Ontario by third parties of timber harvested from several jurisdictions. The prices for these purchases were established by negotiation between buyer and seller. Weighted average market prices reported by KPMG ranged from \$47.36 m<sup>3</sup> for timber harvested from Ontario private land and \$49.15 m<sup>3</sup> for timber harvested from Ontario Crown land.

There are two separate and distinct markets for the supply of standing timber in Québec: the public forest and the private forest. The only private forest prices obtained by Québec are through annual market surveys and a tri-annual census. Québec uses these market prices to set public forest stumpage rates. Québec provided the Department of Commerce with private stumpage price data for the three years 1998, 1999 and 2000.

8. By “arm’s-length” prices, Canada means prices of log sales between a willing seller and a willing buyer that are not related, i.e. market prices freely negotiated between independent parties. Such sales include both sales for a specific price and sales transacted by means of “swapping” a bundle of different types of logs between unrelated tenure holders.

An estimate of the volume of timber harvested in B.C. by companies operating at arm’s-length from sawmills can be obtained by analysing the timber harvested under specific licences and permits separately for companies that have and do not have sawmills. This analysis, based on information on the record prior to the PD, indicates that 30.09 per cent of the timber from Crown licences was harvested by companies that do not have sawmills. In the aggregate (including private land), 33.0 per cent of timber harvested in the province during the POI was harvested by entities that did not have sawmills.

Québec’s TSFMA tenures require the tenure holder to process the public timber they harvest. Forest management contracts (FMC) do not require tenure holders to process timber. Sales from Federal lands are largely stumpage sales done by sealed bid tender. None of the 40,000 registered private woodlot owners is required to process timber. The tenure data submitted prior to the PD shows that up to 27 per cent of the provincial harvest will be sold through arm’s-length transactions from private lands and FMC tenures. In addition, almost 35 per cent of the total log supply comes from arm’s-length transactions from private lands, FMC tenures and log imports.

Approximately 30 per cent of the softwood timber harvested from Ontario’s Crown land during Commerce’s period of investigation was sold by tenure holders to third parties who subsequently processed this into forest products.

Alberta indicated to Commerce that it had survey data (both price and volumes) on arm’s-length transactions in volumes that represented approximately 6 per cent of the total softwood log harvest in Alberta. A sample of a substantial portion of the forest industries in Alberta was used to develop these data. “Arm’s-length” transactions in this survey were defined as transactions entered into freely between totally unrelated parties. Further, this sample was limited to transactions where the cash price was the only consideration exchanged.

In addition to the survey data giving volumes and prices, Alberta also has data on the volume of logs delivered to mills from sources other than from their own forestry tenures. Alberta’s records show that volumes of timber traded or swapped for other logs or woodchips and purchased in cash transactions or in exchange for other consideration comprised 3,900,000 m<sup>3</sup> in the period of investigation or slightly more than 30 per cent of the total softwood sawlog harvest.

Prior to the PD, Canada submitted to Commerce applications for exclusion from 98 producers who purchased logs or lumber at arm’s-length. Of these, 78 were remanufacturers unrelated to firms with harvesting rights and at least 8 were primary mills that purchased all of their log inputs in arm’s-length transactions.

9. The programmes and policies investigated by Commerce were provincial stumpage programs, not the sale of logs. Indeed, the US used state stumpage programmes as benchmarks rather than log sales. There was a significant amount of information on the record at the time of the PD regarding a variety of sources of data that might have been used by Commerce as benchmarks. This information included data on private stumpage, competitive tenures in certain provinces and other evidence that provinces operate their stumpage systems on market terms. Three provinces – Alberta, Ontario and Québec – provided extensive evidence related to private markets operating within their provinces. Alberta also provided Commerce with data broken out for its competitively sold tenures. The four primary exporting provinces, representing 96 per cent of the exports of softwood lumber, provided

information demonstrating that they operated their stumpage systems in a manner consistent with market principles.

The size of the available in-country benchmark market should not determine the adequacy of the data. Rather, adequacy should be assessed taking into account other factors, including the existence of willing buyers and sellers and other indicia of a viable market. For example, arbitrage works between different timber supply sources to ensure that stumpage rates derived from the sale of a relatively small volume of harvesting rights from one source can represent a valid basis for comparison with stumpage rates from other sources.

One example of arbitrage is found in Québec, where the majority of timber on private forestlands is sold as delivered logs; that is, the owner undertakes the logging himself, or contracts with a logger to do the harvesting. A smaller portion of Québec's private harvest is sold as sales of harvesting rights. Both of these sale prices represent valid competitive market prices because the opportunity for arbitrage between the private log and private stumpage markets exists.

**10.** The factual determinations by Commerce in the three previous lumber cases are highly relevant in establishing that cross-border benchmarks are inherently arbitrary and capricious. In these cases, Commerce made specific factual findings and concluded that so many factors affect the comparability of adjacent US and Canadian timber that valid cross-border comparisons are impossible. The facts underlying Commerce's findings have not changed since then and the findings still hold true today, regardless of the change in the legal regime.

Accordingly, Commerce's finding in *Lumber I* that no unified North American market for stumpage existed is valid today. For example, the wide differences between the US and Canada in terms of species composition; size, quality, and density of timber; and terrain and accessibility, remain unchanged.

As for the factors that can be influenced by government, these also have remained unchanged. For example, supply of timber from public lands in the US is still limited, and, as referred to by Commerce in *Lumber III*, variations in exchange rates and other factors tied to the existence of the political border between the two countries remain.

In *Lumber III* Commerce relied on private forest surveys in Québec because it found these surveys accurately reflected market driven prices in Québec. Québec's system has not changed since. Yet, in *Lumber IV*, not only did Commerce ignore such surveys that were on the record prior to the PD, it ignored every other possible in-country benchmark put on the record by the other provinces.

**11. (a)** No. Under Part V of the SCM Agreement, a Member may impose a countervailing measure only where it has established that a subsidy exists in respect of each entity producing or exporting the subject merchandise subject to the measure. Specifically, the investigating authority must establish a "financial contribution" by government that confers a "benefit". Nothing in the SCM Agreement permits an investigating authority to presume the existence of a subsidy simply because the original recipient provides inputs to a downstream producer.

Where the subject merchandise is not produced or exported by the original recipient of an alleged subsidy, the investigating authority must establish the existence of a subsidy in respect of the downstream producer. That is, it must establish that a financial contribution by government has conferred a benefit on that producer. In the absence of a direct relationship between the downstream producer and the government, Article 1.1(a)(1)(iv) sets out the criteria for determining when a government has made an indirect financial contribution to that downstream producer.

The EC argues that an “effects” test should be incorporated into the subsidy definition. However, Article 1.1 does not include such a test. The enquiry under Article 1.1 of the SCM Agreement is whether a government has made a “financial contribution” that confers a “benefit”. The panel in *United States – Export Restraints* summarized this analysis:

We believe ... that the appropriate way to conceive of “financial contribution” is purely as a transfer of economic resources by a government to private entities in the market, without regard to the *terms* of that transfer. Such a transfer can be effected either by a government directly (subparagraphs (i)-(iii)) or indirectly through private bodies (subparagraph (iv)). The question of the terms on which the transfer is made does not have to do with the existence of a financial contribution but rather goes to the separate issue of benefit, as Article 14 makes clear, by providing that to determine whether a benefit exists, the terms of the financial contribution need to be compared with the market terms. [emphasis in original]

The panel went on to state:

In short, the negotiating history confirms that the introduction of the two-part definition of subsidy, consisting of “financial contribution” and “benefit”, was intended specifically to prevent the countervailing of *benefits* from any sort of (formal, enforceable) government measures, by restricting to a finite list the *kinds* of government measures that would, if they conferred benefits, constitute subsidies. The negotiating history confirms that items (i)-(iii) of that list limit these kinds of measures to the transfer of economic resources from a government to a private entity. Under subparagraphs (i)-(iii), the government acting on its own behalf is effecting that transfer by directly providing something of value – either money, goods, or services – to a private entity. Subparagraph (iv) ensures that the same kinds of *government* transfers of economic resources, when undertaken through explicit *delegation of those* functions to a private entity, do not thereby escape disciplines. [emphasis in original]

The EC argument does not, therefore, have support in either the text or in the negotiating history of Article 1. A subsidy exists where there is a financial contribution by government that confers a benefit. An investigating authority must always establish both elements of a “subsidy” as regards a downstream producer.

**(b)** No. In an original investigation an investigating authority may never assume that any of the requirements of the subsidy definition have been met. This is true for upstream producers as it is in respect of an alleged subsidy to downstream producers. Thus a subsidy to upstream producers cannot be presumed to be passed through to downstream producers in any circumstances. This is especially the case regarding arm’s-length transactions where, under fundamental principles of economics, an upstream recipient of a subsidy would not normally subsidize a downstream producer.

**(c)** Yes. Article 1.1 requires in all instances that for a given recipient, a subsidy exists only where there has been a financial contribution and a benefit. In the context of allegations of indirect subsidies, in order to determine that the downstream producer is “subsidized”, it must be found that: (1) a government entrusts or directs the original recipient of a financial contribution to itself make a financial contribution to the downstream producer under subparagraph (iv); and (2) that such subsequent financial contribution be made on terms such that it thereby confers a benefit to the downstream recipient.

**12.** Where the harvester is not free to: process the logs it harvests itself; sell to whomever it wishes on whatever terms and conditions that are mutually agreed; swap logs with other timber

harvesters; or obtain permits to export, then a government requirement that the logging company contract to provide logs to a sawmill for processing may constitute the government directed provision of logs by the logging company to the sawmill.

**13.** With few exceptions, tenure agreements do not contain requirements that tenure holders have contracts with unrelated sawmills.

**14.** Canada does not wish, at this point, to add to its submissions on this subject.

**15.** The issue of liquidation of entries is a red herring, because in the US the entries in the 90 days prior to a PD would rarely if ever be liquidated before a final determination (including, if appropriate, a final critical circumstances determination) was made. At that point, once there is a critical circumstances finding, the liquidation of unliquidated entries may be suspended.

Under US Customs regulations, entries are to be liquidated within one year after entry, but Customs may extend that period by an additional two years. In practice, if the period is not extended, an entry will be liquidated on the 314th day after it was made. Thus entries potentially subject to retroactive application of definitive duties would not be liquidated by the time Commerce is required to complete an investigation.

**16.** Canada implemented its obligations under the SCM Agreement in the Special Import Measures Act (SIMA) and related regulations. In the Canadian system two investigating authorities are involved in decision-making. Dumping and subsidy determinations are made by the Commissioner of the Canada Customs and Revenue Agency (CCRA). Injury decisions are made by the Canadian International Trade Tribunal (CITT).

Under section 41(1)(a)(iv)(C), in a final determination, the Commissioner makes a finding as to whether a particular investigation involves a prohibited subsidy. Where there is a finding of a prohibited subsidy or “specification”, then in making its final injury inquiry under section 42, the CITT is directed, to determine whether the remaining criteria of Article 20.6 are satisfied. Where the CITT makes a positive determination under section 42(1)(c) (as reflected in section 6(a)), the Commissioner is directed by section 6(b) to assess “a countervailing duty in the amount equal to such of the amount of the subsidy on imported goods as is a prohibited subsidy”. Consistent with Article 20.6, which allows for the retroactive assessment of “definitive countervailing duties”, this provision is under the definitive “Antidumping and Countervailing Duty” heading of the Act (i.e., sections 3-7).

Pursuant to section 37.11 of the SIMA, imports considered would be those imported within a representative period within the period of investigation beginning ninety days before the date of initiation and ending on the date of the Commissioner’s PD, which were “massive” relative to a preceding representative period of comparable duration also within the POI.

The retroactive application of final duties would be effected through a determination by a designated CCRA officer under section 55 of the SIMA. This determination is subject to re-determination by the Commissioner under section 59(1) of the Act. While the goods that these duties would be applied to would have been released (or in the US sense, “liquidated”), the record of their entry would still be in the CCRA records system and thus could be retrieved as necessary.

**17.** There is no basis in the SCM Agreement for the application of provisional measures pursuant to a PD of critical circumstances. Accordingly, no Member may take an action or impose a measure in respect of “critical circumstances” on a provisional basis. In this sense “suspension of liquidation” is no different than a bonding requirement.

**18. (a)** The relevant data for Canada as a whole is set out in Commerce's PD. There, based on a comparison of the three months preceding and the three months following initiation of the investigation, Commerce states that it found an increase in import levels of 23.34 per cent using import statistics net of the Maritime provinces, and found an increase of 19.02 per cent when it included imports from the Maritime provinces. Commerce decided that the "massive imports" element of Article 20.6 of the SCM Agreement had been satisfied since both rates of increase were above the regulatory 15 per cent threshold under US law. If Commerce had considered other comparison periods or approaches to seasonality adjustments, as Canada had argued were necessary to an objective assessment of "massive imports", the inclusion of Maritime shipments would have demonstrated an increase in shipments below the 15 per cent threshold.

**(b)** Québec's exports of softwood lumber to the US in FY 2000/2001 amounted to 21 per cent, or approximately one-fifth of total Canadian exports of softwood lumber to the US. Thus, in order for exports from Québec to have accounted for a 15 per cent increase in Canada-wide exports, exports from Québec would have had to increase by five times the 15 per cent amount, or by 75 per cent. There is nothing in the record indicating that exports from Québec followed any pattern different than exports from the rest of Canada.

However, since at most three Québec producers may have benefited from the alleged prohibited subsidy during the POI, any exports from these producers would have been minute relative to total exports from Canada (or even from Québec) and would not have resulted in a "massive imports".

**19.** The Canada-US Softwood Lumber Agreement (SLA) provides the background against which the US should have conducted its "massive imports" analysis. The CVD investigation was timed to coincide with the economic and trade consequences of the expiration of the SLA. A period of investigation adjusted for such consequences would have found normal trade patterns, rather than "massive imports".

In 1996, Canada implemented the SLA through quota-based export fees. The SLA expired on 31 March 2001. In anticipation of this expiration, and the consequent removal of the fees, Canadian exporters and US importers and purchasers of softwood lumber made a number of rational business decisions. Importers stopped purchasing Canadian lumber. This resulted in a drop in prices throughout March. Exporters, deterred by low prices and SLA fees alike, deferred exports to April. Placed in this context, it is hardly coincidental that exports to the US in April 2001 increased by 463 million board feet over total exports in the month of April 2000.

### **To Both Parties**

**1.** When a timber harvester cuts down a tree, it produces goods – logs. The harvester may then use the goods as input into its own sawmill, pulp mill or other mill, if it has one; it may sell the goods in question to other users of logs; or export them. Goods are, accordingly, provided in the sense of Article 1.1 of the SCM Agreement where logs are given or sold from one party to another.

**2.** There is no "international market price" for softwood lumber, even though it is bought and sold internationally. Unlike commodities such as oil or minerals, softwood lumber is priced to specific domestic or regional markets. As well, because of the huge differences between different sorts of lumber, lumber prices vary depending on the species, dimension and grade of the lumber, whether the lumber has been air or kiln-dried, and whether the lumber has been mechanically stress-rated. Different markets would have different requirements, thus making it difficult to have a single "international market price" for lumber.

3. Article 15(b) of the Accession Protocol of China establishes that under Article 14(d) of the SCM Agreement cross-border price comparisons are not permitted. If Article 14(d) permitted Members to consider conditions outside of China there would have been no reason to negotiate this provision. Article 15, unlike the other provisions, introduces special and additional rules. This is apparent from the following:

- the chapeau, which requires the SCM Agreement to be applied “consistent with the following listed considerations”. If this were a reintroduction of the SCM Agreement into the Protocol, the form of wording would not be needed;
- Article 15(b) states that, “the relevant provisions of the SCM Agreement shall apply; *however ...*” This demonstrates that what follows the “however” is outside the normal rules, and that the subordinate clause provides for additional rules;
- when Members use the methodologies set out in 15(a) (antidumping) and 15(b) (CVD), they are required to notify the WTO. If these methodologies were the norm, no such notification would be required; and
- 15(a) expires once a market economy is established in China. However, Members realized that it would not be necessary to require 15(b) to expire, because once there is a market economy, there would be no “special difficulty” in establishing a market benchmark.

4. Attached as Exhibits CDA-63 to CDA-70 please find provincial forest tenure agreements and the relevant underlying legislation from B.C. and Alberta.

5. Commerce did not request any information related to the pass-through issue. Instead, Commerce simply presumed that any subsidy provided on the upstream input logs was automatically passed through in the arm’s-length sale of those logs.

In its submissions, Canada demonstrated that it was impermissible for Commerce to presume benefits to subject merchandise without conducting an upstream subsidy analysis. Canada also demonstrated that in many instances any alleged subsidization would not be passed through from harvesters to arm’s-length lumber producers. These submissions were also consistent with Commerce’s pass-through determination in Lumber III.

Canada also submitted applications for exclusion from many producers who had purchased lumber at arm’s-length from unrelated suppliers. In many instances, these producers were also independent remanufacturers (i.e., completely unrelated to firms with harvesting rights).

B.C. provided information on the purchase and sale of logs in the province. That information, set out in Question 7 above, included the volume and value of logs sold in each log market within the province, as well as detailed information describing the functioning and operation of each log market.

Furthermore, the B.C. log sales information contained sufficient detail to establish the total volume of softwood logs sold domestically to unrelated purchasers on the coast and in the interior. B.C.’s initial questionnaire response stated that, over the past three years, between 26 and 30 per cent of the timber harvested on the Coast was sold through the VLM. This response also demonstrated that between 22 and 25 per cent of the timber harvested in the interior was sold domestically rather than internally consumed by integrated companies.

Alberta stated unequivocally in its’ Questionnaire Response to Commerce that it did not interfere in the disposition of logs harvested from Crown land. Alberta also stated that, “The Province

of Alberta has no policies, regulations or statutes that require, encourage or discourage companies to produce certain products. The expectation is just that operators should make efficient use of the wood fibre.” Alberta also provided extensive data on arm’s-length log sales.

Ontario informed Commerce in its initial questionnaire response that timber is often obtained through an arm’s-length purchase from the private party that acquired it from the Crown (resale). Ontario also provided Commerce with a report prepared by KPMG concerning Crown timber resold at arm’s-length in an after-market. This report demonstrated that approximately 30 per cent of the softwood timber harvested from Crown land was sold by tenure holders to independent third parties who subsequently processed it into forest products.

## ANNEX A-2

### RESPONSES OF THE UNITED STATES TO QUESTIONS POSED IN THE CONTEXT OF THE FIRST SUBSTANTIVE MEETING OF THE PANEL

(21 May 2002)

#### Questions to the United States

1. **Q1:** At the time of the Preliminary Determination, the Commerce Department had extensive evidence on the record indicating that the vast majority of government timber in Canada was provided directly to tenure holders that owned sawmills or other wood processing facilities. Specifically, the laws and regulations of each Canadian province (with the partial exception of Ontario) generally require that tenure holders be sawmills. The evidence described below for each province consisted primarily of provincial legislation, sample tenure contracts and statistical data provided by the provincial governments.

2. More than 83 per cent of the B.C. Crown softwood timber harvest is provided to holders of four types of B.C. tenures. Each of these tenures *requires* the tenure holder to own a processing facility (for these purposes, a sawmill) and process the harvested timber (or an equivalent volume) in its own mill. The remaining B.C. Crown timber is provided under licences that are normally reserved to entities not owning timber processing facilities. However, the B.C. Forest Act requires that all timber harvested from Crown lands be processed in B.C. In addition, other legal restrictions apply to these forms of B.C. tenure, which indicate that transactions for the timber covered by these tenures are not at arm's-length.

3. Quebec ensures that only sawmills are permitted to harvest the vast majority of Crown softwood timber. For example, section 37 of the Quebec Forest Act states that “[n]o one except a person authorized under Title IV to construct or operate a wood processing plant is qualified to enter into” a Timber Supply and Forest Management Agreement, the virtually exclusive form of tenure in Quebec (covering 99 per cent of the Crown harvest).

4. In its questionnaire response, Ontario stated that “[g]enerally, in order to obtain any type of licence, an applicant must either own a forest resource processing facility (e.g., a sawmill, pulpmill, veneer mill, etc.) or must have a market to supply wood to some type of forest resource processing facility.” Alberta stated that “[a]ll forms of commercial tenure own and operate sawmills”.

5. In Saskatchewan, 86 per cent of softwood sawlogs were harvested by Forest Management Agreement holders, all of whom own sawmills and process their own timber. The remainder of the harvest was provided to smaller licencees under Forest Product Permits, some of whom have their own sawmills.

6. In Manitoba, 49 per cent of softwood sawlogs were provided to holders of Forest Management Licences, who by law are required to own timber processing facilities. Virtually all of the remaining 51 per cent of softwood sawlogs were provided under Timber Sales Agreements (“TSA”). The volume of softwood harvested by TSA holders owning sawmills amounted to 46 per

cent of the total softwood sawlog harvest. Thus, approximately 95 per cent of softwood sawlogs were provided directly to sawmills in Manitoba.

7. With respect to the obligations undertaken by the tenure holders, the Commerce Department examined the obligations that tenure holders were legally obligated to assume in Canada and compared them to those assumed by harvesters of the benchmark timber. The Commerce Department calculated a per-unit amount for each category of Canadian obligations that was above and beyond obligations incurred by parties paying stumpage charges in the United States. The Commerce Department used the values for each obligation provided by the Canadian provincial governments in their questionnaire responses, and considered the per-unit cost of these obligations as a form of “in-kind” payment, which it added to the stumpage fee.

8. **Q2(a):** Article 14(d) sets forth guidelines for determining whether the government has provided a good, within the meaning of Article 1.1(a)(1)(iii), for less than adequate remuneration. There should be no doubt that, through timber tenures, the provincial governments provide a good – timber – to lumber producers. Canada’s claims to the contrary are contradicted by ordinary dictionary definitions and Canada’s own laws. Because the provincial governments are unquestionably providing a good within the meaning of Article 1.1(a)(1)(iii), Article 14(d) provides the appropriate guidelines for determining the benefit.

9. **Q2(b):** The phrase “in relation to prevailing market conditions for the good . . . in the country of provision” in Article 14(d) does not restrict the authority to using only prices between buyers and sellers in the country under investigation. The concept of commercial availability is expressly incorporated in Article 14(d), which defines “prevailing market conditions for the good” to include, *inter alia*, availability. Prevailing market conditions in the country of provision may therefore encompass prices commercially available on the world market to purchasers in the country under investigation. The flexibility to use commercially available world market prices in Article 14(d) is reflected in item (d) of the Illustrative List of Export Subsidies, and was confirmed by the panel and the Appellate Body in *Canada Dairy*.

10. The use of world market prices commercially available to producers in the country under investigation is therefore not *per se* inconsistent with Article 14(d). Canada has, in fact, conceded that world market prices can constitute an appropriate benchmark in certain situations. An obvious example of when commercially available world market prices may be an appropriate benchmark is where the government is the sole provider of the input in the country under investigation. The facts of this case present an analogous situation. Specifically, only two provinces provided any information on private stumpage prices, and that limited information was inadequate to serve as a benchmark for those provinces. Moreover, the evidence indicates that the Canadian provincial governments so dominate the market for timber that below-market government prices suppress prices in the small market for private timber in Canada.

11. The Commerce Department’s use of US prices, as opposed to other world market prices, is supported by ample record evidence indicating that Canadian companies import US logs and bid on US stumpage. US timber is therefore “commercially available” to Canadian mills.

12. **Q2(c):** The US interpretation of Article 14(d) is consistent with the general meaning of “benefit” as previously articulated by panels and the Appellate Body, i.e., a benefit is some form of advantage that would not otherwise be available in the marketplace, absent the financial contribution. In *Canada Aircraft*, the panel stated that “[i]n order to determine whether the financial contribution . . . confers a ‘benefit’, i.e., an advantage, it is necessary to determine whether the financial contribution places the recipient in a more advantageous position than would have been the case *but for* the financial contribution. In our view, the only logical basis for determining the position the recipient would have been in absent the financial contribution is the market.” (emphasis added). The

Appellate Body in *Canada Aircraft* similarly stated that “there can be no ‘benefit’ to the recipient unless the ‘financial contribution’ makes the recipient *‘better off’ than it would otherwise have been, absent the contribution*. In our view, the marketplace provides an appropriate basis for comparison in determining whether a ‘benefit’ has been ‘conferred’, because the *trade-distorting potential* of a ‘financial contribution’ can be identified by determining whether the recipient has received a ‘financial contribution’ on terms more favourable than those available to the recipient in the market.” (emphasis added).

13. **Q2(d):** The comparison in Article 14(d) is intended to identify the potentially trade-distorting artificial advantage resulting from the government’s provision of a good. Commercially available prices in the country under investigation are normally the most appropriate benchmark. However, where the evidence indicates that the government so dominates the market that non-government domestic prices for the good in question are suppressed by the alleged below-market government prices for that good, the domestic prices cannot serve as a basis to measure the potential benefit. In such cases, other prices commercially available to producers in the country under investigation can provide an appropriate benchmark.

14. **Q2(e):** The purpose of the Article 14(d) comparison is to determine what, if any, advantage flows from the government’s financial contribution at issue, not other government actions.

15. **Q2(f):** The only instance in which we might even inquire into whether prices in the country under investigation are below world market prices would be where there is other evidence indicating that the non-government prices in the country under investigation may be distorted by the government financial contribution at issue.

16. **Q2(g)(i),(ii):** In this case, and in the only other case in which the Commerce Department has addressed this issue, the government’s share of the market was 90 per cent or more. However, each case must be evaluated on the basis of its particular facts. Normally, where the government dominates the market for a particular good and there is some evidence that government prices are suppressing the rest of the market, the non-government prices could not logically serve as a benchmark. However, that may not always be the case. For example, even where the government dominates the market, if there is an open and competitive auction for some significant portion of the market, those prices could serve as a benchmark. There may also be other instances in which the facts would indicate that the non-government portion of the market was undistorted by the government action. In such cases, the non-government portion of the market could also serve as a benchmark.

17. **Q2(h):** The Commerce Department requested information on private stumpage prices and prices in the spot market for logs in the Maritime Provinces. In their questionnaire response, the Maritime Provinces stated that they had no information on private stumpage prices, that “[t]here is no spot market price for harvested saw logs from Crown land”, that they do “not collect any data concerning spot market prices for . . . logs harvested from private land”, and that surveys of prices for logs harvested from private land “appear to be based on limited sampling”. Given this limited and inadequate information, the Commerce Department was unable to consider whether Maritime prices could serve as an appropriate benchmark.

18. **Q3:** The Commerce Department asked a series of questions regarding private prices in each province or territory. Only the governments of Alberta, Quebec and Ontario provided any information in response to this request. And, as described below, only Quebec and Ontario actually provided private prices. This limited information was insufficient to form the basis for a benchmark for these provinces. In addition, there was information on the record indicating that these private stumpage prices were depressed by the government prices. The largest province in terms of softwood lumber production, British Columbia (representing approximately 60 per cent of Canada’s softwood lumber production), did not provide any private prices for stumpage.

19. Alberta did not provide private prices. In its questionnaire response, it stated: “Alberta does not track private timber harvesting and does not have any data on any private timber used in mills.” It also stated that it “does not collect spot price information for logs from provincial or private lands” and it therefore was “not providing such spot log price information” to the Commerce Department. The only information Alberta did provide was a two-page excerpt from a KPMG survey, which contained a single estimated stumpage value derived from some price data for log sales. No supporting evidence or source information for the estimate was provided.

20. In its questionnaire response, Quebec stated: “Private market standing timber prices are obtained through a market survey of forestry companies that trade standing timber for harvesting every year in Quebec.” However, the Commerce Department also had evidence that private stumpage prices in Quebec are suppressed by the administratively-set price for Crown stumpage.

21. Ontario stated that over 10 per cent of the timber consumed in Ontario’s “forest products industry” is harvested from private lands. However, that figure covers the entire forest products industry, including companies that do not produce the subject merchandise (e.g., pulp mills). Moreover, Ontario stated that it does not regulate or monitor the private timber market on an ongoing basis, and therefore does not collect these data in the course of normal operations. Ontario commissioned an independent forestry research firm to conduct a survey, but the Commerce Department found numerous flaws with this study.

22. The record also contained evidence indicating that private stumpage prices were depressed by the overwhelming majority of government-supplied timber in the market. For example, a Canadian forestry expert concluded that “[t]he *quasi-monopolistic importance of the State in the supply* of the industries *obligates the small producers to align their prices with those of the public forest*”. (emphasis added). Even a provincial forestry official stated in writing that private stumpage prices were affected by the administratively-set price for public stumpage.

23. **Q4:** The statement the Panel refers to pertained to the small private market for stumpage, not log sales. The evidence at the time of the Preliminary Determination indicated that Crown and private stumpage sales were the following percentages of the harvest in each province:

	<u>Crown Sales</u>	<u>Private Sales</u>
British Columbia:	90 per cent	10 per cent
Quebec:	83 per cent	17 per cent
Ontario:	92 per cent	8 per cent
Alberta:	98 per cent	2 per cent
Manitoba:	94 per cent	6 per cent
Saskatchewan:	90 per cent	10 per cent

Only two of the provinces provided data on private stumpage prices, and record evidence indicated that those prices were suppressed by the governments’ administratively-set prices.

24. **Q5:** As stated in the chapeau to Article 14, and confirmed by the Appellate Body in *Canada Aircraft*, the benefit for purposes of Article 1 is the benefit to the recipient. It is the artificial advantage – or benefit – that the Appellate Body in *Canada Aircraft* referred to as the “trade-distorting potential” of a financial contribution. It is to that trade-distorting artificial advantage that the United States was referring in the passage cited by the Panel.

25. **Q6:** *Lead and Bismuth II* concerned subsidies to a government-owned entity, British Steel, which was subsequently sold to private investors. The panel stated that the presumption that the

benefit flowing from a financial contribution continues to flow, even after a change in ownership that created an apparently new and distinct producer, could not be irrebuttable. The panel found that the circumstances in that proceeding, in which British Steel's specialty steels business was first transferred to the partnership UES and then re-acquired by BSplc, rebutted the presumption that the benefit to British Steel continued in UES and BSplc. The panel also found that UES and BSplc were distinct legal persons which, because they had paid fair market value for the assets of British Steel, obtained no benefit from the prior subsidies to British Steel.

26. *Lead and Bismuth II* addressed circumstances that are not present in this case. Most significantly, in the present case the subsidies at issue were bestowed directly on the current producers of the subject merchandise. The evidence simply does not support Canada's claim of a significant volume of timber harvested by independent loggers who sell at arm's-length to lumber mills. The vast majority of Crown sawtimber is provided to Canadian lumber mills under tenures held directly by those mills. Record evidence also indicates that most "independent" loggers are in fact bound by law or by contract to those very same sawmill/tenure holders. Thus, the entity receiving the financial contribution (the provision of timber) and the entity receiving the benefit (below-market stumpage prices) are generally one and the same. As discussed below in response to question 7 to the United States, the other two situations in this case in which the issue of whether a financial contribution to one entity confers a benefit on another may arise – logs harvested by one sawmill and then sold in arm's-length transactions to other sawmills, and lumber sold in arm's-length transactions to companies that produce remanufactured lumber products – are not relevant in an aggregate case.

27. **Q7:** In an aggregate case, the Commerce Department determines the total amount of the subsidy to producers of the subject merchandise and allocates that amount over all sales of the subject merchandise. When all of the alleged recipients of the financial contribution and the benefits are producers of the subject merchandise, no further analysis is required. The precise amount of the benefit received by any specific producer would only be determined in a company-specific review. However, if the government made the financial contribution to an entity that does *not* produce the subject merchandise, it would be necessary to analyze whether that financial contribution benefited another entity that *does* produce the subject merchandise. In this case, the only allegation of a financial contribution to an entity that does not produce the subject merchandise is Canada's claim that there is a significant volume of Crown timber that the provincial governments provide to independent loggers who then sell the timber at arm's-length to lumber mills. However, the evidence does not support Canada's claim.

28. Canada also argues that the Commerce Department was required to perform a pass-through analysis to address two other situations: (1) logs harvested by one sawmill and then sold in arm's-length transactions to other sawmills; and (2) lumber sold in arm's-length transactions to companies that produce remanufactured lumber products. However, in both of these situations, all of the entities involved are producers of the subject merchandise. Therefore, no further analysis is required in an aggregate case. Specifically, a separate benefit analysis is not required in an aggregate case for logs harvested by one sawmill and allegedly sold at arm's-length to another, as the full benefit is always enjoyed by a sawmill, i.e., a producer of the subject merchandise. Likewise, the remanufactured articles at issue are within the scope of the investigation. The Commerce Department therefore properly matched the total benefit received by producers of the subject merchandise (the numerator) to the total sales of the subject merchandise, including remanufactured products (the denominator), without determining any company-specific rates. If any individual producer of subject merchandise believes that it has not received any countervailable benefit, the procedures for review exist.

29. **Q8:** There seems to be no question that provisional countervailing duties would constitute a provisional measure within the meaning of Article 17. Although Article 17.2 is somewhat ambiguous, a cash deposit or bond requirement would also appear to constitute a provisional measure

within the meaning of Article 17. While the United States did not impose a provisional duty, it did require security in the form of cash deposits or bonds.

30. There is no reference in Article 17.2 to withholding of appraisal, which is referred to in the United States as suspension of liquidation. Suspension of liquidation is merely a legal status that enables the assessment of additional duties when all of the issues related to final duty liability are resolved. Nevertheless, under the US countervailing duty law, suspension of liquidation is treated as a provisional measure.

31. **Q9:** Under US law, absent suspension of liquidation, final duties are assessed and no additional duties can be imposed on that entry. Suspension of liquidation is therefore essential to preserve the possibility of exercising the right under Article 20.6 to impose duties retroactively.

32. **Q10:** Suspension of liquidation would enable the Commerce Department to delay final determination of total duty liability. However, if no amount is guaranteed by a cash deposit or bond, Article 20.3 would, on its face, preclude the collection of duties retroactively.

33. The absence of an analogue in the SCM Agreement to Article 10.7 of the Anti-Dumping Agreement does not alter this analysis. Article 10.7 authorizes authorities to take measures even before there is a preliminary determination of dumping or injury. In the case concerning *Hot-Rolled Steel from Japan*, the panel viewed these special “precautionary measures” as something other than provisional measures. Because there is no analogue to Article 10.7 in the SCM Agreement, there is no exception to the requirements of Article 17.1 of the SCM Agreement that would permit early “precautionary measures”. However, the Commerce Department did not take such measures in this case. Where, as in this case, provisional measures are imposed in accordance with Article 17 (i.e., after preliminary determinations of subsidization and injury), Article 20.1 permits a Member to expand the scope of those provisional measures to encompass entries 90 days prior to the preliminary determination if there is sufficient evidence that the circumstances described in Article 20.6 exist.

34. **Q11:** Both suspension of liquidation and the posting of bonds or cash deposits are necessary to ensure the possibility of exercising the right to retroactive relief provided for in Article 20.6. The reference to “suspension of liquidation” in the Preliminary Determination is a short form of reference sometimes used by the Commerce Department when discussing provisional measures generally, including posting of bonds or cash deposits.

35. **Q12:** Article 20.6 requires a finding of “injury which is difficult to repair,” but does not contain an evidentiary standard for that determination. However, this issue was addressed by the panel in *Hot-Rolled Steel from Japan*, which concerned the evidentiary standard in the US anti-dumping law for a preliminary critical circumstances finding. That evidentiary standard is “a reasonable basis to believe or suspect” that critical circumstances exist. That is also the standard in the US countervailing duty law for a preliminary critical circumstances finding. The *Hot-Rolled Steel from Japan* panel found that in applying that standard, the Commerce Department has “made affirmative determinations when sufficient evidence was adduced that the conditions of application were satisfied.” As the *Hot-Rolled Steel from Japan* panel noted, “sufficient evidence” refers to the quantum of evidence necessary to make a determination. What constitutes “sufficient evidence” varies depending on the nature of the determination in question. The approach taken by other panels “has been to examine whether the evidence before the authority at the time it made its determination was such that an unbiased and objective investigating authority evaluating that evidence could properly have made the determination”.

36. **Q13:** Section 351.213(b) of the regulations does not apply to aggregate cases but it does not restrict the Commerce Department’s authority to conduct reviews. The inquiry required in Article 21.2 of the SCM Agreement, on which Canada’s claim is based, is whether continued

imposition of the duty is necessary to offset subsidization. Under section 351.213(k) of the regulations, exporters have the opportunity for a review to determine whether imposition of a duty is necessary on future entries, i.e., whether their subsidy rate is zero. If no subsidy is found, the cash deposit and assessment rate on future entries will be zero, unless the results of a subsequent review demonstrate that subsidies have recurred. Section 351.213(k) therefore fulfills the requirements of Article 21.2.

### Questions to Both Parties

37. **Q1:** While some financial contributions take place at a single point in time, that is not always the case. The Canadian timber tenures are long-term contracts that provide recurring subsidies. As long as the tenure contract remains in force the provincial government is providing the lumber producer with timber, and the producer receives a benefit each time it pays below-market prices for the timber.

38. **Q2:** While there is no uniform world market price for softwood lumber and softwood logs, lumber and logs are traded internationally in all regions of the world. It is possible to calculate average unit import values for lumber and logs in various countries based on either import or export statistics. However, because these statistics are kept on a broad product category basis, the average unit import values are not useful for comparison purposes.

39. **Q3:** The United States negotiated the language of Article 15(b) of the China Protocol, which was intended to clarify that Article 14 of the SCM Agreement allows authorities to measure the benefit on the basis of a benchmark outside the country of investigation when prevailing terms and conditions in the country of investigation are “not . . . available as appropriate benchmarks.” Although Article 14 of the SCM Agreement already allows Members to use such benchmarks, the Members incorporated this clarifying language into Article 15(b) of the China Protocol because they were concerned that prices in China would not be appropriate benchmarks while China was transitioning to a market economy and they wanted to leave no doubt that Article 14 allowed authorities to use external benchmarks in such instances. In addition, because Article 14 only addresses countervailing duty proceedings under Part V of the SCM Agreement, they wanted to make clear that external benchmarks would also remain available were a Member to pursue a WTO proceeding under Part II or III of the Agreement.

40. Article 15(b) is only one of several provisions of the China Protocol that simply restate and clarify existing WTO obligations that apply to all Members. Article 10.1 of the China Protocol, for example, restates existing obligations in Article 25 of the SCM Agreement. Several articles of the China Protocol also restate and clarify existing WTO most-favoured nation and national treatment obligations.

41. **Q4:** This information has been provided in response to question 1 to the United States.

42. **Q5:** In an aggregate case, the Commerce Department determines the total amount of the subsidy to producers of the subject merchandise and allocates that amount over all sales of the subject merchandise. When all of the alleged recipients of the financial contribution and the benefits are producers of the subject merchandise, no further analysis is required to perform the aggregate calculation. Benefits that potentially shift from one producer to another in an arm’s-length transaction would still be part of the overall numerator, as long as both companies produce subject merchandise. Therefore, for two of the three categories that Canada claims a pass-through analysis was necessary – logs harvested by one sawmill and then sold to another, and lumber sold to remanufacturers – the question of pass-through is moot in an aggregate context and the Commerce Department did not request any information on these types of transactions.

43. For the remaining category where Canada claims a pass-through analysis is necessary – independent loggers selling to sawmills – the Commerce Department asked questions about logs sold domestically at arm’s-length prices. In response, Quebec indicated that there were essentially no arm’s-length transactions involving Crown timber sold by independent loggers to sawmills. Ontario suggested that 30 per cent of Crown timber was sold in arm’s-length transactions, but tenure holders who do not own a sawmill are limited with respect to where such harvested timber can be sold and evidence indicated that log swapping was common among large tenure holders. Alberta’s questionnaire response suggested that only a small portion of the harvest was characterized by arm’s-length transactions. B.C. suggested that as much as 30 per cent of Crown timber was sold in arm’s-length transactions, but this figure is misleading because loggers operate as employees or contractors for tenure holders, various requirements serve to narrow the range of purchasers available to any harvester of Crown timber who is not a mill owner, and log swapping is a major part of the so-called arm’s-length transactions. These factors combine to ensure that the great majority of Crown timber is force-fed to tenure-holding lumber producers. As such, the evidence does not support Canada’s claim that a pass-through analysis is necessary or appropriate.

#### Questions to Canada

44. **Q5:** A Member is not always obliged to determine the benefit using as a benchmark market prices from the country under investigation. This is confirmed by numerous references in WTO agreements and prior WTO decisions. The United States also notes that the Panel’s example of a government monopoly over the supply of a good is no different in principle from the circumstances of the instant case, where the provincial governments control 85 to 95 per cent of the market for timber. If it is shown that the government supply significantly distorts the market, the benchmark can be found outside the country, so long as a reasonable effort is made to measure the benefit provided in the country under investigation.

45. **Q8:** Given the ordinary meaning of “arm’s-length,” a so-called independent logger should only be viewed as operating at “arm’s-length” from lumber producers if the harvester is freely negotiating, under no outside control or influence and under no compulsion to sell. The record establishes that not only are there very few transactions by independent harvesters, but even in such transactions, the provincial governments impose numerous restrictions and requirements on the transactions. In light of this evidence, the only reasonable conclusion is that there are no true arm’s-length transactions for Crown timber.

46. **Q10:** Past determinations by the Commerce Department, which apply US law on the basis of different factual records, are of no relevance in determining whether the United States has acted consistently with its obligations in the present case. That is particularly true where, as here, the prior determinations at issue were decided under a different domestic legal standard, as well as different international obligations. At the time of the *Lumber III* determination cited by Canada, under US law the government provision of a good was deemed to provide a benefit if the good “was provided at preferential rates”. That standard is fundamentally different than the current “adequate remuneration” standard and therefore the issue of an appropriate benchmark is fundamentally different as well. The Commerce Department rejected cross-border prices in *Lumber III* because it had “sufficient and reliable non-preferential price data” from within Canada. Other factors, such as comparability, were therefore moot and were simply noted in passing to underscore the Commerce Department’s primary rationale.

47. **Q14(b):** The Commerce Department did not investigate and, therefore, did not conclude that the Maritime Provinces received no support or that lumber sales from the Maritime Provinces were not subsidized.

48. **Q14(e):** Nothing in the SCM Agreement addresses the calculation of a “country-wide rate”. The “country-wide rate” at issue is a creature of US law, not the WTO. Under current US law, the calculation of the country-wide rate is based on the total amount of the subsidy found to exist with respect to the *subject merchandise*, allocated across all sales of the *subject merchandise*. Nothing in US law or practice requires that non-subject merchandise be included in a country-wide rate calculation.