

ANNEX B

PARTIES' RESPONSES TO QUESTIONS FROM THE SECOND MEETING

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ANNEX B-1

CANADA RESPONSE TO QUESTIONS FROM THE PANEL AT THE SECOND MEETING

(4 April 2003)

To both parties

Q1. Could the parties please comment on the relevance, if any, of footnote 36 to Article 10 in the context of Canada's pass-through claim, in particular Canada's assertion that the Agreement requires that the calculation of the subsidization rate of the investigated product must be accurate.

Reply

1. Footnote 36 defines the term “countervailing duty” as a special duty levied for the purpose of “offsetting any subsidy bestowed directly or indirectly”. The ordinary meaning of “offset” is “[s]et off as an equivalent *against*; cancel out by, balance by something on the other side or of contrary nature; counterbalance, compensate”.¹ The concept is further illustrated by the French text of Article 10, which provides that countervailing duties are designed to ‘*neutraliser toute subvention accordée*’. The United States violated Article 10 of the SCM Agreement because it failed to determine the existence of a subsidy before imposing countervailing duties. Where a Member imposes countervailing measures in the absence of a subsidy, there is nothing to “offset” and the duty imposed has no legal justification. Where no subsidy exists, the subsidy amount is zero – not some presumed amount.

2. Other panels and the Appellate Body have examined Article 10 of the SCM Agreement and the relevance of footnote 36. In *United States – Lead and Bismuth II*, a case involving another instance of an impermissible presumption of subsidization by the United States, the panel confirmed that the determination of the existence of a subsidy was a fundamental condition to the lawful imposition of countervailing duties.² The United States agreed.³ The panel stated in particular:

In our view, [the provisions of the SCM Agreement governing the imposition of countervailing measures] are all based on the premise that no countervailing duty may be imposed absent (countervailable) subsidization. Furthermore, we consider that this premise underlies the very purpose of the countervailing measures envisaged by Part V of the SCM Agreement. Footnote 36 to Article 10 of the SCM Agreement provides that “[t]he term ‘countervailing duty’ shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly [...]”. Thus, the imposition of a countervailing duty is only envisaged in

¹ *New Shorter Oxford English Dictionary* (Oxford: Clarendon Press, 1993) at p. 1985. (Exhibit CDA-171)

² *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, Report of the Panel, WT/DS138/R, adopted 7 June 2000, at paras. 6.45-6.57 [“*United States – Lead and Bismuth II*”].

³ *Ibid.*, at para. 6.43, footnote 62 (“[T]he investigating authority must first identify the existence of a subsidy before measuring and allocating the amount of the subsidy found to exist or imposing a countervailing duty”).

circumstances where it is necessary to “offset” a (countervailable) subsidy. In our view, footnote 36 to Article 10 does not envisage the imposition of countervailing duties when no (countervailable) subsidy is found to exist, for in such cases there would be no (countervailable) subsidy to “offset”.⁴

3. The Appellate Body confirmed the panel’s findings in that case.⁵ In *United States – Countervailing Measures Concerning Certain Products from the European Communities*, a case concerning yet more instances of presumed subsidization by the United States, the panel, relying on the text of footnote 36, found that a determination of subsidization in an investigation or review “must be made before countervailing duties can be imposed, and permits a calculation of the extent of subsidization”.⁶ The Appellate Body upheld this finding, and recalled that a subsidy under Article 1.1 is composed of both a “financial contribution” and “benefit”.⁷ It then confirmed that Article VI of GATT 1994 requires an investigating authority to “ascertain the precise amount of a subsidy attributed to the imported product,” and noted Article 10 in furtherance of this obligation.⁸

4. In this case, because the United States has failed to conduct any pass-through analysis and therefore failed to establish the existence of a subsidy, the volume of Crown timber harvested by entities that did not produce subject lumber and the amount of subsidy derived from that volume, for example, must be excluded from the numerator in the subsidy rate calculation. Likewise, no duty can lawfully be imposed on the products of lumber remanufacturers purchasing at arm’s-length.

5. Footnote 36 confirms that pursuant to Article 19.4, in all instances, the subsidy amount must accurately reflect the subsidization found.

Q2. Is it relevant to the interpretation of Article 14(d), in particular its reference to "... in the country of provision", that Articles 14(b) and 14(c) contain no similar reference?

Reply

6. The absence of any reference to “prevailing market conditions ... in the country of provision” in Articles 14(b) and 14(c) is relevant to the interpretation of Article 14(d), as the entirety of Article 14 provides context for this provision.

7. Contrary to what the United States claims, the guidelines contained in Article 14 are not “general principles” that provide no limitation on how Members must measure benefit. Rather, Article 14 prescribes clear rules for measuring benefit with which Members must comply when the financial contribution at issue involves the government provision of equity capital, loans, loan guarantees or goods or services.

8. Articles 14(b) and (c) deal with loans and loan guarantees. Unlike Article 14(d), they do not contain the phrase “in the country of provision”. They therefore do not restrict the benchmark that must be used to measure benefit to in-country benchmarks, in the way Article 14(d) does. That this phrase was included in Article 14(d) and not in Articles 14 (b) or (c) is evidence of the intent of the Members at the time the SCM Agreement was negotiated to distinguish between situations where an

⁴ *Ibid.*, at para. 6.56.

⁵ *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, Report of the Appellate Body, WT/DS138/AB/R, adopted 7 June 2000, at paras. 63 and 75(b).

⁶ *United States – Countervailing Measures Concerning Certain Products from the European Communities*, Report of the Panel, WT/DS212/R, adopted 8 January 2003, at paras. 7.41-7.44.

⁷ *United States – Countervailing Measures Concerning Certain Products from the European Communities*, Report of the Appellate Body, WT/DS212/AB/R, adopted 8 January 2003, at para. 139.

⁸ *Ibid.*

investigating authority should not be restricted to in-country benchmarks (e.g. due to the international nature of financing) and situations where an investigating authority should be so restricted.

Q3. Why, in the US view, are US stumpage prices broadly representative of market conditions in Canada? What is the motivation or incentive for Canadian harvesters to cut timber in the US, at much higher cost than in Canada, especially in the light of the abundant (in the US view, unlimited) supply of Crown timber? Would such purchases be typical, or instead essentially exceptional?

Reply

9. US stumpage prices are not broadly representative of market conditions in Canada for the myriad of reasons that Canada has set out in its Submissions. In particular borders affect prices profoundly and these effects are difficult if not impossible to quantify (political boundaries drive differences in government regulatory regimes, tax regimes, investment regimes, etc.). In addition, US standing timber is not of the same species mix, size, quality, or harvested under similar operating or sales conditions as Canadian standing timber. Moreover, there is a limited distance over which logs can be hauled economically. This is why standing timber is processed into logs, and then into lumber, close to the resource.

10. The only motivation for a Canadian harvester to cut timber in the United States and export the logs back to Canada would be that doing so was economically attractive in comparison with harvesting in Canada, as in the case of, for example, the high quality logs exported from Maine. Such transactions are almost entirely unique to Québec and are the exception for the rest of the country. The United States itself recognized the unique nature of the log trade between Québec and Maine in *United States – PD Softwood Lumber*. As the Panel's question suggests, if private prices in Québec were suppressed, this trade in logs would not exist, as these mills would source their logs from the domestic private market.

11. The import of logs into the rest of Canada represents less than 1 per cent of the total annual harvest.

Q4. In paragraph 40 of its second oral statement, Canada argues that "the fundamental basis for Commerce's rejection of in-country evidence was its reliance on the Preamble to its Regulations to presume price suppression". According to the parties, does the Preamble provide for such a presumption in case of dominant position by the government? According to the parties, did the USDOC interpret the Preamble to imply a presumption against the use of market data where the government holds a dominant position in the market? (See for example p. 37 CDA-1 or p. 58: "The preamble to section 351.511 of the Regulations provides that, where a government has a dominant position in a market, the Department will avoid the use of private prices in determining the adequacy of remuneration. Where the market for a particular good is so dominated by the presence of the government, the remaining private prices in the country in question cannot be considered to be independent of the government price").

Reply

12. The Preamble does not provide for a *per se* rule in the case of a dominant position by a government.⁹ The Preamble merely invites an inquiry into whether a large government presence in the market creates actual distortion. Commerce did not conduct such an inquiry. Rather, it treated the Preamble as imposing a *per se* rule and assumed price suppression based on government involvement in the marketplace.

⁹ Canada also notes that the Preamble does not override the US statute.

13. In paragraph 37 of the Final Determination Commerce described the Preamble as stating that “if the government provider constitutes a majority or a substantial portion of the market, *then* such prices in the country will no longer be considered market based and will not be an appropriate basis of comparison for determining whether there is a benefit.”[emphasis added]. Therefore, in the circumstances of this case, where the government is a “majority provider”, Commerce was not concerned with whether there were private prices in Canada because it had already dismissed these prices as “unusable”. Commerce therefore treated the Preamble as prescribing a *per se* rule that requires the rejection of in-country market transactions as benchmarks in any situation where the government is the “majority provider” of the good.

14. That this was in fact what Commerce did is reinforced by its statement in paragraph 58 of the Final Determination where, with reference to the Preamble alone, Commerce stated that it will avoid using private prices in circumstances where the government has a dominant position and that in such circumstances “the remaining private prices in the country of question *cannot* be considered to be independent of the government price” [emphasis added]. Thus the fact that Commerce found that the provincial governments were “majority providers” was sufficient for it to exclude consideration of private prices in Canada.

To the US

Q5. The US argues that any overstatement of the subsidy amount due to arms’ length transactions for logs between timber harvesters and lumber producers is now being addressed through individual expedited reviews being conducted by the USDOC. Could the US please explain how, if at all, such individual reviews affect the overall aggregate subsidization calculation. That is, does the aggregate subsidization rate remain the same, or is it recalculated to exclude the relevant amounts from the numerator, the denominator, or both, of subsidy amounts attributed to, and sales by, the individual firms subject to expedited review?

Reply

15. A recalculation of the country-wide subsidy rate by the United States at the conclusion of the expedited review process would not address the overstatement of the subsidy amount due to the illegal presumption of subsidy pass-through in arm’s-length transactions. This is because the presumption made was applied to all producers, not just those who have requested expedited reviews. A subsequent review of only a few producers, even if conducted properly, will not change the fact that the country-wide rate applicable to all other producers was established illegally.

16. It is also not certain that pass-through analysis in the expedited review proceedings will be undertaken at all. Almost a year has passed since issuance of the countervailing duty order and Commerce has not even issued a questionnaire eliciting information for a pass-through analysis, and has given no indication whether, or when, the requested pass-through analyses will be conducted.

Q6. Could the US respond to the statistics referred to in paragraph 57 of Canada's oral statement, i.e., that the US recognizes that in British Columbia, 24 per cent of Crown timber was harvested by entities that do not own sawmills, and that scores of producers purchased their log and lumber inputs in arms'-length transactions from independent harvesters and other entities.

Reply

17. Nothing in the SCM Agreement permits the presumption of a subsidy pass-through. At a minimum, an investigating authority must address any record evidence establishing arm’s-length

transactions.¹⁰ The panel in *United States – PD Softwood Lumber* confirmed this obligation.¹¹ The United States has admitted that such transactions exist in this case.¹² The US obligation to establish subsidization in the investigation and calculating the correct subsidy rate is not met by mischaracterizing record evidence after-the-fact in WTO proceedings, nor is it met by any subsequent company-specific review.¹³ By presuming a pass-through, the United States has both impermissibly overstated the subsidy amount and illegally imposed countervailing measures in the absence of a subsidy determination.

Q8. At para. 32 of the US second submission, the US states that the data on private stumpage prices in Ontario and Quebec highlight that "prices that are distorted by the government's financial contribution do not reflect 'market' conditions". Could the US please explain in what way this price information demonstrates this.

Reply

18. In its preliminary response to the Panel's question at the Second Substantive Meeting the US conceded that data on private stumpage prices do not prove price distortion in these provinces. Rather, it pointed to "other factors" that affect the price data so that this data cannot be used as a benchmark.

19. If the "other factors" the United States was referring to were the provincial forest management practices discussed in paragraphs 33-39 of its Second Written Submission, Canada has already observed that these practices were not the subject of the investigation. Moreover, the Final Determination did not analyse whether these forest management practices had any effect on private timber prices and certainly contained nothing demonstrating that these practices had "distorted" the market. Instead, Commerce relied heavily on the Preamble to reject in-country private prices supported by a few pieces of anecdotal evidence and a single fundamentally flawed economic analysis, as discussed in Canada's submissions.

Q9. Could the US respond to the argument at paragraph 40 of Canada's statement that the US took a selective approach to the record evidence in reaching its determination that Canadian private stumpage prices were distorted by the provincial stumpage programmes.

Reply

20. As explained in the comments Canada made at the Second Substantive Meeting, Canada's statement regarding "selective references" in paragraph 40 of its Oral Statement was intended to point out that the provincial forest management practices the United States referred to in its Second Written Submission were not the subject of this investigation. Furthermore, these practices did not form the basis for Commerce's conclusion in the Final Determination that private market prices for stumpage in Canada were distorted by government involvement in the marketplace. That determination was based solely on the Preamble, a flawed economic analysis and a few pieces of anecdotal evidence.

Q11. Could the US comment on Canada's argument at para. 28 of its second submission concerning the third benchmark in Section 351.511 of the USDOC Regulations. In particular, could the US comment, first, on Canada's argument that there are no world market prices for

¹⁰ Canada's Second Written Submission, at para. 48.

¹¹ *United States – Preliminary Determinations With Respect to Certain Softwood Lumber From Canada*, Report of the Panel, WT/DS236/R, adopted 1 November 2002, at para. 7.79 [*"United States – PD Softwood Lumber"*].

¹² Canada's Second Written Submission, at para. 48 and references to US submissions therein.

¹³ Canada's First Written Submission, at para. 146; Canada's Second Written Submission, at para. 48, fn 46.

stumpage, and second, on Canada's position that the evidence shows that provincial stumpage programmes are operated in a manner consistent with market principles, as foreseen by the USDOC Regulations.

Reply

21. The United States in this proceeding, unlike in *United States – PD Softwood Lumber*, has avoided arguing that US prices for short-term timber harvesting rights are “world market prices”. This is undoubtedly because no “world market prices” for stumpage exist.

22. Canada has addressed Commerce’s assertion that US prices for short-term cutting rights are “world market prices” in its previous submissions. However, even Commerce itself essentially accepted that there is no “world market price” for stumpage in the Final Determination when it selected benchmarks from multiple states. If there were in fact a “world market price” Commerce would have used a single benchmark for all of the Canadian provinces.

23. Canada further notes that the US admitted in its preliminary response to the Panel’s question that it would have used its third benchmark – consistency with market principles - if US stumpage prices had not satisfied the second benchmark.¹⁴

Q14. Could the US respond to the argument at paragraph 82 of Canada's oral statement, that new evidence from the petitioners' 4 March 2002 submission was in fact used by the USDOC in its subsidy calculations for Quebec.

Reply

24. At the Second Substantive Meeting of the Panel with the Parties, the United States admitted that the March 4, 2002, evidence submitted by the petitioners (Exhibit CDA-112) was, in fact, relied upon by Commerce in its subsidy calculations for Québec. The US admission confirms what Exhibit CDA-170 establishes, that Commerce used the March 4, 2002, evidence to calculate a Maine benchmark price to compare with Québec prices.

25. The United States has previously admitted that the March 4, 2002, submission by the petitioners contained new evidence that was not on the investigation record.¹⁵

26. Interested parties from Québec were denied any opportunity to prepare presentations on the basis of information the United States admits was new and was relied upon to calculate the Maine benchmark price. By its own admission, the United States has violated Article 12.3 of the SCM Agreement.

Q16. Could the US please respond to the argument in para. 81 of Canada's second submission that the US excluded from the denominator "other softwood products that were also produced in the sawmill establishments from logs entering those sawmills"?

¹⁴ The evidence on the record related to consistency with market principles is set out in Canada’s submissions. See: First Written Submission of Canada, at paras. 106 - 111; and Oral Statement of Canada at the First Substantive Meeting, at para. 54.

¹⁵ Answers of the United States of America to the Panel’s February 24, 2003 Questions, at footnote 72 [“US Answers”].

Reply

27. The United States included the total volume of logs that entered sawmill establishments in its calculation of the amount of the alleged subsidy (the numerator of its subsidy per unit calculation). However, it did not include the value of all products produced from those logs by those establishments in the denominator of its subsidy per unit calculation. Specifically, it did not include the value of residual non-lumber products produced by sawmill establishments in the denominator. This resulted in an inflated subsidy per unit rate. A countervailing duty imposed on the basis of such a rate violates Article 19.4.

28. In response to question 17 of the Panel's First Questions to the Parties, the United States conceded that it "would have included such products [residual products such as posts and ties] in the denominator had Canada provided data from which the value of these sales could have been derived."¹⁶ Likewise, in its Second Written Submission, the United States provided as follows:

To the extent that particular products in the residual products category resulted from the lumber production process, the United States *would have included the sale of such products in the denominator* if Canada had provided information from which the United States could have derived their value.

Canada failed to submit any evidence from which the United States could separate the value of additional products resulting from the lumber production process from the broader residual products category. Accordingly, the United States did not include the residual products category in the denominator.¹⁷ [emphasis added]

29. In the foregoing the United States admitted that the per unit subsidy rate was inflated. Therefore, the countervailing duty rate was correspondingly inflated and the United States has violated Article 19.4.

30. The US reasoning in defence of its violation has no basis in Article 19.4. The United States did not ask for a disaggregated breakdown of product values in the residual category at any point in the investigation.¹⁸

31. More important, the United States did not require disaggregated residual product data to accurately calculate the amount of the alleged subsidy. The United States had data on the record that allowed it to limit its subsidy per unit calculation to subject merchandise – softwood lumber products. By limiting the numerator to the volume of logs entering sawmills that results in softwood lumber only, the denominator could then have properly been limited to the sales value of softwood lumber products. There was no need to deal with the volume or value of residual products to accurately calculate the amount of the alleged subsidy. (This, however, would not have corrected for Commerce's errors in converting from MBF to m³ and in the use of understated final mill sales value data in the denominator.)

32. Even if it were appropriate to calculate the countervailing duty rate by dividing the subsidy to all logs that entered sawmill establishments by sales of all softwood products, the United States still had all the data it needed. The numerator was not limited to logs used in the softwood lumber production process, but included all logs that entered sawmill establishments. All products in the residual products category are softwood products produced by sawmills. Therefore, in such a calculation, all sales in the residual products category would have to have been included in the denominator.

¹⁶ *Ibid.*, at para. 38.

¹⁷ US Second Written Submission, at paras. 63-64.

¹⁸ Canada's Second Written Submission, at para. 83.

To Canada

Q17. With regard to the impermissibility of using US stumpage prices as the benchmark, the US argues in para. 48 of its second submission that: "Canada's assertions ... are based on its view that the provinces provide intangible harvesting 'rights' that cannot be imported". Could Canada please comment.

Reply

33. Canada's position with respect to the impermissibility of using US stumpage prices as the benchmark is based on the plain meaning of the text of Article 14(d). An investigating authority is required by the unambiguous language of Article 14(d) to use in-country benchmarks. As the panel in *United States – PD Softwood Lumber* concluded “the ordinary meaning of this provision excludes an analysis based on market conditions other than those in the country or provision of the goods, i.e. Canada”.¹⁹ The United States' reliance on cross-border comparisons therefore violates Article 14(d). Further, the alleged good Commerce claimed was subsidized was “standing timber”. Standing timber in the United States can only be purchased in the United States and trees growing in the United States cannot be harvested in Canada.

34. Finally, with respect to the right to harvest US standing timber, Canada notes that this right can only be exercised in the United States.

Q18. Given the existence of some US timber sales to Canadian harvesters, in what sense does Canada argue that US stumpage is not "available" to Canadian harvesters. Is it not possible for a Canadian harvester, located in Canada, to bid on and win bids for US timber?

Reply

36. While it is true that Canadian harvesters may bid on stumpage in the United States (in actual fact very few do) that does not make US stumpage available in Canada. US stumpage is not “available” to softwood lumber producers in Canada because timber can be harvested only in the country where it stands, even if the logs produced from its timber can be exported. Harvesting rights related to land cannot be exported across the border because the land cannot be. Just as it make no sense to say that land purchased in one country is also purchased in another country; it makes no sense to say that stumpage purchased in the United States is somehow purchased in Canada.

37. For a price to be available in the country of provision, the good or service must be available for purchase in the country of provision. The question therefore is whether the good is available for purchase in the country of provision. The alleged good that Commerce claimed was subsidized in this case is standing timber.

38. The United States deliberately blurs the distinction between logs and standing timber in order to make its argument that US stumpage is available in Canada. Even if the good at issue were logs, Commerce clearly did not consider the availability of logs a necessary element in its selection of benchmarks. For example, Commerce used the Minnesota benchmark for Alberta and Saskatchewan even though there was no record evidence that logs from Minnesota were available in either province. In addition log export restrictions in place on public lands in Washington, Idaho and Montana – which were the exclusive source of benchmarks for British Columbia - made the import of logs into Canada from these comparison areas impossible.

¹⁹ *United States – PD Softwood Lumber*, at para 7.44.

Q19. Could Canada please respond to the US example in paragraph 19 of the US oral statement, i.e., that based on Canada's argument, prices of products purchased FOB factory gate in the US, by purchasers located in Canada, are not "available" to those purchasers.

Reply

39. In the context of this case the only “products” that could be purchased FOB factory gate in the US are logs, not standing trees and it is standing trees that the United States has alleged is subsidized. The significance of this distinction is that while it may be argued that the logs in this example could be “available” in Canada if they are imported, it cannot be said that the standing timber used to process these logs in the United States is available in Canada. The reason for this is that there must be manufacturing activity involving those standing trees that takes place in the United States before the logs are exported. In this situation it cannot be said that the price of the standing trees that were used in the United States to produce those logs is available in Canada. It is not. It is a price wholly and only available in the United States.

Q20. Canada argues, at para. 74 of its second submission, that the numerator in a subsidization calculation must reflect the proportional amount of the subsidy that can be attributed to the subject merchandise. In other words, Canada's argument seems to be that there must be a volume-based allocation of subsidy amounts among a firm's different products, before the rate of subsidization of the subject merchandise can be calculated.

(a) Is this a correct characterization of Canada's argument on this point? If not, please clarify.

Reply

40. This is a correct characterization of Canada’s position concerning the calculation of the amount of the subsidy to be included in the numerator of the subsidy per unit calculation in this case.

41. Canada’s position is based on the fact that the alleged subsidy arises from the provision of an alleged good that is, in different proportions, a physical input to particular products, only one of which is subject merchandise. A volume-based allocation normally would not be necessary, for example, where the financial contribution is a grant or loan or other fungible resource, or where a good is equally an input to all products produced by a firm. In this case, however, where only a portion of a log (the input product produced from standing timber – the alleged good) produces softwood lumber, a volume allocation at the outset is the only means of properly determining the amount of the subsidy that goes to the allegedly subsidized products.

42. Canada does not suggest a rule for all subsidy calculations. Rather, an investigating authority is required, on the specific facts of each case, to ensure that it does not inflate the subsidy per unit rate. The United States failed to comply with that obligation in this case.

43. It is perhaps useful in order to fully understand Canada’s argument on this point to recall how Commerce calculated the subsidy per unit rate in this case.

- *The Subsidy Amount (numerator)* – Commerce calculated the amount of the alleged subsidy (numerator) by determining a benchmark price for harvested timber in each US state that it considered to be relevant for comparison purposes. The US benchmark prices were expressed in US log scale measurement units. In order to compare with Canadian provincial prices, Commerce converted the US benchmark prices into cubic metres. Commerce deducted its determined cost per cubic metre for harvested timber in each relevant province from the US state benchmark price Commerce considered relevant. Commerce then multiplied this per cubic metre price differential

by the total volume of softwood logs produced from Crown timber in each province that entered sawmills to determine a provincial subsidy amount.

- *The Subsidy Per Unit Rate* – In order to arrive at a subsidy per unit rate, the alleged subsidy was divided by a denominator that consisted of the sales value of some of the products produced from the volume of logs included in the numerator.²⁰

44. Based on the record evidence and the products at issue in this case, the most accurate method of calculating the subsidy amount in the numerator was to add the following step to Commerce's methodology: multiply the alleged subsidy amount by the volume of those softwood logs that actually went into the subject merchandise – softwood lumber products. The denominator could then properly be limited to the sales value of the subject merchandise rather than the value of all products produced from softwood logs that entered sawmill establishments.

- (b) **If this is a correct characterization of Canada's argument, how does Canada reconcile this with the fact that the de minimis rule for countervailing duties is expressed on an ad valorem basis in the SCM Agreement (e.g., Article 11.9)?**

Reply

45. There is no inconsistency between Canada's position and Article 11.9. Canada's proposed approach still results in the calculation of an *ad valorem* rate because the total subsidy in the numerator is still allocated over the total sales value of the subject merchandise.

- (c) **Similarly, how does Canada reconcile this position with the fact that the Annex IV guidelines for calculation of ad valorem subsidization of a product, in the context of (now expired) Article 6.1(a) specifically require that this rate of subsidization be calculated using the total value of the firm's sales as the denominator of the subsidization equation, except in the case of a tied subsidy, in which case the denominator is the value of the firm's sales to which that subsidy is tied? (In other words, the general approach was that the total subsidy amount would be divided by the firm's total sales to arrive at the ad valorem subsidization of the product.) In what way, analytically, is this different from what the USDOC did in the Lumber investigation?**

Reply

46. Subsidization per unit, mentioned in Article 19.4, is the amount of the subsidy attributable to a product subject to countervailing duties. A subsidy per unit rate is the *ad valorem* rate of subsidization, determined by dividing the subsidy attributable to a product by the value of that product.

47. In the case of a tied subsidy, as paragraph 3 of Annex IV sets out, the amount of a subsidy specifically earmarked for the production or sale of a product should be the amount divided by the value of that product, to yield a per unit rate.

48. In the case of an untied cash subsidy, because money is fungible, the assumption is that a producer receiving the subsidy would spread the total amount of the subsidy across the total volume

²⁰ As Canada noted in response to question 16, Commerce did not include the value of residual products in the denominator that were included in its calculation of the subsidy amount. In addition, Commerce used an inaccurate final mill sales value in the denominator that was too low to reflect the actual sales value of remanufactured products within the scope of the investigation.

of production. Accordingly, a rational and relatively easy way of determining the subsidy per unit rate would be to divide the total amount of the subsidy by the total volume of the recipient's sales.

49. In this case, the subsidy attributable to the production of softwood lumber is the volume of the allegedly subsidized log that is used in the production of softwood lumber. In this sense, the most rational way of determining the subsidy per unit rate for the subject merchandise is to determine the amount of the subsidy in the volume of log attributable to the subject merchandise, and to divide that by the value of the subject merchandise.

50. Commerce's approach differed from the one set out in paragraph 2 of Annex IV in two ways. First, as Canada has noted in response to question 16, the United States has admitted that Commerce left out some products from the denominator. When the total amount of the subsidy is divided by less than the total sales of the products to which the subsidy is attributable, by definition, the subsidy per unit rate is inflated.

51. Second, in the specific facts of this case – and this is where the question of “volume” is important – dividing the total amount of the subsidy by the total softwood product sales results in an inflation of the subsidy rate of the subject merchandise.²¹ This is because products other than lumber use very large volumes of wood, but are not valued as highly as the lumber products. Chips and sawdust (co-products), for example, are intermediate products, not finished goods like lumber, when they leave the sawmill. In the period of investigation, softwood lumber sales were 73 per cent of softwood product sales, while other softwood products were only 27 per cent of sales by sawmills.²² However, other softwood products accounted for more than 60 per cent of the volume of softwood products. The large amount these other products add to the numerator from the major wood volumes they use is not balanced out by the value contribution they make to the denominator – creating a sharp increase in the subsidy rate compared to a calculation using only lumber-related numbers.

52. Softwood products other than lumber (that is, co-products and residual products) account for about 60 per cent of the volume of logs that entered sawmills, or in other words, 60 per cent of the alleged subsidy. And yet, they account for about 23 per cent of the value of the production. Using the whole amount of the alleged subsidy, therefore, results in the impermissible attribution of subsidy to certain products and an inflation of the subsidy per unit rate for those products. In the case of Alberta, this aspect of Commerce's methodology had the effect of inflating the subsidy per unit rate from 12 per cent to more than 32 per cent.²³

Q21. Could Canada elaborate in more detail on its argument in paragraph 61 of its oral statement – that is, where exactly does Canada see an internal contradiction between the US pass-through and specificity arguments?

Reply

53. The United States found that that the alleged stumpage subsidy goes to primary sawmills holding harvesting rights, and presumed that the subsidy was passed-through to certain downstream remanufacturers that do not hold stumpage but that purchase Crown logs or lumber at arm's length. This presumption was based on the remanufacturers' use of an allegedly subsidized *input*, not on the nature of their *output*. And if the alleged stumpage subsidy automatically goes to downstream remanufacturers of subject lumber, then it also automatically goes to any other downstream producer.

²¹ See also Canada's Second Written Submission, at paras. 73-78.

²² Verification of the Government of Canada (January 23, 2002) at Exhibit 7 – “Worksheets for Calculating Total POI Lumber Shipments by Sawmills”. (Exhibit CDA-133)

²³ Canada's Second Written Submission, at para. 78.

54. In its specificity finding, however, the United States determined that the alleged stumpage subsidy was made *only* to “pulp and paper mills and the saw mills and remanufacturers *which are producing the subject merchandise*”. This finding is based on the nature of the output product. The two findings are not reconcilable: to the extent that a subsidy is “passed-through” to the users of lumber made from allegedly subsidized logs whether or not they harvested those logs, then the alleged subsidy is passed through to all users of products made from those logs. This universe of recipients is far larger than *only* the remanufacturers that produce the subject merchandise. It includes not only remanufacturers that produce non-subject merchandise, but also, the myriad other downstream industries using softwood-origin inputs.

55. This is but one example of the internal contradictions in the US logic. Another is in the US positions on financial contribution and specificity. If, as the US posits, the provision of an extraction/harvesting right (as in the case at hand) can be considered to be a “good” under Article 1, then Article 2 cannot be reduced to an analysis of whether the users of the harvesting right are fewer than everyone in the jurisdiction in question. To do so, as we have explained, reduces the specificity provision to automaticity and superfluousness. This, neither logic nor the principles of treaty interpretation will permit.

Q22. While Canada has indicated that during the investigation, Saskatchewan made clear that it rejected the use of any US state as a benchmark, the US argument at paragraph 40 seems to go to a different point, as the US indicated in its comments before the Panel at the second meeting. In particular, the US argument seems to be that Canada cannot now claim before the Panel that the USDOC's choice of a non-contiguous state as a benchmark for Alberta and Saskatchewan came as a complete surprise. The US cites as support for this assertion Saskatchewan's own arguments to the USDOC that if any cross-border comparison were to be used, Alaska, a non-contiguous state, was preferable to Montana, a contiguous state. Could Canada please address this specific point.

Reply

56. The United States has submitted a portion of a Saskatchewan reply brief to Commerce to this Panel and suggested that it demonstrates that interested parties should have been aware of the potential choice of a non-contiguous benchmark state to compare with Alberta and Saskatchewan.²⁴ This argument has no merit for at least two reasons.

57. First, even after Saskatchewan's reply brief was submitted on 22 February 2002, and in fact, even after the Final Determination was issued on 25 March 2002, the United States continued to justify Commerce's choice of benchmark states in the Preliminary Determination on the basis that the chosen states bordered the relevant provinces. On 13 June 2002, the United States filed the following in response to a panel's question in *United States – PD Softwood Lumber*:

Even within the United States, not all timber prices are appropriate. The Department of Commerce did not use prices from the large timber-growing areas in the southeast, *or from any non-contiguous state*, because as a matter of commercial reality, Canadian lumber producers do not consider it commercially viable to transport logs over that long a distance.²⁵ [emphasis added]

58. It is not credible to suggest that all interested parties, including those from Alberta, should have been aware of the potential choice of a non-contiguous benchmark state – let alone a “particular” non-contiguous benchmark state – on the basis of an alternative argument in a reply brief of one of the

²⁴ Case Brief of the Government of Saskatchewan, at pps. 25-27 (22 February 2002) (Exhibit US-95).

²⁵ *Answers of the United States of America to the Panel's 6 June 2002 Questions*, WT/DS236, 13 June 2002, at para. 95. (Exhibit CDA-162). See paras. 88-89 in Canada's Second Written Submission.

interested parties. This is especially true where the United States itself continued to justify the validity of the benchmarks in the Preliminary Determination even after the Final Determination on the basis that the relevant states bordered the provinces.

59. Second, the United States argues in its Second Oral Statement that interested parties “knew that factors such as climate, terrain, and species mix – not proximity – were the key considerations, and that a non-contiguous state might be selected for the benchmark.”²⁶ Rather than justifying Commerce’s unannounced switch of benchmark state, this substantiates the procedural violations claimed by Canada.

60. The portion of the Saskatchewan reply brief immediately preceding the excerpt submitted by the United States as Exhibit US-95, is dedicated to demonstrating the irrationality of using Montana as a basis of comparison with Saskatchewan for a variety of reasons including differences in commercial timber species mix, geography, topography and timber size.²⁷ In its reply brief, Saskatchewan noted that Montana and Saskatchewan have no commercial softwood species in common. While Saskatchewan’s commercial harvest is made up primarily of white spruce, jack pine and black spruce, Montana’s harvest is made up of Douglas fir, ponderosa pine and lodgepole pine.²⁸ Even though Saskatchewan did not advocate any cross-border comparison, it suggested Alaska as a potential benchmark because sales of the same commercial species were reported in both Saskatchewan and the interior of Alaska.

61. Saskatchewan and Alberta were able to make detailed and focussed presentations concerning Montana that highlighted differences in factors such as species mix, timber size, and geography, to name a few, precisely because they were aware that Montana was the potential benchmark state. They were able to demonstrate that Montana was an inappropriate benchmark because they were aware that it was under consideration and were able to tailor their submissions accordingly. As the United States has admitted, these submissions were instrumental in demonstrating that Commerce had erred in choosing Montana as the benchmark state in the Preliminary Determination.²⁹ Yet, interested parties were denied the same opportunity with respect to Minnesota. Commerce deprived itself of valuable information about the appropriateness of Minnesota as a benchmark state because it failed to inform interested parties of the state it might use as a benchmark.

62. Article 12.8 is an obligation on investigating authorities to inform interested parties prior to a final determination “of the essential facts under consideration which form the basis for the decision whether to apply definitive measures.” An oblique reference by petitioners in a countervailing duty petition that any of the 50 states could serve as a benchmark does not satisfy an investigating authority’s obligation under Article 12.8.³⁰ In the same vein, an alternative argument in a reply brief

²⁶ Second Oral Statement of the United States, at para. 40.

²⁷ Case Brief of the Government of Saskatchewan, at pps. 14-25 (22 February 2002) (Exhibit CDA-172).

²⁸ *Ibid.*, at p. 19.

²⁹ See *Issues and Decision Memorandum: Final Results of the Countervailing Duty Investigation of Certain Softwood Lumber Products from Canada*, 21 March 2001, at pps. 113 and 138-139. See also US First Written Submission, 22 January 2003, at paras. 164 and 168.

³⁰ Canada’s Second Written Submission, at para. 87.

made by one interested party in respect of a state that was not used as a benchmark does not serve as notice of the essential fact of the benchmark under consideration for the purpose of Article 12.8.

ANNEX B-2

UNITED STATES RESPONSE TO QUESTIONS FROM THE PANEL AT THE SECOND MEETING

(4 April 2003)

Q1. Could the parties please comment on the relevance, if any, of footnote 36 to Article 10 in the context of Canada's pass-through claim, in particular Canada's assertion that the Agreement requires that the calculation of the subsidization rate of the investigated product must be accurate.

Reply

1. As the United States has previously noted¹, Article 10 of the *WTO Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") provides a general obligation to impose countervailing duties in conformity with the obligations in the SCM Agreement. The general definition of a countervailing duty in footnote 36 to Article 10 does not alter that general obligation. By defining the term "countervailing duty" as "a special duty levied for the purpose of offsetting any subsidy", footnote 36 to Article 10 complements Article 19.4 of the SCM Agreement, which, as the United States has previously noted², establishes the subsidy found to exist as an upper limit on the amount of the countervailing duty that may be levied.

2. The definition of a countervailing duty in footnote 36 does not, however, impose any obligations regarding how the existence of a subsidy is to be determined. Furthermore, the general definition of "countervailing duty" cannot override the more specific provision of Article 19.3 of the SCM Agreement, which permits the imposition of countervailing duties on non-investigated exporters of the subject merchandise. As the United States has explained throughout this proceeding³, subjecting uninvestigated companies to countervailing duties does not constitute an impermissible presumption that those companies received a subsidy benefit. Article 19.3 permits Members to apply countervailing duties to exports from companies that were not individually investigated, and Members routinely do so. Moreover, Article 19.3 clearly contemplates that Members may apply countervailing duties to such companies even though they may not have received any subsidy benefit or may have received a subsidy benefit significantly lower than the rate applied.⁴

¹ See First Written Submission of the United States, fn. 213 (22 January 2003) ("US First Written Submission").

² *Id.* at para. 96, fn. 213; Answers of the United States to the Panel's Questions, para. 30 (24 February 2003) ("US First Response to Panel Questions"); Second Written Submission of the United States, para. 56 (6 March 2003) ("US Second Written Submission"); Oral Statement of the United States at the Second Meeting of the Panel, para. 34 (25 March 2003).

³ See US First Written Submission, at para. 109; Oral Statement of the United States at the First Meeting of the Panel, para. 33 (11 February 2003) ("US First Oral Statement").

⁴ As discussed in our previous submissions, Article 19.3 simply obligates Members to provide expedited reviews for such companies to calculate individual subsidy rates, and these reviews are currently underway in this case. See, e.g., US First Oral Statement, at para. 34.

3. In its preliminary response to this question at the second substantive meeting of the Panel, Canada referenced the panel and Appellate Body reports in *United States – Lead and Bismuth*.⁵ The underlying measures at issue in those reports, however, were the final results of administrative reviews conducted with respect to particular companies, and the issue under consideration was whether those particular companies had received subsidies. The focus on whether the particular companies involved received subsidies is inapposite here because the measure at issue in this case is the final determination in an investigation and, as discussed above, Article 19.3 of the SCM Agreement clearly contemplates the imposition of countervailing duties on non-investigated exporters. Thus, the reports that Canada cited are not relevant to this dispute.

Q2. Is it relevant to the interpretation of Article 14(d), in particular its reference to “in the country of provision”, that Articles 14(b) and 14(c) contain no similar reference?

Reply

4. All of the guidelines in Article 14 of the SCM Agreement address the determination of whether a benefit has been conferred, i.e., whether the recipient is better off with the government’s financial contribution than it would otherwise have been absent the financial contribution. The guidance in each subparagraph is tailored to the type of financial contribution at issue.

5. Articles 14(b) and (c) provide that the benefit from a government loan or loan guaranty must be determined by comparison to a “comparable commercial” loan that “the firm could actually obtain on the market” or the amount that the firm would pay on a “comparable commercial” loan absent the government guarantee. In conducting the analysis, neither Article 14(b) or (c) requires any examination of financial markets in the country under investigation, or any adjustments, before using lending rates from sources outside the country under investigation.

6.. Article 14(d), like the other provisions of Article 14, must answer the basic inquiry of whether the recipient is better off than it would otherwise have been absent the government’s financial contribution. In accordance with the findings of the Appellate Body⁶, the point of comparison under Article 14(d) is, as always, the “market”. Thus, the point of comparison must be a market-determined price undistorted by the government’s financial contribution. Article 14(d) requires that adequate remuneration be determined “in relation to prevailing market conditions . . . in the country of provision”. In light of that language, the most probative evidence of adequate remuneration is actual market-determined prices in the country of provision. That language is not, however, a directive to use price data solely from sources in the country of provision in all cases. Where there are no reliable “market” prices in the country of provision, price data from sources outside the country of provision may form the basis for the adequate remuneration analysis. In such cases, however, adjustments must be made, as necessary, to relate the analysis to conditions of sale “in the country of provision.”

Q3. Why, in the US view, are US stumpage prices broadly representative of market conditions in Canada? What is the motivation or incentive for Canadian harvesters to cut timber in the US, at much higher cost than in Canada, especially in the light of the abundant (in the US view, unlimited) supply of Crown timber? Would such purchases be typical, or instead essentially exceptional?

⁵ See Appellate Body Report, *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, WT/DS138/AB/R, adopted 7 June 2000; Report of the Panel, *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, WT/DS138/R, adopted 7 June 2000.

⁶ See Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, para. 157.

7. As the United States has noted previously⁷, when the market, rather than the government, sets timber prices, it does so based on the value of the downstream product, lumber. The North American lumber market is highly integrated. Thus, timber values in both Canada and the United States are driven by the same demand for lumber, and, in fact, 60 per cent of all Canadian lumber is exported to the United States. Canada does not enjoy a comparative advantage. As discussed in our prior submissions,⁸ the timber supply in the United States is comparable to Canadian timber, and the United States used species-specific benchmarks to account for any differences in species mix. The US timber prices are therefore broadly representative of the fair market value of timber in Canada. While there are some differences in conditions of sale, those differences were accounted for in the benchmark calculation.⁹

8. Furthermore, it is undisputed that Canadian mills can and do purchase US timber.¹⁰ Given the wide availability in Canada of Crown timber at below-market rates, these purchases are relatively infrequent, especially outside of Quebec, but they do occur for a number of reasons, such as local availability or related-party transactions.¹¹ While the supply of Crown timber in Canada is not “unlimited,” the availability of additional supply in each province affects the marginal price that Canadian mills will pay for timber from other sources, and thus the volume of Canadian purchases of US timber is doubtless much less than it would be, but for the Canadian subsidies. At the same time, the fact that some transactions occur demonstrates that US timber prices are in fact commercially available to Canadian mills.

Q4.. In paragraph 40 of its second oral statement, Canada argues that “the fundamental basis for Commerce’s rejection of in-country evidence was its reliance on the Preamble to its Regulations to presume price suppression”. According to the parties, does the Preamble provide for such a presumption in case of dominant position by the government? According to the parties, did the USDOC interpret the Preamble to imply a presumption against the use of market data where the government holds a dominant position in the market? (See for example p. 37 CDA-1 or p. 58: “The preamble to section 351.511 of the Regulations provides that, where a government has a dominant position in a market, the Department will avoid the use of private prices in determining the adequacy of remuneration. Where the market for a particular good is so dominated by the presence of the government, the remaining private prices in the country in question cannot be considered to be independent of the government price”).

Reply

9. Under the US regulations, the preferred benchmark for determining adequate remuneration is actual market-determined prices in the country under investigation. The Preamble states that, where such prices exist, the US Department of Commerce normally will not account for government distortion of the market. Thus, the presumption is that government involvement in the market does *not* affect the use of in-country prices. The Preamble does recognize, however, that government distortion of the market may be significant where the government has a majority share of the market.

⁷ See US First Written Submission, at para. 79.

⁸ *Id.* at paras. 77-84 and fn. 106.

⁹ *Id.* at paras. 77-84 and fn. 59; US Second Written Submission, at paras. 46-50; US First Response to Panel Questions, at paras. 11-13.

¹⁰ See US First Written Submission, at para. 80, fn. 104.

¹¹ Quebec’s forestry consultants report that much of the Maine timber harvested by Quebec lumber producers is taken from Maine timberlands owned directly by Canadian companies. See Del Degan, Massé et Associés Inc., *The Private Forest Standing Timber Market in Québec*, 91 (July 2001), appended to Response of the Government of Quebec to the Department’s 25 June 2001 Questionnaire, volume 3, Exhibit QC-S-100 (3 August 2001) (Exhibit CDA-29).

Rejection of actual in-country prices is limited, however, to cases “where it is reasonable to conclude that actual transaction prices are significantly distorted as a result of the government’s involvement in the market . . .”¹² Thus, the Preamble does not “presume” price suppression on the basis of the government’s market share. The United States’ application of its regulations in this case was consistent with that policy.

10. The specific statements from the *Final Determination* referenced in the Panel’s question should not be viewed out of context. First, the statements were intended to paraphrase the Preamble itself, which, as noted above, does not establish a presumption that in-country prices are distorted whenever the government has a majority share of the market. Second, it is evident from the *Final Determination* that the United States did not, in fact, simply presume that private prices in Canada were distorted as a result of the provincial governments’ 90 percent market share. The provinces’ dominant market share was sufficient to raise the potential for significant distortion of private prices. Consistent with the Preamble, however, the United States relied on record evidence that established that the private prices in Canada were distorted by the government’s dominant role in the market. That evidence was discussed in the *Final Determination*, in the general benefit section and in the province-specific sections.¹³ Had the United States employed a presumption of distortion, such evidence would have been irrelevant.

Q5. The US argues that any overstatement of the subsidy amount due to arms’ length transactions for logs between timber harvesters and lumber producers is now being addressed through individual expedited reviews being conducted by the USDOC. Could the US please explain how, if at all, such individual reviews affect the overall aggregate subsidization calculation. That is, does the aggregate subsidization rate remain the same, or is it recalculated to exclude the relevant amounts from the numerator, the denominator, or both, of subsidy amounts attributed to, and sales by, the individual firms subject to expedited review?

Reply

11. This is an issue actively under consideration by the United States in the ongoing expedited reviews. The reviews are being conducted, and this issue will be addressed, consistent with the United States’ obligations under the SCM Agreement.

Q6. Could the US respond to the statistics referred to in paragraph 57 of Canada’s oral statement, i.e., that the US recognizes that in British Columbia, 24 per cent of Crown timber was harvested by entities that do not own sawmills, and that scores of producers purchased their log and lumber inputs in arms’-length transactions from independent harvesters and other entities.

¹² *Issues and Decision Memorandum: Final Results of the Countervailing Duty Investigation of Certain Softwood Lumber Products from Canada*, 59 (21 March 2002) (“*Issues and Decision Memorandum*”) (Exhibit CDA-1), quoting *Countervailing Duties, Final Rule*, 63 Fed. Reg. 65348, 65377 (25 November 1998) (“Preamble”).

¹³ *Id.* at 36-38, 58-59, 95-98. See also US First Written Submission, at paras. 68-72; US Second Written Submission, at paras. 33-45.

Reply

12. First, Canada's statistical reference to the percentage of British Columbia ("B.C.") Crown timber "harvested by entities that do not own sawmills" is misleading. Obviously, entities in B.C. that do not own sawmills (e.g., pulp mills) harvest Crown timber. The subsidy was calculated, however, based solely on the volume of softwood timber that actually entered sawmills. Thus, the portion of the harvest that did *not* enter sawmills is irrelevant. The vast majority of the timber entering sawmills came from the mill's own tenure.

13. Moreover, the statistics referred to in paragraph 57 of Canada's oral statement at the second substantive meeting of the Panel are inconsistent with the record evidence provided by B.C. itself. As the United States explained in its second written submission, 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.¹⁴ In addition, another 4.6 per cent of the harvest is allocated under section 21 of the Small Business Forest Enterprise Programme ("SBFEP"), which imposes requirements that have effects similar to explicit mill ownership requirements.

14. The remaining B.C. Crown timber is provided under licenses that are normally reserved (with some case-by-case exceptions) to entities not owning timber processing facilities. These include SBFEP Section 20 licences (7 per cent of the softwood timber harvest) and woodlot licenses (2 per cent of the softwood timber harvest). However, there are a number of legal restrictions (e.g., local processing requirements) that call into question whether any transactions for the timber covered by these tenures could be considered to be at "arm's-length". Moreover, as B.C. stated: "For the most part, loggers operate as employees or contractors for holders of private lands or Crown tenures".¹⁵

15. Finally, as noted above, tenure holders are required to process the timber they harvest, or an equivalent volume, in their own mills. Thus, many of the alleged arm's-length sales are, in fact, simply log trades or swaps among tenure holders. Thus, Canada's claims referenced in the Panel's question are not supported by the record.

Q7. Could the US respond to the argument in paragraph 61 of Canada's statement that the US positions in respect of pass-through and specificity are internally inconsistent.

Reply

16. Canada prefaces its erroneous assertion of an inconsistency on the flawed premise that what is at issue is a "subsidy on standing timber".¹⁶ The subsidy at issue, however, is a subsidy to lumber producers, including remanufacturers. Specifically, the subsidy is the provision of provincial timber for less than adequate remuneration.

¹⁴ See US Second Written Submission, at fn 48, citing Response of the Government of British Columbia to the Department of Commerce's 1 May 2001 Questionnaire, vol. 9, Exhibits BC-S-59 at section 1.02, BC-S-62 at section 15.01, BC-S-63 at section 14.01 (28 June 2001) ("B.C. 28 June Questionnaire Response") (Exhibit US-76). See also US First Written Submission, at fn. 137, citing *United States – Lumber Preliminary Determination with Respect to Certain Softwood Lumber from Canada*, Answers of the United States of America to the Panel's 26 April 2002 Questions, paras. 2-3 (8 May 2002) ("US Response to US – Lumber Preliminary Determination Panel's Questions") (Exhibit US-37).

¹⁵ See US Response to US – Lumber Preliminary Determination Panel's Questions, at para. 3 (Exhibit US-37), quoting B.C. 28 June Questionnaire Response, at vol. 15, BC-LER-45.

¹⁶ Oral Statement of Canada at the Second Substantive Meeting of the Panel, para. 60 (25 March 2003).

17. Remanufacturers use provincial tenures and were included in the United States' specificity determination. As stated in the *Final Determination*:

Benefits under these Provincial stumpage [programmes] are limited to those companies and individuals specifically authorized to cut timber on Crown lands. These companies are pulp and paper mills and the saw mills and *remanufacturers* which are producing the subject merchandise. This limited group of wood product industries is specific under section 771(5A)(D)(iii)(I) of the Act.¹⁷

Article 2.1(c) of the SCM Agreement provides that a subsidy is specific if it is used by a limited number of enterprises, industries, or group of industries. The subsidy at issue is the provision of Crown timber for less than adequate remuneration. Thus, the analysis of whether the subsidy is specific is properly focused on the holders of provincial tenures.

18. The benefit calculation was not in any way inconsistent with the specificity determination. As the United States has explained previously, it conducted this investigation on an aggregate basis. The aggregate methodology is consistent with the SCM Agreement and Canada has not argued to the contrary. In an aggregate investigation, the United States determines the total amount of the subsidy provided during the period of investigation to producers of the subject merchandise (the numerator), then allocates the total subsidy across all of those producers (the denominator).

19. The subject merchandise, lumber, is produced both by primary mills ("sawmills") and secondary mills ("remanufacturers"). The numerator was therefore based on the total volume of Crown logs entering sawmills.¹⁸ Likewise, both remanufacturers and sawmills were included in the denominator of the ad valorem subsidy rate calculation, i.e., a portion of the subsidy benefit was allocated to remanufacturers. Allocation of the total subsidy to producers of the subject merchandise (sawmills and remanufacturers) does not constitute an impermissible presumption that any individual producer received a portion of the subsidy. In fact, Article 19.3 of the SCM Agreement specifically provides for the imposition of duties without determining company-specific rates in an investigation.

20. There is, therefore, no inconsistency in the United States' positions with respect to specificity and the allocation of the subsidy.

Q8. At para. 32 of the US second submission, the US states that the data on private stumpage prices in Ontario and Quebec highlight that "prices that are distorted by the government's financial contribution do not reflect 'market' conditions". Could the US please explain in what way this price information demonstrates this.

Reply

21. In paragraph 32 of its second written submission, the United States was not suggesting that the price data from Ontario and Quebec proves the distortion. Rather, the United States was noting that, in light of other evidence demonstrating that those prices are distorted by the government's financial contribution, they cannot serve to measure the subsidy benefit. The evidence that the

¹⁷ *Issues and Decision Memorandum*, at 52 (emphasis added) (Exhibit CDA-1).

¹⁸ As noted previously, the United States did not include the volume of Crown logs from tenures held by remanufacturers in the numerator due to a lack of available data. See US First Written Submission, at para. 104, fn. 134; US First Response to Panel Questions, at para. 36, fn. 47.

provincial tenure systems distort the small private sector timber sales is discussed in the *Final Determination* and in the United States' prior submissions to the Panel.¹⁹

Q9. Could the US respond to the argument at paragraph 40 of Canada's statement that the US took a selective approach to the record evidence in reaching its determination that Canadian private stumpage prices were distorted by the provincial stumpage programmes.

Reply

22. The United States considered all of the evidence presented. As we have noted previously, evidence that Canada claims the United States ignored was, in fact, considered, but found unpersuasive.²⁰ Where the parties submit evidence in support of opposing views, it is the role of the investigating authority to weigh that evidence and draw a conclusion. In that respect, an investigating authority must, in the end, select the evidence it finds persuasive and on which it will rely. Article 22.5 of the SCM Agreement requires that a final determination include "all relevant information on the matters of fact and law and reasons which have led to the imposition of final measures," including the reasons for the acceptance or rejection of relevant arguments or claims made. The United States did so in the 164 page *Final Determination*, and Canada has not claimed that the United States' determination is inconsistent with Article 22.5 of the SCM Agreement.

Q10. Could the US please elaborate on its reference to Article 14 as containing "guidelines", and not "detailed rules". Is the US suggesting that the reference to "guidelines" in the chapeau of Article 14 means that where the word "shall" appears in subparagraphs (a) through (d) of Article 14, it is less than fully binding?

Reply

23. Article 14 of the SCM Agreement expressly states that it contains "guidelines" that Members must follow in calculating a subsidy benefit. While the guidelines are binding, they are, nonetheless, guidelines rather than detailed rules. A "guideline" is a general principle to guide the development of policies and procedures.²¹ The guidelines in Article 14 are quite distinct from the types of detailed rules found elsewhere, such as in Article 2 of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* ("Antidumping Agreement"). Article 2 of the Antidumping Agreement specifies how to perform dumping calculations and the particular data that must be used for specific purposes. As discussed in our prior submissions,²² Article 14(d) of the SCM Agreement provides that the adequate remuneration analysis must relate to prevailing market conditions in the country of provision, but does not specify the methods for doing so or the types of data that may be used. Thus, where there are no market-determined benchmark prices in the country of provision, a Member may, consistent with the guideline set out in Article 14(d), rely on prices from sources outside the country of provision, provided that adjustments are made, as necessary, to relate the adequate remuneration determination to conditions of sale in the country of provision.

¹⁹ See, e.g., US First Written Submission, at paras. 68-76; US Second Written Submission, at paras. 33-44. See also *Issues and Decision Memorandum*, at 36-38, 57-59, 75-77, 95-98, 109-111, 128-129, 137 (Exhibit CDA-1).

²⁰ See Closing Statement of the United States at the First Meeting of the Panel, para. 6 (12 February 2003); US Second Written Submission, at paras. 40-43.

²¹ See *The New Shorter Oxford English Dictionary*, 1159 (1993) (defining "guideline" as "a directing or standardizing principle laid down as a guide to procedure, policy, etc.") (Exhibit US-12).

²² See, e.g., US First Written Submission, at para. 46.

24. Moreover, Canada concedes that a price that is available to purchasers in the country of provision is part of the prevailing market conditions in the country of provision.²³ As discussed below in response to question 11, US timber prices are available to lumber producers in Canada.

Q11. Could the US comment on Canada's argument at para. 28 of its second submission concerning the third benchmark in Section 351.511 of the USDOC Regulations. In particular, could the US comment, first, on Canada's argument that there are no world market prices for stumpage, and second, on Canada's position that the evidence shows that provincial stumpage programmes are operated in a manner consistent with market principles, as foreseen by the USDOC Regulations.

Reply

25. Under the US regulations, the second tier in the benchmark hierarchy states:

If there is no useable market-determined price with which to make the comparison under paragraph (a)(2)(i) . . . the Secretary will seek to measure the adequacy of remuneration by comparing the government price to a world market price where it is reasonable to conclude that such price *would be available to purchasers in the country in question*. Where there is more than one *commercially available* world market price, the Secretary will average such prices to the extent practicable, making due allowance for factors affecting comparability.²⁴

As used in the US regulation and in prior determinations, the term "world market price" simply means a price for the good or service from a source outside the country under investigation.²⁵ However, only world market prices that are commercially available to purchasers in the country under investigation fall within the ambit of the second tier of the regulation.²⁶

26. Availability is a case-by-case factual determination. As the United States has discussed in its prior submissions²⁷, the record demonstrates that prices for US timber are commercially available to lumber producers in Canada. Canada argues that US timber prices are not available to purchasers in Canada because the trees must be harvested in the United States. Under Canada's reasoning, FOB US factory prices are not available to purchasers in Canada because the purchaser must take delivery in the United States. The reality is, however, that when Canadian lumber producers need wood fibre, they can (and occasionally do) purchase US trees. They take delivery in the United States, but they transport the harvested timber to Canada and process it in Canadian mills. The prices for US timber are therefore available to purchasers in Canada.

27. Canada also argued that the US prices are not available to purchasers in Canada because of log export restrictions. However, the vast majority of timber in the United States is privately held, and none of the privately held timber is subject to export restrictions. These private timber sales are the primary driver of US stumpage fees in the timber market overall. The export restrictions that

²³ See Second Written Submission of Canada, para. 41 (6 March 2003).

²⁴ 19 C.F.R. § 351.511(a)(2)(ii) (emphasis added) (Exhibit US-14).

²⁵ The provision for averaging multiple world market prices reflects the fact that the term "world market price" is not being used narrowly, i.e., it is not restricted to commodities with a single worldwide price.

²⁶ The Preamble to the US regulations illustrates the importance of commercial availability by noting that prices for electricity in Europe are not likely to be an appropriate basis for determining the value of electricity in Latin America because the electricity "in all likelihood would not be available to consumers in Latin America." *Issues and Decision Memorandum*, at 35 (Exhibit CDA-1), citing Preamble, 63 Fed. Reg. at 65377.

²⁷ See, e.g., US First Written Submission, at para. 80.

Canada refers to are limited to public timber in Western states. As the United States explained in the *Final Determination*, however, that public timber is sold through open and competitive public auctions in which most purchasers have the choice of buying public or private stumpage. The auction prices for public timber therefore reflect market prices generally, including private timber prices commercially available to purchasers in Canada.²⁸

28. The US regulations provide that “[i]f there is no world market price available to purchasers in the country in question”, the adequacy of remuneration will normally be determined by assessing whether the government price is consistent with market principles.²⁹ Where commercially available world market prices exist, as in this case, analysis under the third tier of the US regulations is unnecessary. If the government price is less than the market benchmark price, it is, by definition, less than adequate remuneration.

29. The fact that the provincial stumpage prices are below the market benchmark price contradicts Canada’s claim that the provincial stumpage programmes are operated in a manner consistent with market principles. That benchmark comparison is all that is necessary to establish the existence of a benefit, consistent with Article 14(d). Nevertheless, as discussed in our prior submissions,³⁰ other evidence demonstrates that the provincial tenure systems are based on public policy objectives, not market principles. Moreover, the United States disagrees with Canada’s argument that evidence that British Columbia makes a profit on its timber sales is sufficient to find that government prices are based on market principles. A government price below fair market value – even a profitable one – is not based on market principles.³¹

Q12. What is the basis for the US statement in footnote 40 that the reports on the profits earned by provinces on their timber sales implicitly account for the cost to the government of trees as \$0?

Reply

30. Footnote 14 of the United States’ oral statement provides the relevant citation to B.C.’s questionnaire response, which can be found at Exhibit CDA-48. With respect to Alberta, Ontario, and Quebec, the United States directs the Panel’s attention to pages 10, 11, and 12 of Exhibit CDA-47. The “profit” calculation in Exhibit CDA-48 is the basis for Canada’s claim that B.C. prices timber in accordance with market principles. The only costs incurred by B.C. included in this calculation, however, are current administrative expenses.³² Nowhere in the calculation is there a figure for the value of the trees themselves. Thus, the calculation effectively values the trees at zero. The information set forth in Exhibit CDA-47 suffers from the same infirmity.

Q13. The US, at paras. 83-85 of its second submission, in the context of Canada’s Article 12.8 claim, emphasizes the words “essential facts under consideration”. The complete phrase from

²⁸ See *Issues and Decision Memorandum*, at 44 (Exhibit CDA-1).

²⁹ The Preamble to the regulations states that “[i]n our experience, these types of analyses may be necessary for such goods or services as electricity, land leases or water.” *Id.* at 35 (Exhibit CDA-1), citing Preamble, 63 Fed. Reg. at 65377-78. All of the cases that Canada cited with respect to US practice concerning the third tier in the regulatory hierarchy involved the provision of electricity or other types of goods or services (port facilities; railway “hopper car” services) for which there was no evidence of world market prices commercially available to purchasers in the country under investigation.

³⁰ See US First Written Submission, at paras. 69-70; US Second Written Submission, at paras. 35-38.

³¹ See also US response to Question 12, below.

³² The calculation includes current expenses for “silviculture,” “roads and bridges,” “protection,” “timber sales costs,” and “sustainable forest management.” See B.C. 28 June Questionnaire Response, at Exhibit BC-S-111 (Exhibit CDA-48). See also PricewaterhouseCoopers, *Report on Revenues and Expenditures of Certain Canadian Provinces Relating to Stumpage Operations*, 10-12 (25 June 2001) (Exhibit CDA-47).

Article 12.8, however, is “essential facts under consideration *which form the basis for the decision* whether to apply definitive measures”. The US implies in its arguments that Canada’s interpretation of Article 12.8 would require, essentially, disclosure of the entire final results before the final determination was actually made. Under the facts of this case, could the USDOC simply have informed the parties, before issuing its final determination, that it was considering changing the comparison state to Minnesota, and allowing the parties a brief period to comment? Does the US consider that such a disclosure would be equivalent to issuing the entire final determination in advance? Please comment, and explain any reasons why such an approach would not have been possible, if this is the US view.

Reply

31. The parties challenged the decision to use Montana in their case briefs, which were submitted one month before the *Final Determination* was issued. We have no basis on which to determine when, in response to those comments, the United States first considered changing to Minnesota. Thus, we cannot speculate on whether there would have been sufficient time to request, receive, and analyze additional comments.³³

32. Moreover, it is the view of the United States that Article 12.8 did not require additional opportunity for comment. The very purpose of notice and comment is to afford parties the opportunity, as they had in this case, to persuade the investigating authority to take specific positions. There may be many issues on which an investigating authority considers changing its mind in response to comments from the parties, but ultimately does not do so; in other instances the investigating authority may change its mind. Nothing in Article 12.8 of the SCM Agreement requires an ongoing notification of that deliberative process. Furthermore, Article 12.8 does not preclude an investigating authority from altering a final decision in response to parties’ comments without affording further opportunity to comment. Reading such an obligation into Article 12.8 would undermine the very purpose of notice and comment. The investigating authority could effectively be precluded from altering a decision in response to comments in many instances because of the obligation to complete what is often a very complex investigation within a specified period.

33. Article 12.8 simply requires that a certain result be achieved, i.e., that interested parties be informed of the essential facts under consideration which form the basis of the decision whether to apply definitive measures in time to defend their interests. Article 12.8 does not require any specific procedure for achieving the required result. To determine whether that result has been achieved in a particular case, it is necessary to view the process as a whole.

34. Because Article 12.8 addresses events “before a final determination is made,” it cannot be read as requiring pre-notification of the final determination. In this case, where the parties had ample opportunity to defend their interests, Canada’s position is equivalent to a requirement to issue a pre-notification of the final decision with respect to the benchmark state (and, by logical extension, pre-notification of the final decision with respect to all issues for which the final decision differed in any respect from the preliminary determination).

35. It is evident from the record of the investigation that the parties had ample notice and opportunity to defend their interests. First, the record establishes that the parties knew that the United States was considering a US state as the basis for the market benchmark and knew the United States’

³³ This was a very complex investigation and the *Final Determination* required the United States to weigh the evidence and make decisions on a substantial range of issues. Thus, if the United States initially focused on other issues or other provinces, it is possible that specifically identifying Minnesota as being under consideration, in time for parties to submit additional comments on the benchmark determination, would have been precluded as a practical matter.

preliminary choice of benchmark state. The parties also knew that the benchmark state would be selected from evidence on the record and that the record only contained evidence on Washington, Idaho, Montana, North Dakota, Minnesota, Michigan, New York, Vermont, New Hampshire, Maine, and Alaska.³⁴

36. Second, the parties knew the criteria that the United States would use to select the benchmark state, which included species mix, climate, and topography.³⁵ Saskatchewan obviously did not believe that the potential pool of states was limited by contiguity, given that Saskatchewan itself proposed Alaska, a non-contiguous state, as an alternative.

37. Third, the parties were aware of all of the data on each state under consideration, including those not selected in the preliminary determination. And finally, the parties were aware of the arguments presented by all other parties concerning the appropriate comparison state.

38. The parties received all of this information in sufficient time to defend their interests, as evidenced by their case and rebuttal briefs. It is therefore evident that the only thing the interested parties did not know in this case was the United States' final decision *after* considering the essential facts and the comments of the parties.

Q14. Could the US respond to the argument at paragraph 82 of Canada's oral statement, that new evidence from the petitioners' 4 March 2002 submission was in fact used by the USDOC in its subsidy calculations for Quebec.

Reply

39. Canada's argument at paragraph 82 of its oral statement relates to footnote 151 of the United States' second written submission. That footnote states, in its entirety:

Moreover, the 4 March 2002 letter primarily commented on the MFPC Letter and provided an analysis of information that Quebec had placed on the record on January 4, 2002. Although the United States *considered petitioners' March 4 rebuttal comments, it did not rely on the information provided*. The United States instead relied on a publication by the US Department of Agriculture, which was already on the record. *See Issues and Decision Memorandum*, at 62 (Exhibit CDA-1).³⁶

As demonstrated below, this statement is accurate with respect to the issue of the use of studwood in Maine for lumber production.

40. In its December 20, 2001 letter, the Maine Forest Products Council ("MFPC") contended that it was inappropriate for the United States to use only sawlog prices to calculate stumpage prices from Maine.³⁷ The MFPC proposed a weighted average stumpage price, including prices for pulpwood and studwood in the calculation.³⁸ The MFPC proposed that studwood account for approximately 74 per cent of the weighted-average stumpage price.³⁹ The petitioners responded to this proposal on

³⁴ See US First Response to Panel Questions, at para. 52; US Second Written Submission, at para. 88.

³⁵ See US First Response to Panel Questions, at para. 52; US Second Written Submission, at para. 88.

³⁶ US Second Written Submission, at para. 91, fn. 151 (emphasis added).

³⁷ See Letter from MFPC to Deputy Assistant Secretary Bernard Carreau, 1 (20 December 2001) ("MFPC Letter") (Exhibit CDA-100).

³⁸ *Id.* at 2.

³⁹ *Id.* at 5.

4 March 2002, submitting a report by Lloyd C. Irland, which contended that the proportion of studwood in the Maine harvest is substantially lower than that alleged by the MFPC.⁴⁰

41. Thus, the main issue addressed by the MPFC Letter and the petitioners' 4 March 2002 submission was the percentage of the timber used in lumber production in Maine that was studwood. As explained in its *Issues and Decision Memorandum*, the United States made independent enquiries of the Maine Forest Service ("MFS") to identify the names of the four softwood studmills operating in Maine and analyzed their production from a US Department of Agriculture report previously placed on the record to arrive at studwood ratio of 25.36 per cent.⁴¹

42. As the United States acknowledged in its responses to the Panel's first set of questions⁴², the petitioners' 4 March 2002 submission also included species-specific studwood stumpage prices that had not been placed on the record previously. The petitioners obtained these prices, however, from a public source, the MFS Stumpage Reports, which is the same source that the United States used in its preliminary determination in this case. Indeed, Quebec had access to this source and submitted aggregate studwood stumpage prices from the MFS in its January 4, 2002 submission.⁴³ The 4 March 2002 submission represented the only record source for species-specific studwood stumpage prices for Maine, and, in order to make the calculation as accurate as possible, the United States used these prices from the 4 March 2002 submission in its calculations of the market-based benchmarks for Quebec. The United States also used species-specific information from the March 4, 2002 submission pertaining to the total volume of sawlogs harvested in each county of Maine.

Q15. Could the US please respond to the argument in para. 67 of Canada's second submission, in which Canada seems to imply that the US argues that the SCM Agreement contains no obligation to *correctly* calculate the rate of subsidization. Is this the US argument? Alternatively, is the US arguing that there is such an obligation, but that it simply is not found in SCM Article 19.4? If the latter is the US position, in which specific provision(s) of the SCM Agreement does the US consider that this obligation is found?

Reply

43. It is the position of the United States that, although there are obligations in the SCM Agreement concerning the calculation of the subsidy, there are no such obligations in Article 19.4 of the SCM Agreement. Article 19.4 simply provides that the duty may not exceed the subsidy found to exist. This was confirmed by the Appellate Body, which recently stated that Article 19.4 "set[s] out the obligation of Members to limit countervailing duties to the amount . . . of the subsidy found to exist by the investigating authority."⁴⁴

44. Article 19.4 does not establish the methodological obligations that Canada alleges. For example, there is no obligation in Article 19.4 to allocate the subsidy on a volume, as opposed to value, basis, and there is no basis in Article 19.4 to read into the SCM Agreement a host of undefined obligations with respect to the calculation of the rate of subsidization. What constitutes a "correct" calculation can only be determined by reference to the explicit obligations in the Agreement.

⁴⁰ See Lloyd C. Irland, *Estimates of Maine Spruce-Fir Log Production by Grade, 2000* (March 2002), Attachment 2 to Letter from Dewey Ballantine to Secretary of Commerce Donald Evans (4 March 2002) (Exhibit CDA-112).

⁴¹ See *Issues and Decision Memorandum*, at 61 (Exhibit CDA-1).

⁴² See US First Response to Panel Questions, at para. 56, fn. 72.

⁴³ *Id.* at para. 56, fn. 71.

⁴⁴ Appellate Body Report, *United States – Countervailing Measures Concerning Certain Products from the European Communities*, WT/DS212/AB/R, para. 139, adopted 8 January 2003.

45. Various provisions of the SCM Agreement are relevant to Members' obligations to calculate the ad valorem subsidy rate. Article 14, for example, establishes obligations concerning the calculation of the amount of the benefit. Annexes II and III provide guidelines on when indirect tax rebate, duty deferral, and duty drawback programmes can provide a benefit and thereby constitute an export subsidy. Annex IV provided specific rules for the calculation of the ad valorem subsidy rate with respect to the determination of whether serious prejudice existed as defined by the now lapsed Article 6.1(a) of the SCM Agreement.

46. In addition to these obligations, the calculation of the ad valorem subsidy rate must have evidentiary support and a reasoned basis. Article 22.5 obligates Members to provide public notice of all relevant information of matters of fact and law and the reasons that led to the imposition of final measures.

47. Moreover, many of the alleged "obligations" that Canada contends are established by Article 19.4 are in reality questions of fact. For example, Canada's claims regarding the conversion factor and the exclusion of residual products from the denominator are in fact challenges to the United States' findings of fact. The Panel, however, is not charged with *de novo* review. As demonstrated in the *Final Determination*, the United States considered all of the relevant facts and provided a reasoned explanation for its conclusions.

Q16. Could the US please respond to the argument in para. 81 of Canada's second submission that the US excluded from the denominator "other softwood products that were also produced in the sawmill establishments from logs entering those sawmills"?

48. The United States has acknowledged that some of the products in the "residual products" category would have been included in the denominator had Canada provided the information necessary to determine the value of those products.⁴⁵ Canada, however, failed to do so. Canada merely provided a single number representing all shipments of products in the residual products category and a list of those products.⁴⁶ Canada did not provide any break-out of the residual product category that would have allowed the United States to include those products that resulted from the lumber manufacturing process. The residual products category clearly included products not produced by sawmills, such as spruce logs and other wood in the rough.

Q20. Canada argues, at para. 74 of its second submission, that the numerator in a subsidization calculation must reflect the proportional amount of the subsidy that can be attributed to the subject merchandise. In other words, Canada's argument seems to be that there must be a volume-based allocation of subsidy amounts among a firm's different products, before the rate of subsidization of the subject merchandise can be calculated.

- (a) **Is this a correct characterization of Canada's argument on this point? If not, please clarify.**
- (b) **If this is a correct characterization of Canada's argument, how does Canada reconcile this with the fact that the *de minimis* rule for countervailing duties is expressed on an *ad valorem* basis in the SCM Agreement (e.g., Article 11.9)?**
- (c) **Similarly, how does Canada reconcile this position with the fact that the Annex IV guidelines for calculation of *ad valorem* subsidization of a product, in the context of (now expired) Article 6.1(a) specifically require that this rate of subsidization be calculated using the total value of the firm's sales as the denominator of the subsidization equation, except in the case of a tied subsidy, in which case the denominator is the value of the firm's sales to which that subsidy is tied? (In other words, the general approach was**

⁴⁵ See US Second Written Submission, at para. 63.

⁴⁶ See US First Response to Panel Questions, at para. 38.

that the total subsidy amount would be divided by the firm's total sales to arrive at the *ad valorem* subsidization of the product.) In what way, analytically, is this different from what the USDOC did in the Lumber investigation?

Reply

49. At the Panel's second substantive meeting, Canada preliminarily agreed that the chapeau to these questions was a correct characterization of its argument. Thus, Canada's claim is that to calculate the subsidy to lumber, the United States was required to allocate the total subsidy benefit based on volume rather than value. Article 19.4 of the SCM Agreement, however, does not contain an obligation to allocate a subsidy on the basis of volume rather than value. "The most logical conclusion to be drawn from this silence is that the choice . . . is up to the investigating authority".⁴⁷

50. Whatever additional calculation steps Canada may propose to convert the subsidy amount to an *ad valorem* rate are irrelevant. Canada's methodology still presumes an obligation in the first instance to allocate the subsidy benefit based on volume, and no such obligation exists in the SCM Agreement.

⁴⁷ Panel Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India*, WT/DS141/RW, circulated 29 November 2002, para. 6.87 (finding that because nothing in the text of Article 2.2.2(ii) of the Antidumping Agreement specified whether averages should be weighted by volume or value, the choice is up to the investigating authority); *see also id.* at para. 6.82, quoting Appellate Body Report, *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products*, WT/DS50/AB/R, adopted 16 January 1998, para. 45.