



Trade Law Memo.

Subsidies and Softwood Lumber: Are There Settlement Prospects in 2003?

Indications are that a solution to the Canada-U.S. softwood lumber war in 2003 could be as elusive as ever. Federal-provincial differences, the absence of unanimity and cohesion among Canadian stakeholders and the intractability of American producers, are significant roadblocks, even if the Canadian and U.S. governments would like to get this issue behind them.

Critical Points.

Whatever happens, the softwood lumber case provides important lessons. First, it illustrates the obvious dangers of over-exposure to — indeed, outright dependence on — a single market and the harm that can be inflicted when private trade law remedies are used to restrict access to that market.

Second, it illustrates the limitations of current anti-dumping and countervailing duty laws in settling these kinds of disputes. It also shows the difficulties of imposing State-negotiated settlements in a system that is primarily geared to protect private interests, as opposed to protecting markets.

Third, it highlights the central role of the WTO in international trade disputes and the fact that any negotiated settlement will be directly influenced by what WTO panels decide.

The WTO Challenge.

The Canadian government claimed success in its first WTO challenge of the United States countervailing duty determination. That was based on the panel's conclusion last September that the U.S. had erroneously calculated the amount of subsidy by using U.S. market prices as the benchmark for measuring the extent of the subsidy benefit under provincial stumpage programs. The panel held that under the Subsidies Agreement, the U.S. was required to use Canadian open market prices as the benchmark.

The "Subsidies" Issue.

On the main point in the case, however, the WTO panel upheld the American position. The panel rejected Canada's argument that stumpage programs were not "subsidies" as defined in the Subsidies Agreement.

Based on this finding, American softwood producers hardened their stand. Their public comments throughout last fall were to the effect that the WTO had vindicated their position, that Canadian stumpage was contrary to international rules and legally countervailable and that, as a consequence, there was no justification for backing down.

The U.S. Responds.

The U.S. government's official response to these developments came in early January, with a discussion paper on a settlement framework. The paper is thoughtful and detailed, but makes no bones about insisting that the provinces move to a what the U.S. considers to be a market-based system.

Bolstered by the WTO ruling, the U.S. argues that current provincial measures are market-distorting, confer long-term benefits on tenure holders that insulate them from the market and, as a result, ensure the continued over-production of lumber in Canada regardless of market forces. This allows low-cost Canadian lumber exports to injure U.S. producers.

What is required to settle the dispute, the paper says, is a wholesale change to these provincial programs. The ultimate test, it says, will be "whether a province's modified stumpage system will produce results consistent with those the province could expect from the sale of all of its standing timber at open auction". Ideally, this should be through auctioning off 100% or close to 100% of Crown timber and trashing the current stumpage systems of administered rents.

Oversight of Canadian Changes.

The U.S. paper goes further however, in terms of the process it envisages as part of a settlement package. It sets out proposals that are unprecedented in scope and would effectively make the U.S. government the final authority over Canadian forestry management measures and practices.

To remove the current duties, the paper provides that the Commerce Dept. will have to approve any changes to provincial stumpage programs that adopt free market principles. This approval would be within the framework of existing U.S. trade law. The present countervailing duties would stay in place but a province that modified or eliminated its stumpage program could apply for a “changed circumstances” review. Then, Commerce would conduct a review but only if the evidence showed “significant structural changes” in an individual province’s stumpage measures.

Such a review would be through detailed, ongoing audits and a full examination of every aspect of the new pricing mechanisms, as determined by the Commerce Department. Under U.S. trade law, U.S. petitioners will have access to all data and the right to challenge each and every submission filed by the Canadian side.

Where Do We Go From Here?

It is difficult to know if any progress could be made on the basis of these proposals. The B.C. Minister of Forests has made some positive sounds but voices from Québec appear dead-set against such draconian provisions for U.S. oversight.

Even assuming a kind of auction or free-market pricing system could be accepted by the provinces, it seems doubtful that the Canadian side would accept a one-sided “changed circumstance” review by the Commerce Dept. A more productive route would be to “bilateralize” the settlement and enshrine the ingredients in a separately crafted Canada-U.S. agreement. Instead of trying to shoehorn this into the review framework under U.S. law, such an agreement would allow for periodic review by the two governments and for a means of resolving disputes where there is cogent evidence that the Canadian provinces are not materially complying with the agreement’s terms.

The duties would then be reduced in accordance with the degree of movement to an open market system in the individual provinces. If changes did not reflect bilaterally agreed free market prices, the duties would be applied but only to the extent of any shortfall.

In summary, a possible resolution would be to remove this from the context of U.S. law and elevate it to the level of a bilateral agreement, with reasonable provisions for compliance monitoring — on a joint basis — and with a mechanism for resolving claims of material non-compliance.

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