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## **TRADE LAW MEMORANDUM**

### **THE SOFTWOOD LUMBER CASE ROLLS ON**

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#### **LATEST WTO DECISION MAY HELP CANADIAN NEGOTIATORS – MAYBE**

As reported in the media this week, the latest WTO panel said the U.S. was wrong in calculating the amount of countervailing duties that could be charged on Canadian softwood.

Will this help the Canadian side? The answer is a qualified “yes”, in that every legal victory can add some marginal weight to Canada’s negotiating position.

But the panel also said that the U.S. could re-do its calculations by using the right benchmarks, leaving the door open to a revision of U.S. duties. It is therefore hard to agree with the claim that Canada achieved full victory at the WTO.

Along with others, we believe that the legal case is less critical than the negotiating table, when the real and lasting solution in this bitter dispute will be found. As we said before, however, a negotiated deal will almost certainly leave the U.S. government and the U.S. industry in the driver’s seat.

**WHAT IS A “SUBSIDY”?**

This latest WTO panel decision remains confidential under WTO rules. However, it appears to be the same as an earlier WTO ruling last fall. The Panel confirmed that two vital ingredients are needed for a subsidy to be found and for countervailing duties to be imposed. First, there has to be a governmental contribution (in cash or kind) to a specific industry. Second, even with that contribution, there has to be a benefit conferred on that industry.

If, for the sake of argument, a government provided goods or services to industry, but at market rates, the first branch of the definition would be met but not the second branch, because no benefit was conferred. Hence, no subsidy and no right to apply countervailing duties.

The WTO ruling accepts the U.S. argument that stumpage programs are indeed financial contributions by provincial governments to the softwood industry. That was the conclusion of the earlier WTO panel. It means the first branch of the test has been satisfied.

But the Panel then said that the U.S. Commerce Department applied the wrong method in determining the amount of benefit, thereby failing the second test. The problem was that Commerce valued Canadian stumpage on the basis of “cross-border benchmarks”, comparing provincial stumpage rates with the price of timber sold in the open market in the United States.

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The Panel ruled that under the WTO *Subsidies Agreement*, the benefit, and hence the amount of duties, must be determined in relation to the market conditions in the country under investigation, that is, on the basis of open market sales of standing timber in Canada.

The disapproval of the Commerce Department's use of U.S. benchmarks is an important victory for Canada. But it has that key qualification. The U.S. has the option of recalculating the amount of subsidy on the basis of Canadian market prices.

#### **WHERE DO WE GO FROM HERE?**

We are far from the end. But recent press reports are that a deal is slowly being cobbled together, based on a Canadian export tax (to replace U.S. duties) and a quota system to cap the level of Canadian exports.

If details can be resolved, the result will be a system of long-term managed trade – not free trade – that will almost certainly give the U.S. government final say in deciding if and when reforms of provincial stumpage programs are sufficient to allow the proposed export tax to be removed.

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