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UNITED STATES – FINAL COUNTERVAILING DUTY DETERMINATION WITH RESPECT TO CERTAIN SOFTWOOD LUMBER FROM CANADA

Recourse by Canada to Article 21.5
(DS257)

Report of the Panel

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Dominican Republic – Import and Sale of Cigarettes	Panel Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/R, 26 November 2004, adopted 19 May 2005.
EC – Bed Linen (Article 21.5 – India)	Appellate Body Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW, adopted 24 April 2003 Panel Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/RW, adopted 24 April 2003, as modified by the Appellate Body Report, WT/DS141/AB/RW
US – Line Pipe	Appellate Body Report, *United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea*, WT/DS202/AB/R, adopted 8 March 2002
US – Shrimp (Article 21.5 – Malaysia)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481
US – Softwood Lumber III	Panel Report, *United States – Preliminary Determinations with Respect to Certain Softwood Lumber from Canada*, WT/DS236/R, adopted 1 November 2002

Short Title	Full Case Title and Citation of Case
US – Softwood Lumber IV	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004 Panel Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/R and Corr.1, adopted 17 February 2004, as modified by the Appellate Body Report, WT/DS257/AB/R

I. PROCEDURAL BACKGROUND

1.1 On 17 February 2004, the Dispute Settlement Body ("DSB") adopted the recommendations and rulings in the reports of the original panel and the Appellate Body in *US – Softwood Lumber IV*.

1.2 In respect of pass-through, the original panel concluded that:

> "the USDOC's[1] failure to conduct a pass-through analysis in respect of upstream transactions for log and lumber inputs between unrelated entities was inconsistent with Article 10 SCM Agreement and Article VI:3 of GATT 1994."[2]

1.3 More specifically, the original panel found that:

> "the USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to unrelated sawmills producing subject softwood lumber; and in respect of lumber sold by tenure-holding harvester/sawmills to unrelated lumber re-manufacturers was inconsistent with Article 10 and thus Article 32.1 SCM Agreement, and with Article VI:3 of GATT 1994."[3]

1.4 The original panel therefore upheld Canada's claim that the United States' imposition of countervailing duties in respect of such transactions was inconsistent with Articles 10 and 32.1 SCM Agreement and Article VI:3 of GATT 1994.[4]

1.5 The United States appealed from the original panel's pass-through conclusion. The Appellate Body stated that the United States "contend[ed] that the [original panel] erred in finding that a pass-through analysis is required in respect of sales of *logs* from tenure-holding sawmills producing softwood lumber to unrelated sawmills, and for sales of lumber by tenure-holding sawmills to unrelated lumber remanufacturers."[5] According to the Appellate Body, the United States "[did] not appeal the [original panel's] finding that, where a subsidy is received by an independent timber harvester[6], a pass-through analysis is required in respect of sales to unrelated sawmills or unrelated remanufacturers".[7]

1.6 In respect of pass-through, the Appellate Body stated that it upheld the original panel's finding that:

> "USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *logs* by tenured harvesters/sawmills to unrelated sawmills is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994."[8]

1.7 The Appellate Body stated that it reversed the original panel's finding that:

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[1] We shall continue the original panel's practice of referring to the US Department of Commerce as "USDOC".

[2] Panel Report, *US – Softwood Lumber* IV (hereinafter "Panel Report"), para. 8.1(c).

[3] Panel Report, para. 7.99.

[4] Panel Report, para. 8.1(c).

[5] Appellate Body Report, *US – Softwood Lumber* IV, (hereinafter "Appellate Body Report"), para. 16, emphasis in original.

[6] Before the Appellate Body, the United States used the term "independent harvester" in the same way as it had in the original dispute, namely, "'entities that do *not* produce [softwood lumber] product[s] under investigation'". Appellate Body Report at para. 127. In the Section 129 Determination, the USDOC used the term "independent harvester" to refer to "tenured independent harvesters/sawmills" (see note 52 *infra*).

[7] Appellate Body Report, para. 16, footnote omitted.

[8] Appellate Body report, para. 167 (e), emphasis in original.

> "USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *lumber* by tenured harvesters/sawmills to unrelated remanufacturers is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994."[9]

1.8 At the DSB meeting of 17 December 2004, the United States informed the DSB that it had complied with the DSB's recommendations and rulings.

1.9 On 30 December 2004, Canada requested the establishment of a panel pursuant to Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU").[10] At the same time, Canada also requested authorization from the DSB to suspend the application to the United States of certain concessions or other obligations, pursuant to DSU Article 22.2.

1.10 At its meeting of 14 January 2005, the DSB decided, in accordance with DSU Article 21.5, to refer to the original panel the matter raised by Canada in document WT/DS257/15. At that meeting, it also was agreed that the Panel should have standard terms of reference as follows:

> "To examine, in the light of the relevant provisions of the covered agreements cited by Canada in document WT/DS257/15, the matter referred to the DSB by Canada in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements".[11]

1.11 The Panel was composed as follows:

Chairman: Mr Elbio O. Rosselli

Members: Ms Marta Calmon Lemme
Mr Remo Moretta

1.12 On 14 January 2005, the DSB also referred the matter of suspension of concessions to the Panel for arbitration pursuant to DSU Article 22.6.[12]

1.13 China and the European Communities reserved their rights to participate in the Panel proceedings as third parties.

1.14 The Panel met with the parties and third parties on 21 April 2005.

1.15 The Panel submitted its interim report to the parties on 20 May 2005. The Panel submitted its final report to the parties on 3 June 2005.

II. FACTUAL ASPECTS

2.1 With a view to implementing the rulings and recommendations of the DSB in respect of this dispute, on 19 November 2004, the United States issued a draft determination pursuant to Section 129 of the *Uruguay Round Agreements Act*. The United States issued its final Section 129 Determination on 6 December 2004 (the "Section 129 Determination").

2.2 On 20 December 2004, the United States published the final results of the first assessment review of the countervailing duties on imports of softwood lumber from Canada (the "First

[9] Appellate Body Report, para. 167 (f), emphasis in original.
[10] WT/DS257/15.
[11] WT/DS257/19.
[12] WT/DS257/20.

Assessment Review"). Pursuant to the US retrospective system of duty assessment, the First Assessment Review provided for retrospective final assessment of the countervailing duties to be levied on import entries of softwood lumber from Canada between 22 May 2002 and 31 March 2003. The First Assessment Review also determined the cash deposit rate to be levied on imports of softwood lumber from Canada as of 20 December 2004. The First Assessment Review was initiated in July 2003, pursuant to a request in May 2003 from Canada and other interested parties.

2.3 The arguments of the parties and third parties as presented to the Panel are contained in their written and oral submissions, the texts of which are appended to this report.

III. INTERIM REVIEW

3.1 The Panel issued its interim report to the parties on 20 May 2005. On 24 May 2005, both parties submitted written requests to the Panel to review precise aspects of the interim report but neither party requested an interim review meeting. On 26 May 2005, both parties commented in writing on the other party's requests for review of the interim report. This section summarizes the parties' requests and comments, and contains the Panel's responses thereto, and forms part of the Panel's findings.

A. REQUEST BY CANADA FOR REVIEW OF PRECISE ASPECTS OF THE PANEL REPORT

1. Request of Canada

3.2 Canada asks the Panel to introduce changes into paragraphs 4.71-4.73, 4.82, 4.83, 4.88, and 4.89.

3.3 Canada asks the Panel to make findings, in paragraph 4.73, concerning the USDOC's exclusion of certain transaction-specific data on log sales (submitted by Tembec (Manitoba)). Canada notes that although the USDOC excluded these data from pass-through analysis for reasons other than not being at arm's length[13], these reasons were "equally inconsistent" with the United States' obligations pursuant to the DSB's recommendations and rulings. Canada asserts that the parties would "benefit" from findings by the Panel on the Tembec (Manitoba) data.

3.4 Canada also asks the Panel to expand the description of Canada's arguments in paragraph 4.83, concerning the USDOC's treatment of aggregate data submitted by Canadian respondents. The suggested amendments would expand on the description of Canada's arguments that the sample data submitted by Canadian respondents were representative, that it was impossible for respondents to provide the full data requested by the USDOC, or more data than they did provide, and that USDOC was obliged to use the data provided by the respondents as the basis of the pass-through analysis.

3.5 Concerning paragraph 4.88, Canada takes issue with the Panel's statement that Canada "has not disputed that the USDOC needed" company-specific and/or transaction-specific data for the purpose of determining affiliation of parties to the log sales transactions, which according to Canada is inaccurate in the light of the totality of Canada's arguments, as reflected in Canada's suggested redraft of paragraph 4.83. Canada also asks the Panel to insert a statement that the USDOC accepted that aggregate data could, and did, control for affiliation.

3.6 In paragraph 4.89, Canada asks the Panel to insert a statement that "investigating authorities nevertheless have an obligation to perform analyses, on the basis of available data, in a manner that is consistent with the obligation under Article VI:3 of GATT 1994 and Articles 10 and 32.1 of the SCM

[13] According to both parties, USDOC did not conduct a pass-through analysis in respect of these log sales because the sales were made after the end of the period of investigation.

Agreement not to presume that the subsidy passed through to an unrelated purchaser of the input product".

3.7 Canada states that the Panel finds in paragraphs 4.71-4.73, and 4.82 that the USDOC was required to conduct a pass-through analysis irrespective of any considerations as to whether or not sales were at "arm's length". Canada requests that the Panel insert a statement in this context that "even if the U.S. arguments on 'arm's length' were accepted, the five 'factors' identified by USDOC in this case, including who pays the stumpage and the presence of non-cash components to a transaction, do not transform an arm's-length transaction into one that is not at arm's length".

2. Comments of the United States

3.8 The United States submits that the Panel should reject all of the amendments proposed by Canada. Concerning paragraph 4.73, the United States argues that the issue concerning Tembec (Manitoba) raised by Canada in its request for interim review is outside the Panel's terms of reference, as Canada's claim on pass-through was concerned with the appropriateness of USDOC's arm's length analysis. The United States further argues that in any case, as acknowledged by Canada, Tembec (Manitoba) submitted no data to the USDOC concerning log sales during the period of investigation.

3.9 The United States objects to Canada's request to expand the description of Canada's arguments in paragraph 4.83, stating that the original summary is sufficient, and that if Canada's request were accepted, without an equivalent expansion of the description of the US arguments, this would create an appearance of imbalance. Furthermore, given that the submissions of the parties are appended to the report, the United States considers a full recitation of detailed arguments unnecessary.

3.10 Concerning paragraph 4.88, the United States disagrees as a factual matter that Canada disputed the USDOC's need for company-specific and/or transaction-specific for purposes of determining affiliation. The United States asserts that Canada is confusing the question of whether the USDOC needed certain data with whether the USDOC should have accepted whatever data Canada offered.

3.11 The United States also disagrees with Canada's suggested amendment to paragraph 4.89, stating that the suggestion is inappropriate, and would directly contradict the Panel's immediately preceding statement that the Panel is reluctant to instruct investigating authorities concerning data issues in pass-through analysis.

3.12 Finally, the United States takes issue with Canada's suggested amendment to paragraphs 4.71-4.73 and 4.82 to "clarify" certain points in respect of the USDOC's arm's length factors. According to the United States, given that the Panel found that the USDOC should have conducted a pass-through analysis regardless of the issue of arm's length, Canada's suggestion is irrelevant and would call on the Panel to make substantial new findings that would then need to be subjected to additional interim review.

B. REQUEST BY THE UNITED STATES FOR REVIEW OF PRECISE ASPECTS OF THE PANEL REPORT

1. Request of the United States

3.13 The United States requests the Panel to make certain technical drafting corrections and clarifications to paragraphs 2.2, 4.20, 4.21, and 4.48, and to footnote 45 of the interim report (footnote 47 of the final report). The United States also requests substantive changes to paragraphs 4.38, 4.41, 4.47, 4.48 and 4.49.

3.14 First, the United States requests that in paragraphs 4.38, 4.41 and 4.49, we change the references to "dispute settlement decisions" to "dispute settlement reports", to avoid potential

confusion with "decisions" that might be made, for example, pursuant to Article IX of the Marrakesh Agreement.

3.15 Second, the United States asserts that at paragraph 4.47, the Panel mischaracterizes the United States' argument concerning the *EC – Bed Linen (Article 21.5)* dispute. The United States indicates that its argument on that point is correctly summarized at paragraph 4.45.

3.16 Third, the United States contends that paragraph 4.48 is factually incorrect in stating that the Final Determination and the First Assessment Review involve "'pass-through of the subsidy benefit, in respect of **the same import entries** . . . . '"

2. Comments of Canada

3.17 Canada only comments on the last of the United States' comments, concerning the factual accuracy of the reference to "the same import entries" in paragraph 4.48. According to Canada, this statement is factually accurate, and the issue is correctly described at paragraph 4.41, the accuracy of which the United States does not contest.

C. EVALUATION BY THE PANEL

1. Request of Canada

3.18 Concerning Canada's request in respect of paragraph 4.73, we have not made any findings in respect of the issue concerning Tembec (Manitoba)'s sales of logs. We consider that this issue falls outside our terms of reference, as set by the request for establishment of the Panel, as it does not correspond to any of the legal claims set forth in the first four "tirets" on page two of the request (WT/DS257/15).

3.19 In response to Canada's requests concerning the summary of its arguments in paragraph 4.83, we have slightly modified the text of that paragraph, and have inserted footnote 65.

3.20 Concerning paragraph 4.88, we do not consider that Canada has disputed the USDOC's need for company-specific and/or transaction-specific data to determine affiliation of parties to log transactions. We have introduced footnote 66 to clarify our understanding of the nature of, and the USDOC's use of, the aggregate data that the USDOC accepted for purposes of determining affiliation.

3.21 We have not introduced in paragraph 4.89 the statement requested by Canada, but have introduced a final sentence to that paragraph, as well as footnote 67, to clarify our view in respect of the issues raised by Canada's comment.

3.22 We have not introduced in paragraphs 4.71-4.73 and 4.82 the statement requested by Canada concerning certain of the arm's length factors applied by the USDOC. Such a statement would be inappropriate in view of our findings that pass-through analysis should have been conducted in respect of log sales between unrelated parties, irrespective of any considerations as to whether or not such sales were "arm's length".

2. Request of the United States

3.23 We have accepted the United States' suggested changes to paragraphs 2.2, 4.20, 4.21, and 4.48, and to footnote 45 of the interim report (footnote 47 of the final report). We also have made other technical corrections to the report, as necessary.

3.24 We have not accepted the United States' suggestion in respect of paragraphs 4.38, 4.41 and 4.49, because we believe that it is clear from the context that the word "decisions" refers to the

findings cited in that section of the report, and is not used in a generic sense that could potentially sweep in other kinds of actions.

3.25 In the light of the US comments, we have amended paragraph 4.47 slightly, to refer to what we see as the implication of the US argument, rather than to refer to the US argument as such.

3.26 We have added footnote 44, to clarify to which import entries the phrase in paragraph 4.48 "the same import entries" refers. Footnote 44 contains a cross-reference to paragraph 4.41, cited by Canada in its comments on the US suggestion concerning this paragraph.

IV. FINDINGS

4.1 This case concerns Canada's claim that the USDOC failed to properly implement the rulings and recommendations of the DSB in respect of the *US – Softwood Lumber IV* proceeding. In particular, Canada claims that, in the Section 129 Determination and First Assessment Review, the USDOC continued to presume pass-through of subsidy benefit in respect of various categories of sales of logs to unrelated purchasers. Before examining Canada's claims, we shall first rule on a preliminary ruling requested by the United States.

A. US REQUEST FOR PRELIMINARY RULING

1. Arguments of the parties

4.2 The United States requests a preliminary ruling that the final results of the First Assessment Review of the countervailing duty order on softwood lumber from Canada are not "measures taken to comply" with the recommendations and rulings of the DSB under Article 21.5 of the DSU. According to the United States, these results fall outside the scope of Article 21.5, and this Panel lacks jurisdiction to review them.

4.3 The United States submits that the First Assessment Review was a proceeding: separate from both the original countervailing duty investigation determination challenged by Canada and the Section 129 Determination at issue here; initiated prior to the DSB's adoption of recommendations and rulings in this dispute; that had nothing to do with complying with the recommendations and rulings of the DSB.

4.4 The United States notes that the *EC – Bed Linen (Article 21.5 – India)* panel granted the European Communities' preliminary ruling request to exclude from consideration certain antidumping duty measures taken by the European Communities that were cited by India, but that the panel found were not "taken to comply." The United States asserts that, in that dispute, in which the European Communities was found to have incorrectly calculated anti-dumping duties in an investigation of bed linens from India, the European Communities voluntarily applied the revised calculation method to anti-dumping duties imposed on Pakistan and Egypt. The United States asserts that, after concluding that no duties should be imposed on bed linen from those sources (as a result of the recalculation), the European Communities re-examined whether imports from India, considered alone, caused injury to the domestic industry. According to the United States, the European Communities concluded that they did, and therefore affirmed the imposition of anti-dumping duties on bed linen from India. The United States asserts that India challenged this finding of injury and the resulting imposition of duties on bed linen from India as a WTO-inconsistent measure "taken to comply" under Article 21.5.

4.5 The United States notes that the panel, in deciding not to review the latter measure, stated that

> "[T]he fact that the EC, subsequent to its re-examination of the dumping determinations with respect to imports from Egypt and Pakistan, and in the context of a review initiated on the request of Eurocoton, carried out an analysis of whether

> injury was caused by imports from India alone does not, *ipso facto*, establish that Regulation 696/2002 is a measure "taken to comply". Rather the opposite would seem to be the case – that Regulation would seem to be an entirely new determination, reached as a result of events subsequent to the EC having adopted a measure to comply with the DSB's recommendation."[14]

4.6 The United States submits that the final results of the First Assessment Review are not "measures taken to comply". The United States asserts that, before the original panel, Canada challenged the USDOC's Final Determination in the countervailing duty investigation on softwood lumber from Canada.[15] After the DSB adopted its recommendations and rulings, and within the agreed "reasonable period of time", the United States made the Section 129 Determination, in which it conducted a "pass through" analysis and recalculated the countervailing duty rate.[16] The new reduced rate was applicable to entries of subject merchandise on or after 10 December 2004. The United States submits that original investigations and assessment reviews are different processes which serve distinct purposes. The purpose of an investigation is to determine the existence, degree, and effect of any alleged subsidy; the purpose of an assessment review is to determine the amount of duty to be assessed on previous imports of subject merchandise and the estimated countervailing duty rate to be applied to future imports. The United States argues that the distinction between countervailing duty investigations and assessment procedures is explicitly recognized in the Agreement on Subsidies and Countervailing Measures ("SCM Agreement").[17]

4.7 The United States submits that the First Assessment Review was not a measure taken to comply with the recommendations and rulings of the DSB. Rather, it resulted from a separate affirmative request by Canada, among others, that USDOC review new sales and subsidies data for the purposes of assessing countervailing duties for imports during the review period and of setting a new estimated countervailing duty rate for subsequent imports.

4.8 The United States also argues that the First Assessment Review was initiated on 1 July 2003, eight months before the DSB's recommendations and rulings in this dispute were adopted. The United States asserts that the First Assessment Review, therefore, had nothing whatsoever to do with "implementing" the DSB's recommendations and rulings. The United States submits that, for obvious temporal reasons, the results of this assessment review – which was initiated before the DSB issued its recommendations and rulings – cannot be considered "measures taken to comply". By contrast, the United States asserts that the USDOC initiated the Section 129 proceeding for the specific purpose of addressing the DSB's recommendations and rulings. The United States further asserts that the agreement of the parties on the "reasonable period of time" to implement the recommendations and rulings in this dispute was negotiated in the light of, and specifically refers to, the US procedures for implementing WTO reports[18] – that is, the Section 129 procedures.

4.9 The United States submits that Article 21.5 proceedings are by their nature more focused and limited than other panel proceedings under Article 6.2 of the DSU. The United States argues that it is beyond the scope of such a limited 90-day inquiry to fully examine an entirely new set of assessment review results based on a wholly new administrative record, consisting of new sales, new imports, potentially new respondents and potentially new subsidy programmes.

4.10 Canada submits that the final results of the First Assessment Review rendered non-existent the pass-through analysis and adjustment under the Section 129 Determination, and that the final results of the First Assessment Review are therefore an integral part of the Panel's determination "as

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[14] *EC – Bed Linen (Article 21.5 – India)* (Panel), para. 6.20.
[15] Panel Report, paras 2.1 - 2.4.
[16] Section 129 Determination. Exhibit CDA-5.
[17] The US refers in this regard to SCM Agreement, fn. 52.
[18] WT/DS257/13.

to the *existence* … of measures taken to comply" under Article 21.5 of the DSU. Canada also argues that upholding the US preliminary objection would be contrary to the purpose of Article 21.5 proceedings.

4.11 Regarding the Section 129 Determination being rendered non-existent by the First Assessment Review, Canada argues that in *Australia – Leather II (Article 21.5 - US)*, the United States itself argued that measures that undo measures taken to comply appropriately fall within the scope of Article 21.5 of the DSU:

> Under Article 21.5, this panel is to consider "the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings." Plainly, if this Panel can determine the "existence" of measures taken to comply with the recommendations, it can consider whether the measures purportedly taken to comply were effectively rendered non-existent.

4.12 Furthermore, Canada asserts that, in declining to include certain EC measures in its compliance review, the abovementioned *EC – Bed Linen (Article 21.5 - India)* panel specifically noted that India "does not argue that the subsequent two measures undo the compliance effectuated by the first measure."[19]

4.13 Canada also submits that the final results of the First Assessment Review are properly before the Panel because they are inextricably linked to the recommendations and rulings of the DSB and to what the United States claims as being its "measures taken to comply". Canada asserts that the treatment by USDOC of the pass-through issue in the final results of its First Assessment Review is nearly identical to its treatment of pass-through in the Section 129 Determination. Canada also notes that USDOC published preliminary results for the First Assessment Review containing a "pass-through" section nearly four months after the DSB made its recommendations and rulings, and issued final results nearly ten months after those recommendations and rulings. Canada asserts that the Section 129 Determination and the First Assessment Review are inextricably linked to the DSB recommendations because they both address the obligations of the United States to conduct pass-through analyses with respect to independent harvester and sawmill-to-sawmill log transactions for the same exports for the same period of time.

4.14 Regarding the US argument that assessment reviews and original investigations are different proceedings, and that the review was initiated prior to the recommendations and rulings of the DSB, Canada submits that the United States ignores the fact that, under US law, the USDOC may implement the recommendations and rulings of the DSB concerning an original investigation through a subsequent administrative review.[20]

4.15 Canada asserts that Article 21.5 of the DSU requires a compliance panel to examine the substance of a Member's measures notwithstanding any argument that the form of the measures could preclude compliance review. Canada notes that in *Australia – Automotive Leather II (Article 21.5 -*

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[19] *EC – Bed Linen (Article 21.5)*, Panel Report, at para. 6.21. Canada also refers to the Third Party Submission of the European Communities (Annex C-3), at para. 26, citing *Dominican Republic – Import and Sale of Cigarettes*, at paras. 7.11-7.21.

[20] Canada refers in this regard to the "Statement of Administrative Action" in *Message from the President of the United States Transmitting the Uruguay Round Agreements, Texts of Agreements Implementing Bill, Statement of Administrative Action and Required Supporting Statements*, H.R. Doc. No. 103-316, vol. 1 at 656 (Exhibit CDA-1), at 356-357. ("Furthermore, while subsection 129(b) [of the Uruguay Round Agreements Act] creates a mechanism for making new determinations in response to a WTO report, new determinations may not be necessary in all situations. In many instances, such as those in which a WTO report merely implicates the size of a dumping margin or countervailable subsidy rate (as opposed to whether a determination is affirmative or negative), it may be possible to implement the WTO report recommendations in a future administrative review under section 751 of the Tariff Act.")

US), for example, the panel found that the subsequent loan was within its jurisdiction to examine under Article 21.5 of the DSU because it was "inextricably linked to the steps taken by Australia in response to the DSB's ruling in this dispute, in view of both its timing and its nature."[21] Canada also notes the finding of the panel in *Australia – Salmon (Article 21.5 - Canada)* that:

> … an Article 21.5 panel cannot leave it to the full discretion of the implementing Member to decide whether or not a measure is one "taken to comply". If one were to allow that, an implementing Member could simply avoid any scrutiny of certain measures by a compliance panel, *even where such measures would be so clearly connected to the panel and Appellate Body reports concerned, both in time and in respect of the subject-matter, that any impartial observer would consider them to be measures "taken to comply"*.[22]

4.16 Canada submits that the US reliance on *EC – Bed Linen (Article 21.5 - India)* is misplaced, as the panel in that dispute found that the EC measures in question were not "taken to comply" within the meaning of Article 21.5 of the DSU because they did not deal with the subject matter upon which the DSB had made recommendations and rulings. Canada submits that the panel expressly noted that "[t]he situation might be different had there been a claim in the original dispute challenging the cumulative assessment of the effects of imports from India, Egypt, and Pakistan."[23]

4.17 Canada asserts that the US argument that an Article 21.5 panel does not have jurisdiction to evaluate USDOC's treatment of additional record evidence concerning exports subject to a US definitive countervailing duty misses the point entirely, as a panel's assessment "as to the existence or consistency with a covered agreement of measures taken to comply" under Article 21.5 of the DSU necessarily involves an examination of new factual information. Canada notes in this regard that the Appellate Body stated in *EC – Bed Linen (Article 21.5 - India)* that:

> [A]n Article 21.5 panel is not confined to examining the "measures taken to comply" from the perspective of the claims, arguments, and factual circumstances relating to the measure that was the subject of the *original* proceedings. Moreover, the relevant facts bearing upon the "measure taken to comply" may be different from the facts relevant to the measure at issue in the original proceedings. It is to be expected, therefore, that the claims, arguments, and factual circumstances relating to the "measure taken to comply" will not, necessarily, be the same as those relating to the measure in the original dispute. Indeed, a complainant in Article 21.5 proceedings may well raise *new* claims, arguments, and factual circumstances different from those raised in the original proceedings, because a "measure taken to comply" may be *inconsistent* with WTO obligations in ways different from the original measure.[24]

4.18 Canada also submits that the US request for a preliminary ruling runs contrary to the very purpose of an Article 21.5 panel in its review of the imposition of countervailing measures, since the US obligation to demonstrate whether, and to what extent, alleged subsidies to log production pass through arm's length log purchases before imposing duties on softwood lumber products would remain in dispute for each annual assessment review under Article 21 of the SCM Agreement during the potential five-year life (or longer) of the US definitive countervailing measure. Canada asserts that such a result would leave the DSB in the absurd situation of having made numerous identical

[21] Panel Report, *Australia – Automotive Leather II (Article 21.5 – US)*, para. 6.5.

[22] *Australia – Salmon (Article 21.5 - Canada)*, at para. 7.10(22) [emphasis added]. Canada also refers to *EC – Bed Linen (Article 21.5)*, Panel Report, at para. 6.17.

[23] *EC – Bed Linen (Article 21.5)*, Panel Report, at para. 6.18, fn. 36.

[24] *EC – Bed Linen (Article 21.5)*, Appellate Body Report, at para. 79 [emphasis in original]. Canada also refers to the EC Third Party Submission (Exhibit C-3), at para. 28, referring in addition to the Appellate Body's report in *US – Shrimp (Article 21.5 – Malaysia)*, at para. 86.

recommendations and rulings concerning a definitive countervailing duty for which compliance may never be secured. In this regard, Canada notes that the United States argued in *Australia – Salmon (Article 21.5 - Canada)* that:

> [W]e also wish to express the agreement of the United States with the broad and inclusive approach the Panel has taken thus far in defining the scope of this proceeding. The Panel's approach is the only one consistent with the purpose of the WTO dispute settlement system as reflected in Articles 3 and 21 of the Dispute Settlement Understanding: the prompt settlement of disputes. Disputes could not be settled "promptly" if a defending party were permitted to thwart a thorough review of its WTO compliance by staging the introduction of details of new measures over a period of time, and then arguing that they must escape WTO scrutiny for a further period of time.[25]

4.19 The United States denies that the results of the First Assessment Review rendered the Section 129 Determination non-existent. The United States submits that the Section 129 Determination, in implementing the recommendations and rulings of the DSB with respect to the final investigation determination, confirmed that the resulting imposition of countervailing duties on May 22, 2002, was consistent with the SCM Agreement. According to the United States, the very fact that Canada is, itself, challenging the Section 129 Determination shows that Canada believes that it is of ongoing effect and relevant to the issue of compliance.

4.20 The United States asserts that the present case is not a situation like that presented in *Australia – Automotive Leather II (Article 21.5 - US)*, in which a WTO-inconsistent subsidy was both withdrawn and "regranted" in another form on the same day, in "inextricably linked elements of a single transaction."[26] The United States asserts that first, in *Australia – Leather II (Article 21.5 - US)*, the United States was arguing that the panel should review whether a prohibited subsidy had actually been withdrawn, as specifically required by Article 4.7 of the SCM Agreement, when the repayment of a grant had been contingent on the simultaneous grant of a loan on non-commercial terms. The United States submits that, in contrast, this proceeding involves the question of whether a measure has been brought into conformity with a WTO agreement.

4.21 The United States submits that second, the *Australia – Leather II (Article 21.5 - US)* panel concluded that the subsidy had not been withdrawn at all, because the supposed repayment and the non-commercial loan were, in effect, a single transaction in which the subsidy simply shifted form. The United States asserts that, in this dispute, the Section 129 Determination and the First Assessment Review results are separate and independent actions. The United States asserts that the Section 129 Determination was made to bring the measure in dispute into conformity with the SCM Agreement as recommended by the DSB, whereas the First Assessment Review was conducted for a completely unrelated reason. According to the United States, therefore, the First Assessment Review in no way affects that result of the Section 129 Determination.

4.22 The United States also submits that the results of the First Assessment Review are not inextricably linked, either to the Section 129 Determination, or to the recommendations and rulings of the DSB. The United States notes Canada's reliance on *Australia – Leather II (Article 21.5 - US)*, and that panel's finding that the relevant subsidy had not been withdrawn, because the supposed repayment and the non-commercial loan were "inextricably linked elements of a single transaction."[27] The United States asserts that that situation is very different from this one. In particular, the United States notes that the Section 129 Determination and the First Assessment Review results were not in

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[25] *Australia – Salmon (Article 21.5 - Canada)*, Third Participant Submission of the United States, 9 December 1999, at para. 5. (Exhibit CDA-54)

[26] Panel Report, *Australia Leather II (Article 21.5 - US)*, para. 6.50.

[27] *Australia –Leather II (Article 21.5 - US)*, para. 6.50.

any sense contingent on one another, nor were they in any sense part of a single transaction. The United States submits that the First Assessment Review would have taken place regardless of whether there was a Section 129 proceeding under way, and, indeed, regardless of whether there even was a WTO dispute.

4.23 The United States notes that Canada also relies on *Australia – Salmon (Article 21.5 - Canada)*. The United States asserts that the imposition of a ban by Tasmania, one of Australia's sub-federal units, was obviously a response to the modification of the ban. The United States asserts that the Tasmanian ban did not arise from a proceeding initiated as a matter of domestic law requirements, irrespective of any WTO challenge, but was rather an *ad hoc* action taken after the DSB had made recommendations and rulings against an Australian import ban and after Australia had taken action to modify the ban. By contrast, the United States asserts that the assessment review was initiated:

- upon request of the parties (including Canada), eight months before the DSB's recommendations and rulings were even adopted;
- pursuant to a US statutory provision that requires initiation upon request on a specific schedule and under specific deadlines; and
- for the purpose of assessing countervailing duties on entries not previously examined – not for the purpose of implementing any recommendations or rulings.

4.24 Regarding Canada's argument that the facts of *EC – Bed Linen (Article 21.5 - India)* should be distinguished from the present case, the United States submits that the *EC – Bed Linen (Article 21.5 - India)* dispute demonstrates that a new determination that was made in a subsequent segment of an antidumping or countervailing duty proceeding – and not made to implement recommendations and rulings of the DSB – falls outside the jurisdiction of Article 21.5 panels.

4.25 The United States further submits that properly applying DSU Article 21.5 does not "ignore the purpose of compliance proceedings". The United States asserts that, contrary to Canada's arguments, a review under Article 21.5 of the Section 129 Determination permits the prompt settlement of disputes: Canada complained about an inconsistency in the final investigation determination, and this Panel will review whether that inconsistency has been corrected. The United States argues that Canada appears to suggest that the US system of retrospective duty assessments somehow compels the Panel, in the special case of the United States, to sweep the assessment review into this Article 21. 5 proceeding.[28] The United States submits, however, that there is nothing in Article 21.5 or in the SCM Agreement that requires a different interpretation of "measures taken to comply" for those Members that employ a retrospective duty assessment system, rather than a prospective one.

2. Arguments of the third parties

4.26 The European Communities considers that the US view (if accepted) would turn the US system of countervailing duty assessment into a moving target that escapes the WTO disciplines. The European Communities submits that the phrase "taken to comply" cannot be read to limit the 21.5 proceeding to those measures that were explicitly taken to replace the measure at issue in the original proceedings, but must be read together with its immediate and broader context as well as the purpose of the DSU to reach a prompt solution of a dispute. The European Communities asserts that because the phrase is preceded by the term "existence" and followed by the expression "with the recommendations and rulings of the DSB", an Article 21.5 panel is tasked to assess whether or not there is a failure to comply and whether or not the original dispute has been resolved (as opposed to assessing the conformity of a particular measure with a particular provision of the *Agreement*

[28] The United States refers in this regard to Canada's Second Written Submission, para. 27 (Annex A-2).

Establishing the World Trade Organization ("WTO Agreement"), as panels are required to do in initial proceedings).

4.27 The European Communities submits that the broader purpose of Article 21.5 of the DSU is to secure the solution of a dispute between two WTO Members relating to the measures brought before the original Panel. The European Communities asserts that this was explicitly recognised by the panel in *Australia – Salmon (Article 21.5 - Canada)*, which even considered a measure taken during the Article 21.5 proceeding since "to do otherwise would, in our view, go against the principle of prompt settlement of disputes and could hamper implementation of both DSB recommendations in the original dispute and our findings in this case."[29]

4.28 The European Communities submits that the US view is based on the assumption that the measures to be attacked in countervailing duty cases are the determinations made by the investigating authorities. The European Communities asserts that this is false, since Article 10 of the SCM Agreement clarifies that the measure of concern is the "imposition of a countervailing duty", defined as a "special duty levied" for the purpose of offsetting a subsidy. The European Communities submits that it is the duty itself that interferes with trade and is the measure of concern. The European Communities asserts that the assessment review at hand in this case is a hybrid instrument. It fixes the final duty rate for the assessment period with retrospective effect, but is not a fully-fledged review of both the subsidy and injury within the meaning of Article 21 of the SCM Agreement.[30] The European Communities notes that the assessment review does not change the date of the expiry of the measure under Article 21.3. The European Communities does not accept the US argument that footnote 52 of the SCM Agreement recognises that these types of assessment review are separate from the original determination (and / or a Section 129 determination). The European Communities also notes that the United States has not disputed Canada's characterisation of the First Assessment Review as superseding both the original countervailing duty determination and the Section 129 Determination. The European Communities asserts that, at the date of the establishment of the Panel (14 January 2005), only the First Assessment Review was effectively in place. The European Communities submits that, according to WTO jurisprudence, a measure that essentially replaces an earlier measure remains within the terms of reference of an original Panel.[31] The European Communities submits that, *a fortiori*, an Article 21.5 Panel must be in a position to assess whether an annual administrative review determination that confirms and supersedes the original determination relating to the same countervailing duty constitutes a "continuing violation".

4.29 The European Communities also rejects the US argument that *EC – Bed Linen (Article 21.5 - India)* stands for a general proposition that any review measure is outside the scope of a 21.5 proceeding. The European Communities asserts that the review measures at issue in that case were entirely different in nature. In particular, those measures were either specific reviews of antidumping duties imposed on exporters from other Members (Egypt and Pakistan) or entirely new determinations in a review based on results of an event subsequent to the European Communities having adopted the implementing measure in *EC – Bed Linen (Article 21.5 - India)*. In other words, they were dismissed because they did not relate to the original dispute between the European Communities and India.

4.30 According to the European Communities, accepting the US view that the First Assessment Review is not subject to a DSU 21.5 panel review would turn the US system of duty assessment into a moving target that escapes from countervailing duty disciplines. Each assessment review would have to be subject to a new panel request, and by the time the panel, Appellate Body and implementation procedure was completed, another assessment review would have overtaken the results of any Section

[29] Panel Report, *Australia – Salmon (Article 21.5 - Canada)*, para. 7.21.
[30] Panel Report *US – Softwood Lumber III*, para 7.151.
[31] The European Communities refers to the Panel Report in *Dominican Republic – Import and Sale of Cigarettes*, paras. 7.11-7.21

129 determination. A new panel would have to be started against this review, creating a "Groundhog Day" situation.

4.31 China asserts that, on the one hand, the First Assessment Review was made in a totally separate investigation procedure and based on the import data that is irrelevant to that of the original investigation. On the other hand, China asserts that the two determinations at issue were made under the framework of the same set of proceedings which effectively affects import of softwood lumber from Canada and the First Assessment Review supersedes the Section 129 Determination. In China's view, the first argument relates to the question of whether the First Assessment Review is a "measure[] taken to comply", while the second argument concerns the matter whether the Section 129 Determination is rendered non-existent.

4.32 Although China acknowledges that the First Assessment Review may not be properly categorized as a "measure[] taken to comply", China argues that this consideration does not lead to a decisive answer to the question of whether this measure is properly before this panel. China recalls that, on the basis of the plain language of Article 21.5, the purpose of the proceedings under this provision is to review and solve the dispute on "the *existence* or *consistency* with a covered agreement of measures taken to comply with the recommendations and rulings" of the DSB. China believes that "existence" and "consistency" are two distinct aspects of the subject measure. The latter involves review that is not only "limited to 'the issue of whether or not [a Member] has implemented the DSB recommendation'" [32], but also "in the light of any provision of any of the covered agreements."[33] On the other hand, the former relates to the status of the revised new measure. According to China, both aspects are equally important though the "existence" matter is crucial in solving the threshold issue in these proceedings.

4.33 China asserts that the dispute of *Australia – Automotive Leather II (Article 21.5 - US)* demonstrates a similar fact pattern that should be referenced by this Panel. China notes that, in that case, the Article 21.5 panel said:

> The 1999 loan is inextricably linked to the steps taken by Australia in response to the DSB's ruling in this dispute, in view of both its timing and its nature. In our view, the 1999 loan cannot be excluded from our consideration without severely limiting our ability to judge, on the basis of the United States' request, whether Australia has taken measures to comply with the DSB's ruling. In the absence of any compelling reason to do so, we decline to conclude that a measure specifically identified in the request for establishment is not within our terms of reference. [34]

4.34 In China's view, in an Article 25.1 procedure, if the complaining party submits that a "measure[] taken to comply" is invalidated by a subsequent measure, the compliance panel should at least assess this claim that relates to the "measure[] taken to comply" on the basis of relevant facts – the subsequent measure. China asserts that to exclude the second measure would put the panel at the risk of failing to make a comprehensive and well-founded judgement on the existence of a measure taken to comply with DSB recommendations and rulings. China believes that, as a result of the countervailing duty assessment system adopted by the US, the results of an assessment review may, at least in form, replace the original final determination. In particular, China notes that the results of the First Assessment Review were announced ten days after the Section 129 Determination took effect. Thus, the First Assessment Review established a new rate for cash deposit for the goods from Canada and replaced the rate in the Section 129 Determination. According to China, such changes in the applicable duty rate deserve further consideration on whether the First Assessment Review, in

[32] *Canada - Aircraft (Article 21.5)*, Appellate Body Report, para.40.
[33] *Australia - Salmon (Article 21.5 - Canada)*, para.7.10.
[34] *Australia – Automotive Leather II (Article 21.5 - US)*, para. 6.5.

substance, rendered the Section 129 Determination non-existent. China therefore submits that the facts presented by Canada in these proceedings, at least, have demonstrated that there is likelihood that the First Assessment Review may nullify the Section 129 Determination.

4.35 In summary, China is of the opinion that, although the First Assessment Review may not be a measure taken to comply, it is closely linked to and may have an important effect on the existence of the purported measure taken to comply – the Section 129 Determination. On such basis, China believes it is the mandate of this Panel to consider the First Assessment Review in these proceedings.

3. Evaluation by the Panel

4.36 The US request for a preliminary ruling concerns the scope of Article 21.5 of the DSU, which provides in relevant part:

> Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel.

4.37 In particular, the US request requires us to determine whether or not the First Assessment Review, or at least the treatment of pass-through contained therein, constitutes a "measure[] taken to comply" with the rulings and recommendations of the DSB in respect of the Final Determination.

4.38 In addressing this issue, we are guided by dispute settlement decisions regarding the scope of DSU Article 21.5. These decisions indicate that Article 21.5 proceedings are not restricted to measures formally, or explicitly, taken by Members to implement DSB rulings and recommendations. In this regard , we note that the panel in *Australia – Salmon II (Article 21.5 – Canada)* found that:

> an Article 21.5 panel cannot leave it to the full discretion of the implementing Member to decide whether or not a measure is one "taken to comply". If one were to allow that, an implementing Member could simply avoid any scrutiny of certain measures by a compliance panel, even where such measures would be so clearly connected to the panel and Appellate Body reports concerned, both in time and in respect of the subject-matter, that any impartial observer would consider them to be measures "taken to comply".[35]

4.39 That case concerned Australia's implementation of DSB rulings and recommendations regarding import restrictions on untreated fresh, chilled or frozen salmon from Canada. Australia stated that it implemented the DSB's rulings and recommendations through a series of import risk analyses that entered into force on 19 July 1999. On 20 October 1999, during the course of the Article 21.5 proceedings concerning the measures adopted by Australia in July 1999, the Government of Tasmania adopted measures restricting all imports of salmonids. The panel employed the following terms in finding that the October 1999 measure fell within the terms of its DSU Article 21.5 review:

> "Without attempting to give a precise definition of "measures taken to comply" that should apply in <u>all</u> cases, we are of the view that in the context of this dispute at least any quarantine measure introduced by Australia subsequent to the adoption on 6 November 1998 of DSB recommendations and rulings in the original dispute – and within a more or less limited period of time thereafter -- that applies to imports of fresh chilled or frozen salmon from Canada, is a "measure taken to comply". The Tasmanian ban, introduced on 20 October 1999, imposes an import prohibition on all

[35] *Australia – Salmon (Article 21.5 – Canada)*, page 106.

> imports of salmonids into part of Australia on quarantine grounds. We thus find that it is a measure taken to comply in the sense of Article 21.5."[36]

4.40 The scope of DSU Article 21.5 proceedings was also addressed by the panel in *Australia – Leather II (Article 21.5 - US)*. That case concerned Australia's implementation of DSB's rulings and recommendations regarding the withdrawal of a prohibited export subsidy. In September 1999, the subsidy recipient repaid the prospective element of the subsidy. Simultaneously, the Government of Australia provided a loan to the original subsidy recipient. In finding that both the repayment of the original subsidy, and the new loan, fell within the scope of its DSU Article 21.5 review, the panel stated:

> The 1999 loan is inextricably linked to the steps taken by Australia in response to the DSB's ruling in this dispute, in view of both its timing and its nature. In our view, the 1999 loan cannot be excluded from our consideration without severely limiting our ability to judge, on the basis of the United States' request, whether Australia has taken measures to comply with the DSB's ruling. In the absence of any compelling reason to do so, we decline to conclude that a measure specifically identified in the request for establishment is not within our terms of reference.[37]

4.41 The parties agree that the Section 129 Determination falls within the scope of these DSU Article 21.5 proceedings. In our view, and taking into account previous dispute settlement decisions regarding DSU Article 21.5, the USDOC's treatment of pass-through in the First Assessment Review is also covered by these proceedings, because it is clearly connected to the panel and Appellate Body reports concerning the Final Determination, and because it is inextricably linked to the treatment of pass-through in the Section 129 Determination. In particular, we note that certain import entries subject to the prospective effect of the Final Determination are also subject to the retrospective effect of the First Assessment Review. Thus, while the First Assessment Review resulted in an assessment rate for import entries during the period 22 May 2002 – 31 March 2003, those entries had initially been subject to the cash deposit rate determined in the Final Determination.[38] Furthermore, the prospective effect of the Section 129 Determination was superseded by the prospective effect of the First Assessment Review, in the sense that import entries that would have been subject to the cash deposit rate fixed by the Section 129 Determination became subject to the cash deposit rate fixed by the First Assessment Review, once the latter took effect. Thus, even though the period of investigation of the Final Determination and Section 129 Determination may differ from the period of review of the First Assessment Review, and even though the latter was initiated before the DSB adopted any rulings or recommendations regarding this matter, there is in fact considerable overlap in the effect of these various measures. Since the pass-through analysis in the First Assessment Review could, therefore, have an impact on, and possibly undermine, any implementation of the DSB rulings and recommendations regarding pass-through by the Section 129 Determination, we consider that the pass-through analysis in the First Assessment Review should also fall within the scope of these DSU Article 21.5 proceedings.[39]

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[36] *Australia – Salmon (Article 21.5 – Canada)*, page 106 (footnote deleted).

[37] *Australia – Leather II (Article 21.5 - US)*, para. 6.5.

[38] Import entries subject to the Section 129 Determination cash deposit would be assessed pursuant to a subsequent assessment review, if requested. We do not attach importance to the fact that import entries subject to the Section 129 Determination cash deposit were not formally subject to the First Assessment Review, since the Section 129 Determination amended and replaced the Final Determination, such that there is no need to distinguish between the coverage of these two measures for present purposes.

[39] We do not here mean to imply that, on the basis of our interpretation and analysis of the scope of DSU Article 21.5, other elements of the First Assessment Review, dealing with issues unrelated to the scope of the DSB's adopted recommendations and rulings in the original dispute between the parties, could be treated as part of a "measure[] taken to comply" and thereby challenged through an Article 21.5 proceeding.

4.42 The United States argues that the findings of the *Australia – Leather II (Article 21.5 - US)* panel should be distinguished, because the Section 129 Determination and First Assessment Review were not contingent on one another. We acknowledge that the First Assessment Review was not contingent on the Section 129 Determination, and note that the First Assessment Review might very well have been initiated even if the Section 129 Determination had not been undertaken. However, the degree of contingency between the relevant measures was clearly not the sole, or determining factor, in the reasoning of the *Australia – Leather II (Article 21.5 - US)* panel regarding the inclusion of the loan in the DSU Article 21.5 proceeding.[40] That panel was concerned more generally with the "timing and nature" of the subsequent loan. As noted above, we consider that there is sufficient overlap in the timing, or temporal effect, and nature of the Final Determination, Section 129 Determination and First Assessment Review for the latter to fall within the scope of the present DSU Article 21.5 proceedings.

4.43 The United States also argues that the findings of the panel in *Australia – Salmon (Article 21.5 - Canada)* should be distinguished because that case concerned an *ad hoc* action taken after the DSB adopted its rulings and recommendations, whereas the First Assessment Review was initiated pursuant to domestic law requirements, eight months before, and independent of any consideration of, the rulings and recommendations of the DSB in *US – Softwood Lumber IV*. We note, however, that the *Australia – Salmon (Article 21.5 - Canada)* panel made no reference to the *ad hoc* nature of the Tasmanian import ban in its findings. Accordingly, since the *ad hoc* nature of that import ban did not influence that panel's findings, this is no basis on which to distinguish those findings from the present case. In any event, we consider that the *Australia – Salmon (Article 21.5 - Canada)* panel was concerned primarily with the timing and subject-matter of the Tasmanian import restriction, and its subsequent impact on the July 1999 implementing measures adopted by the Government of Australia, just as we are concerned primarily with the potential impact of the results of the First Assessment Review on the Final Determination and Section 129 Determination.

4.44 The United States also argues that the First Assessment Review is a new determination, separate from the Final Determination and Section 129 Determination, and initiated prior to the DSB's adoption of recommendations and rulings in this dispute. The United States relies on the following findings of the panel in *EC – Bed Linen (Article 21.5 - India)*:

> [T]he fact that the EC, subsequent to its re-examination of the dumping determinations with respect to imports from Egypt and Pakistan, and in the context of a review initiated on the request of Eurocoton, carried out an analysis of whether injury was caused by imports from India alone does not, *ipso facto*, establish that Regulation 696/2002 is a measure "taken to comply". Rather the opposite would seem to be the case – that Regulation would seem to be an **entirely new determination**, reached as a result of **events subsequent** to the EC having adopted a measure to comply with the DSB's recommendation.[41]

4.45 According to the United States, the *EC – Bed Linen (Article 21.5 - India)* dispute demonstrates that a new determination that was made in a subsequent segment of an anti-dumping or

[40] In its comments on Canada's reply to Question 21 from the Panel, the US asserts that "the fact that the grant repayment was conditioned on the provision of the new non-commercial loan was central to the panel's finding that the two actions were 'inextricably linked elements of a single transaction'". We note that the US refers in this regard to para. 6.50 of the *Australia – Leather II (Article 21.5 - US)* report, where the panel was addressing the substantive issue of whether or not Australia had withdrawn its prohibited subsidies. Contingency between the subsidy repayment and new loan was not mentioned explicitly by that panel at para. 6.5 of its report, where it was determining whether or not to include the new loan in the scope of its DSU Article 21.5 proceeding.

[41] *EC – Bed Linen (Article 21.5)*, para. 6.20 (bold emphasis added).

countervailing duty proceeding – and not made to implement recommendations and rulings of the DSB – falls outside the jurisdiction of DSU Article 21.5 panels.[42]

4.46 In *EC – Bed Linen (Article 21.5 - India)*, the European Communities imposed anti-dumping duties on imports of bed linen from Egypt, India and Pakistan. The European Communities made a cumulative injury assessment. The European Communities was found to have incorrectly calculated anti-dumping duties on imports from India. The European Communities amended its calculation in respect of such imports from India. The parties agreed that the re-determination of dumping in respect of imports from India fell within the scope of DSU Article 21.5. The European Communities also applied the revised calculation method to other anti-dumping duties imposed on imports from Egypt and Pakistan. As a result, the European Communities found that anti-dumping duties should not be imposed on such imports. Consequently, the European Communities conducted a separate injury analysis in respect of imports from India, to determine whether such imports alone caused injury to the domestic industry. The European Communities found that they did, and therefore affirmed the imposition of anti-dumping duties on imports of bed linen from India. India claimed that the determinations in respect of Egypt and Pakistan, and the finding of injury and the resulting imposition of anti-dumping duties on bed linen from India, were measures "taken to comply" under DSU Article 21.5. The above panel finding relied on by the United States concerns the Panel's exclusion of the India-specific injury determination from the scope of the DSU Article 21.5 proceedings.

4.47 While we acknowledge that the First Assessment Review is a new determination made in a subsequent segment of a countervailing duty proceeding, we disagree with what we see as the implication of the United States argument, i.e., that *EC – Bed Linen (Article 21.5 – India)* stands for the principle that a measure taken in a subsequent segment of a proceeding could never constitute a "measure[] taken to comply" in the meaning of DSU Article 21.5, if it is not explicitly so identified. Rather, we understand the panel in *EC – Bed Linen (Article 21.5 – India)* to have ruled that, in the particular circumstances of that case, the measure taken in a subsequent segment of a proceeding did not constitute a "measure[] taken to comply". In our view, the above finding of the *EC – Bed Linen (Article 21.5)* panel can be distinguished from the present case, as the First Assessment Review does not concern "events subsequent" to the Final Determination and Section 129 Determination. The relevant measure in *EC – Bed Linen (Article 21.5 - India)* concerned an injury determination initiated as a result of a re-determination of dumping in respect of imports that were not covered by the relevant rulings and recommendations of the DSB. Thus, not even the re-determination of dumping in respect of those imports was a "measure[] taken to comply", let alone the new injury determination prompted by that re-determination of dumping. By contrast, the First Assessment Review is far more closely connected to what the United States considers is the "measure[] taken to comply", i.e., the Section 129 Determination. In particular, the First Assessment Review is concerned with the same

[42] The US also argues that Article 21.5 proceedings are by their nature more focused and limited than other panel proceedings under Article 6.2 of the DSU, and that it is beyond the scope of such a limited 90-day inquiry to fully examine an entirely new set of assessment review results based on a wholly new administrative record, consisting of new sales, new imports, potentially new respondents and potentially new subsidy programmes. We note, however, that US law allows DSB rulings and recommendations to be implemented through administrative reviews in certain circumstances (see "Statement of Administrative Action" in *Message from the President of the United States Transmitting the Uruguay Round Agreements, Texts of Agreements Implementing Bill, Statement of Administrative Action and Required Supporting Statements*, H.R. Doc. No. 103-316, vol. 1 at 656 (Exhibit CDA-1), at 356-357). This undermines the US argument that assessment reviews should be excluded from the scope of DSU Article 21.5 proceedings. Furthermore, we note that measures taken to comply with the rulings and recommendations of the DSB may be every bit as complex, if not more so, than the original measure in dispute. DSU Article 21.5 does not provide for accelerated procedures because implementation measures are necessarily simple, or straightforward. It does so in order to ensure that justice is delivered swiftly. In any event, we note that we are only finding that part of the First Assessment Review (i.e., the pass-through analysis) is covered by these DSU Article 21.5 proceedings. We are not finding that the entirety of the First Assessment Review is covered by these proceedings.

substantive issue as the Section 129 Determination, i.e., pass-through. In addition, the First Assessment Review applies to import entries that were initially subject to the cash deposit rate fixed by the measure subsequently replaced by the Section 129 Determination. Furthermore, the panel in *EC – Bed Linen (Article 21.5 - India)* explicitly noted that India "[did] not argue that the subsequent two measures und[id] the compliance effectuated by the first measure".[43] We can only assume that the panel would have reached a different conclusion if India had argued that the subsequent measures undid the compliance effectuated by the first measure, as Canada has done in the present case.

4.48 We further note that in addressing the scope of the Article 21.5 proceedings in *EC – Bed Linen (Article 21.5 - India)*, the Appellate Body had regard to "the object and purpose of the DSU". In this regard, the Appellate Body noted that, by virtue of Article 3.3 of the DSU, "the prompt settlement of disputes" is "essential to the effective functioning of the WTO". Given the overlap in effect of the Final Determination, Section 129 Determination, and the First Assessment Review, we are very conscious that if we exclude the pass-through analysis in the First Assessment Review from these proceedings, Canada and the United States will still dispute the same issue, i.e., pass-through of subsidy benefit, in respect of the same import entries[44], as they did in the original proceedings concerning the Final Determination. In our view, this would be wholly inconsistent with the object and purpose of the DSU which, as noted above, is to ensure the prompt settlement of disputes.

4.49 Before concluding, we note that Canada, China and the European Communities have made a number of arguments that might suggest that DSU Article 21.5 should be interpreted broadly in the present case because of the peculiarities of the system of retrospective duty assessment applied by the United States. We do not consider it appropriate to base our findings on such arguments, because the interpretation and application of DSU Article 21.5 must accommodate both prospective and retrospective duty assessment systems. As a consequence, we have considered carefully the operation of DSU Article 21.5 in the context of both prospective and retrospective duty assessment systems, in light of the abovementioned dispute settlement decisions.

4.50 For the foregoing reasons, we reject the US request for a preliminary ruling that the First Assessment Review falls outside the scope of these DSU Article 21.5 proceedings, in so far as the pass-through analysis is concerned.

B. SCOPE OF USDOC'S PASS-THROUGH ANALYSIS

4.51 Canada's main argument in this proceeding is that USDOC, in implementing the rulings and recommendations of the DSB, continued to presume a pass-through of subsidy benefits, rather than conducting the required analysis. Canada claims that this resulted in the imposition of countervailing duties in a manner inconsistent with Articles 10 and 32.1 of the SCM Agreement, and Article VI:3 of the GATT 1994. In particular, Canada argues that USDOC completely excluded entire groups of transactions, on the basis that these were not arm's length sales, and in addition erred by rejecting the aggregate data and information provided by Canada in support of its pass-through claim, requiring instead company-specific data[45], and also by applying "inappropriate"[46] benchmark prices for those transactions that were individually examined for pass-through. Canada also claims that, in the Section 129 Determination and the First Assessment Review, the USDOC continued to presume pass-through

[43] *EC – Bed Linen (Article 21.5)*, para. 6.21.

[44] We refer to those import entries for which the Final Determination set the cash deposit rate, and the First Assessment Review finalized the duty assessment. *See*, para. 4.41, *supra*.

[45] We recall here that the United States objected (at our substantive meeting with the parties) to Canada's assertion that the USDOC had "rejected" any data submitted by Canada in the Section 129 proceeding (Canada's first written submission, para. 32). In commenting on this argument, Canada clarified that it was not claiming that the United States had outright rejected the information in question, but instead that the USDOC had failed to analyse various record data when any of the five factors existed (Canada's reply to Question 27 from the Panel).

[46] Canada's first written submission, page 22, heading 2 (Annex A – 1).

in respect of purchases of logs from sawmills by unrelated tenure-holding sawmills. Furthermore, Canada claims that the USDOC presumed pass-through in respect of all sawmill-to-sawmill transactions in the context of the First Assessment Review. Canada claims that, as a result of all the above, the United States impermissibly inflated the amount of countervailing duties levied on imports of softwood lumber from Canada. We shall examine each of these claims in turn.[47]

1. Arm's length transactions

(a) Arguments of the parties

4.52 Canada asserts that pass-through should be investigated whenever there is a transaction between unrelated parties. In both the Section 129 Determination and the First Assessment Review, however, USDOC only investigated pass-through in respect of a narrower category of transactions, namely those that were found by USDOC to be at arm's length. Canada states that the USDOC found that transactions between unrelated parties were not at arm's length if any one of the following factors existed in the province: (1) limitations on log sales in Crown tenure contracts; (2) wood supply commitment letters; (3) payment of the stumpage fees by the downstream log purchaser; (4) log purchase agreements of a certain structure; or (5) fibre exchange agreements between tenured sawmills.

4.53 Canada disputes the application of what Canada refers to as USDOC's "external factor" test. According to Canada, a transaction between unrelated parties is by definition an arm's length transaction. Canada asserts that, because the external factors identified by the USDOC do not transform an arm's length transaction into one that is not at arm's length, the existence of any such factors cannot excuse the United States from its obligation to conduct the required benefit pass-through analysis. According to Canada, none of the factors identified by USDOC alters the fact that sellers of logs attempt to obtain the best price available in transactions with unrelated purchasers.

4.54 The United States asserts that the DSB's recommendations and rulings concerned only (1) arm's length sales (2) between unrelated parties. According to the United States, both of these conditions must be fulfilled before a pass-through analysis becomes necessary. In particular, the United States argues that sales between formally unrelated parties are not necessarily arm's length. The United States asserts that the DSB's recommendations and rulings themselves recognize a distinction between arm's length and affiliation, presenting arm's length sales as a subset of sales between unrelated entities, since the DSB (by virtue of para. 167(e) of the Appellate Body's report) ruled that USDOC should have conducted "a pass-through analysis in respect of arm's length sales of *logs* . . . to unrelated sawmills." (emphasis in original) The United States argues that whether the entities operate "at arm's length" involves more than just a question of formal affiliation; it involves an analysis of whether one party effectively "controls" the other or whether the parties have roughly equal bargaining power. The United States argues that its five factor test addresses this issue of control, since many of the circumstances of sales of lumber in Canada are controlled by government mandates and other government-imposed conditions.

4.55 The United States asserts that USDOC identified two categories of government-mandated restrictions whereby log sellers are not free to act in their best interests to choose and negotiate among

[47] Canada's request for establishment of a panel also refers to a claim concerning the USDOC "applying the results of the 'pass-through' analysis to a countervailing duty cash deposit rate invalidated as a result of judicial review proceedings conducted in accordance with US law, and failing to apply the results to a valid rate" (WT/DS257/15, page 2). Although this claim was alluded to in the introduction to Canada's first written submission (para. 10) (see Annex A – 1), Canada did not revert to this claim in the substantive part of that submission. Nor did Canada pursue this claim in its subsequent oral or written submissions to the Panel. We therefore consider that Canada has effectively abandoned this claim. In any event, we find that the very brief reference to this issue at para. 10 of Canada's first written submission is insufficient to establish a *prima facie* case in support of Canada's claim.

potential buyers: (1) limitations on log sales that are contained in Crown tenure contracts, such as appurtenancy and local processing requirements, and (2) wood supply agreements. The United States asserts that USDOC also determined that many of the Canadian log sales could not be considered to be at arm's length because the actual structure of certain log purchase agreements empowered the purchasing sawmill to control many aspects of the transaction. Specifically, with respect to certain log purchase agreements, the sawmill actively manages all aspects of harvest and delivery. With respect to others, the sawmill finances or provides other goods or services as part of the transaction.

4.56 The United States asserts that USDOC also considered that it was not required to conduct a pass-through analysis when two other factors were present: (i) payment of the stumpage fees by the downstream lumber producers and (ii) fibre exchange agreements between Crown tenure holders. Although the United States submits that these factors are "not exclusively arm's-length issues",[48] it is clear that the USDOC found that transactions were not arm's length when these factors existed.[49]

4.57 The United States argues that its approach to implementing the DSB's recommendations and rulings is based on the explicit language of the Appellate Body's ruling.

(b) Evaluation by the Panel

4.58 The United States has emphasized before us throughout this Article 21.5 proceeding that it based its approach to pass-through, in the Section 129 Determination[50], on the language of the Appellate Body's report, and specifically on the Appellate Body's use of the phrase "arm's length" in its ruling. We recall that the exact wording of the Appellate Body's ruling is:

> "the Appellate Body ... upholds the Panel's finding ... that USDOC's failure to contact a pass-through analysis in respect of **arm's length** sales of *logs* by tenured harvesters/sawmills to unrelated sawmills is inconsistent..."[51]

We further recall that our finding being upheld by the Appellate Body makes no reference to the term "arm's length".

(i) Scope of original panel findings compared with scope of appeal and scope of Appellate Body rulings

4.59 Before entering into the details of the Appellate Body's ruling, and its potential implications for the parties, we first recall that in the original dispute there were three broad categories of transactions in respect of which we found that the United States' failure to conduct a pass-through analysis was inconsistent with various provisions of the covered Agreements. Specifically, these categories were: (1) sales of logs by tenured timber harvesters that do not produce lumber to unrelated lumber producers; (2) sales of logs by tenured harvester-sawmills to unrelated sawmills; and (3) sales of lumber by tenured harvester-sawmills to unrelated lumber re-manufacturers. The United States did not appeal our finding in respect of the first of these categories of transactions. It did appeal our findings in respect of the second and third categories of transactions. The Appellate Body, in turn, upheld our finding in respect of the second category, and reversed our finding in respect of the third category.

[48] US second written submission, para. 23 (see Annex B – 2).

[49] See, for example, page 4 of Section 129 Determination (Exhibit CDA-5) ("where we determined that any of the sales reported by the Canadian parties were affected by one or several of the five factors listed above, we concluded that the transactions were not conducted at arm's length").

[50] The US arguments in this proceeding did not cover USDOC's conduct of the Final Assessment Review. We note, however, that the USDOC adopted the same approach to pass-through in the First Assessment Review as in the Section 129 Determination.

[51] Appellate Body Report, para. 167(e) (italic emphasis in original, bold emphasis supplied).

4.60 Given both the scope and the outcome of the US appeal, the DSB's recommendations and rulings which the United States was obliged to implement in respect of the first category of transactions consist exclusively of our findings. In respect of the second category, these recommendations and rulings consist of our findings and the relevant findings of the Appellate Body. In respect of the third category, in view of the reversal on appeal of our findings, there were no DSB recommendations and rulings for the United States to implement. We take up the first and second categories separately.[52]

(ii) Sales of logs by tenured timber harvesters that do not produce lumber to unrelated lumber producers

4.61 Canada objects to USDOC's application of the five factors in all situations in order to identify for further pass-through analysis log sale transactions that were made at "arm's length". Canada argues that, instead, a pass-through analysis is required in respect of all log sales between unrelated entities. The United States did not appeal our findings in respect of sales of logs by tenured timber harvesters that do not produce lumber to unrelated lumber producers. Thus, as noted, our findings alone constitute the substance of the DSB's recommendations and rulings in respect of this category of transactions. We therefore start by recalling the details of our analysis and findings on the pass-through issue in general, along with our specific pass-through findings on this category of transactions.

4.62 We recall that, as a general matter, the primary focus of our discussion and findings on pass-through in our Panel Report centred on affiliation. Thus, we described the "basic question" presented by Canada's pass-through claim as

> "whether USDOC was obligated to conduct a pass-through analysis in respect of the input transactions between timber harvesters (both those that produce lumber and those that do not) and **unrelated** sawmills, and between sawmills and unrelated re-manufacturers ...".[53]

4.63 We then explained that we understood Canada's claim to be

> "that where upstream transactions between **unrelated** entities exist for inputs, any subsidies to the producers of those inputs cannot be assumed also to be subsidies to the downstream product under investigation."[54]

4.64 We noted that

> "[w]here the subsidies at issue are received by **someone other than** the producer of the investigated product, the question arises whether there is subsidization in respect of that product."[55]

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[52] We note that Canada's arguments concerning the USDOC pass-through analysis refer to transactions between "independent harvesters" and sawmills. This could mean that Canada's claim is limited to the first category of transactions identified above. However, since note 2 of the USDOC's Section 129 Determination provides that "[f]or purposes of this determination, the referenced log sales by tenured independent harvesters/sawmills will be referred to as sales by independent harvesters", we understand Canada's claim concerning "independent harvester" transactions to include both of categories of transactions. Furthermore, we understand that both categories of transactions were covered by the Section 129 Determination, whereas only the first category of transaction was covered by the First Assessment Review. If the USDOC were to have applied its five factor approach in respect of the second category of transactions in the First Assessment Review, our evaluation would have been the same as for the USDOC's treatment of that category of transactions in the Section 129 Determination.

[53] Panel Report, para. 7.81 (emphasis supplied).

[54] Panel Report, para. 7.85 (emphasis supplied).

4.65 We then stated that

> "[t]he heart of the pass-through issue is whether, where a subsidy is received by **someone other than** the producer or exporter of the product under investigation, the subsidy nevertheless can be said to have conferred benefits in respect of that product."[56]

4.66 Finally, we concluded, at paragraph 7.99 of our report, that

> the USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to **unrelated** sawmills producing subject softwood lumber ... was inconsistent with Article 10 and thus Article 32.1 SCM Agreement, and with Article VI:3 of GATT 1994.[57]

4.67 This conclusion was repeated in similar terms in the final section of the Panel Report, where we held that:

> "the USDOC's failure to conduct a pass-through analysis in respect of upstream transactions for log and lumber inputs between **unrelated** entities was inconsistent with Article 10 SCM Agreement and Article VI:3 of GATT 1994".[58]

4.68 At most places in our analysis and conclusions, therefore, we did not use the term "arm's length" in discussing the pass-through issue, but instead addressed the potential obligation to conduct a pass-through analysis as pertaining to transactions between unrelated parties.

4.69 We acknowledge, however, that we did make some limited references to the term "arm's length" in our findings, although we did not define that term. Footnote 163 of our Panel Report, which was included in a sentence describing the "basic question presented by [Canada's] claim" as concerning the need to conduct a pass-through analysis in respect of transactions between unrelated entities, states, in relevant part:

> "We note that this claim only concerns such alleged **arms'-length** transactions between unrelated entities ..."[59]

4.70 We also used the term "arm's length" at paragraphs 7.94 and 7.95 of our report, in the context of the first category of transactions, namely log sales to lumber producers by timber harvesters that do not produce lumber. In particular, in paragraph 7.94 we identified such sales as the first type of "arms' length" transaction that we needed to address. We then summarized the US position as being that no pass-through analysis was needed for such transactions because of their small volume and because they might not be at "arms' length". This latter was a reference back to the US argument, summarized at paragraph 7.76 of our report, that "the many restrictions imposed on tenure holders, including requirements to process timber locally, 'suggests that all or most of the sales by independent loggers may not be at arms'-length'". We noted, at paragraph 7.95 of our report, that the United States neither cited to any record evidence establishing "the volume of the possible arms'-length sales at issue", nor argued that USDOC had made efforts to collect such information. We went on to say that the United States had not conducted the required pass-through analysis for these transactions, and had "point[ed] to no factual basis in the record for its conclusion that such an analysis was not necessary".

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[55] Panel Report, para. 7.85 (emphasis supplied).
[56] Panel Report, para. 7.91 (emphasis supplied).
[57] Panel Report, para. 7.99 (emphasis supplied).
[58] Panel Report, para. 8.1(c) (emphasis supplied).
[59] Panel Report, note 163 (emphasis supplied).

4.71 As noted above, however, our overall conclusion in respect of all categories of log sales (including by timber harvesters not owning sawmills to sawmills) was clear in stating that pass-through analysis was required where the parties to such transactions were unrelated. In short, based on the language of our conclusion and the underlying language of our analysis, in the original dispute before us, our primary focus in respect of the pass-through issue was in fact transactions between unrelated parties.

4.72 Indeed, in the present Article 21.5 proceeding, even the United States explicitly acknowledges that our findings were not premised on or restricted by any concept of "arm's length" transactions. In particular, in response to one of our questions, the United States notes that

> "as evident in paragraph 7.95, however, the original panel's findings did not depend upon whether or not the sales claimed by Canada were, in fact, arm's length sales."[60]

4.73 We thus conclude that, in respect of log sales by tenure-holding timber harvesters that do not own sawmills to unrelated sawmills, the USDOC's exclusion from pass-through analysis of certain such sales on the grounds that they were not at "arm's length" was inconsistent with the United States' obligations pursuant to the DSB's recommendations and rulings.

(iii) Sales of logs by tenured harvester-sawmills to unrelated sawmills

4.74 We now turn to the second broad category of log sales at issue in this Article 21.5 proceeding, in respect of which the United States appealed our finding that a pass-through analysis was required. For this category – log sales by tenured harvester/sawmills to unrelated sawmills – the Appellate Body upheld our finding but in doing so introduced the term "arm's length", which does not appear in our finding. We recall that in the original dispute and before the Appellate Body, both parties used the term "arm's length" at various points in their arguments, apparently with considerably different meanings. They presented no arguments concerning the issue of "arm's length" as such, however. As noted above, in the Panel Report we did make some limited references to the term "arm's length", although not in the context of the second category of log sales, and we did not ascribe any particular definition to this term. In addition, and most significantly for this Article 21.5 proceeding, the term arm's length appears in numerous places in the Appellate Body's analysis (although without being defined), especially in its ruling at paragraph 167(e) upholding our finding in respect of this category of log sales.

4.75 We understand the United States to argue in the present proceeding that it based its implementation of the DSB's recommendations and rulings on the explicit wording used by the Appellate Body, which according to the United States upheld our finding to the extent of "arm's length" sales of logs by tenured harvester/sawmills to unrelated sawmills. In other words, the United States views the Appellate Body (and thus the DSB) as having modified, albeit implicitly, our conclusions concerning the pass-though issue in respect of this category of log sales. On this basis, a primary focus of the USDOC's analysis in the Section 129 Determination in respect of log sales by tenured harvester/sawmills to unrelated sawmills was to identify which transactions in the universe of such sales were and were not at arm's length. For Canada, however, the term "arm's length" has to do exclusively with corporate affiliation – any transaction between unaffiliated parties is, by definition, an arm's length transaction. Thus, for Canada, the Appellate Body used the term "arm's length" synonymously with "unrelated".[61] Canada argues that therefore, the USDOC, by not conducting a competitive benefit analysis in respect of the sales between unrelated parties that it found not to be at "arm's length", failed to comply with the DSB's recommendations and rulings.

[60] US Answers to Panel's questions, 29 April 2005 (Article 21.5 proceeding), at paragraph 9.

[61] See, for example, para. 10 of Comments of Canada on the Responses by the United States Following the Substantive Meeting of the Panel.

4.76 We thus find ourselves confronted with significant ambiguity surrounding the issue of pass-through in the DSB's recommendations and rulings in respect of log sales by tenured harvester/sawmills to unrelated sawmills, which ambiguity seems to have arisen from the inclusion of the term "arm's length" in the conclusion set forth at para. 167(e) of the Appellate Body Report.[62] It is not clear to us why the Appellate Body chose to include this term in its ruling. This ambiguity is compounded by the fact that the participants in the appellate proceedings were each relying on separate meanings of that term. In this regard, while we can understand that the United States sought to give meaning to the Appellate Body's use of the term "arm's length", we disagree with the United States' reasoning.

4.77 There are several important factors in respect of which we are in no doubt. First, the scope of the DSB recommendations and rulings to be implemented by the United States is not based exclusively on the adopted findings of the Appellate Body. The findings of the original panel adopted by the DSB are also relevant in this regard.

4.78 Second, as noted above and as acknowledged by the United States, *our* overall conclusion in respect of all categories of log sales (whether or not the tenured log seller owns a sawmill) was clear in stating that pass-through analysis was required where the parties to such transactions were unrelated.

4.79 Third, the explicit language used by the Appellate Body at para. 167(e) of its report was to "uphold" our conclusion in respect of log sales by tenured harvester/sawmills to unrelated sawmills, as set forth in the relevant part of the first sentence of para. 7.99 of the Panel Report. That is, para. 167(e) of the Appellate Body Report contains no explicit modification of the finding at para. 7.99 of the Panel Report in respect of log sales by tenured harvester/sawmills to unrelated sawmills.

4.80 Nor does the United States argue that there is such an *explicit* modification. Rather, the United States' argument is that the Appellate Body, in introducing the word "arm's length" into its ruling, *implicitly modified* our conclusion. In this context we recall that Article 17.13 of the DSU permits the Appellate Body to "uphold, modify or reverse" the findings of a panel. We would expect, however, that any such action would be explicit. In particular, if the Appellate Body intended to modify a finding that it was explicitly upholding, such modification presumably likewise would be made explicitly. Indeed, in other cases, the Appellate Body has been very explicit when modifying a panel's findings, identifying precisely which finding (or which part of a finding) was being modified.[63] In this case, however, the Appellate Body Report contains no discussion of the meaning of the term "arm's length", nor any explanation of how it may have intended to distinguish that term from the word "unrelated". We consider that for an Article 21.5 panel to accept, in such circumstances, that the Appellate Body had *implicitly* modified the underlying panel findings could have serious systemic implications, since it could result in significant uncertainty regarding the import of Appellate Body reports, and the resultant DSB rulings and recommendations. For these reasons, it would not be appropriate for us to proceed on the basis that the Appellate Body may have intended to modify our findings in respect of sales by tenured harvester/sawmills to unrelated sawmills but refrained from saying so explicitly.

4.81 In any event, while acknowledging the existence of a certain ambiguity, on balance we are not persuaded that the Appellate Body's finding that a pass-through analysis was required in respect of

[62] We recall here that the United States does not consider that our findings in the original dispute were conditioned on any concept of "arms' length". See para. 4.72, *supra*.

[63] See, for example, para. 196(d) of the Appellate Body Report in *Brazil –Aircraft. See* also paras. 199 and 263(f) of the Appellate Body Report in *US – Line Pipe*. Although para. 168 of the Appellate Body Report refers to modification of the Panel Report, there is no indication precisely which part of the Panel Report is being modified. In such circumstances, there is no reason to believe that the Appellate Body was referring to anything other than the modification resulting from the Appellate Body's explicit reversal of certain of the original panel's findings.

"arm's length sales of *logs* by tenured harvesters/sawmills to unrelated sawmills" is necessarily different from (in the sense that it would modify) our finding that a pass-through analysis was required in respect of "logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to unrelated sawmills". In particular, we note that the Appellate Body used a virtually identical formulation – also including a reference to "arm's length sales" - at para. 123 of its Report. Footnote 147 to para. 123 confirms that, in para. 123, the Appellate Body was indeed referring to para. 7.99 of the Panel Report. Since para. 123 of the Appellate Body report marks the beginning of the Appellate Body's introduction to the pass-through issue, we do not understand the Appellate Body to be substantively modifying para. 7.99 of the Panel Report at that juncture. Instead, it would seem much more reasonable to conclude that the Appellate Body was merely paraphrasing the relevant finding set forth at para. 7.99 of the Panel Report. Equally, we do not agree that a modification should necessarily be implied from the use of virtually identical language later in the Appellate Body Report. Instead, one could again understand the Appellate Body to be merely paraphrasing the relevant finding of the original panel.

4.82 In light of all of the foregoing considerations, and notwithstanding our acknowledgement of a certain ambiguity in respect of the term "arm's length", we do not accept the US argument, based on para. 167(e) of the Appellate Body Report, that the rulings and recommendations of the DSB only required a pass-through analysis in respect of "arm's length" log sales by tenured harvester/sawmills to unrelated sawmills. Instead, given that the Appellate Body upheld, without explicit modification, the relevant finding at para. 7.99 of the Panel Report, we consider that the United States was required to implement the recommendations and rulings of the DSB by conducting a pass-through analysis in respect of all log sales by tenured harvester/sawmills to unrelated sawmills -- covered by the finding at para. 7.99 of the Panel Report regarding sales of logs by "tenure-holding harvesters (whether or not also lumber producers) to unrelated sawmills producing softwood lumber" -- irrespective of any considerations as to whether or not such sales were "arm's length".

2. Rejection of aggregate data

(a) Arguments of the parties

4.83 Canada claims that in its Section 129 Determination, USDOC considered only company-specific, transaction-by-transaction data for the pass-through analysis, disregarding all aggregate transaction and pricing data submitted as an alternative by the Canadian respondents[64,65]. Canada asserts that the specific data requested by USDOC was impossible to collect as it involved hundreds of thousands of transactions by thousands of companies in Canada. Canada claims that USDOC nevertheless refused to provide reasonable alternatives for data submission, even though its CVD investigation was undertaken on an aggregate basis. Canada claims that the Panel already made it clear that company-specific data are not necessarily required to conduct a pass-through analysis. Canada refers in this regard to para. 7.98 of the Panel Report, where the Panel stated that it was "not convinced that the need to conduct a pass-through analysis for these transactions would necessarily or inevitably convert every aggregate case into a company-specific case." Canada also refers to footnote 170 of the Panel Report, where the Panel stated "[f]or example, inquiry into possible relationships between the entities concerned, and the use of sampling or other statistical techniques in respect of the relevant transaction at issue, might offer possible approaches to be explored."

[64] As noted above, however, Canada clarified in response to questioning by the Panel that it did not claim that USDOC outright rejected the data. Rather, Canada challenged how the USDOC did and did not use them. See para. 4.51 and footnote 45, *supra*.

[65] Concerning these alternative data, Canada asserts that in many instances, Canadian respondents provided data from a representative sample of Canadian companies. According to Canada, the data provided were as much as were practicably available, and could and should have been used by the USDOC to complete its pass-through analysis.

4.84 The United States asserts that, to conduct its pass-through analysis, the USDOC first had to obtain data from Canada supporting Canada's claim that a portion of the total volume of Crown logs processed into lumber – as reported by Canada – should be reduced to account for arm's length log sales between unrelated parties in which no benefit passed through. The United States submits that, because the USDOC had conducted the original investigation on an aggregate basis and not on a company-specific basis and had not previously conducted such a pass-through analysis, the administrative record did not contain evidence supporting Canada's claims.

4.85 The United States asserts that the USDOC therefore asked Canada, through questionnaires, to identify the volume of log sales subject to its pass-through claims, and to provide specific information necessary to determine whether during the period of investigation there were arm's length sales of logs by independent harvesters to unrelated sawmills and by tenured harvesters/sawmills to unrelated sawmills. According to the United States, this would allow the USDOC to identify transactions that were eligible for the last phase of the analysis (competitive benefit). The requested information related to, *inter alia*, the relationship between the parties to the specific transactions (such as whether the parties were affiliated) and the circumstances surrounding the subject sales.

4.86 The United States further submits that the DSB's recommendations and rulings treated pass-through as a company-specific issue. In particular, the United States notes that the Appellate Body referred to the need to determine whether a benefit conferred "on the input *producer*" passed through to the "*producer* of the processed product" (emphasis supplied).

4.87 The United States rejects Canada's argument that the Panel already indicated that company-specific data are not necessarily required to conduct pass-through analyses. The United States argues that, in response to US arguments to the effect that there is a mismatch between an investigation conducted on an aggregate basis and the company-specific nature of the pass-through issue, the Panel simply found that pass-through can indeed be examined during an aggregate investigation. According to the United States, the Panel did not suggest that company-specific information should not be used to analyze whether there was a pass-through of subsidies.

(b) Evaluation by the Panel

4.88 First, we note the US argument that the USDOC needed company-specific and / or transaction-specific data in order to determine whether or not the parties to the transactions were related. Canada has not disputed that the USDOC needed such data for this purpose. Since the question of affiliation is central to the threshold issue of whether or not a pass-through analysis is required, we see no reason why the USDOC should be prevented from collecting company-specific and /or transaction-specific data for this purpose.[66]

4.89 Second, Canada has not argued that a company-specific and/or transaction-specific analysis is inconsistent with any particular provision of the SCM Agreement. In the absence of specific provisions, we are reluctant to instruct investigating authorities what data they should collect, and how they should use those data, in the context of their pass-through analyses. Nor do we consider that investigating authorities have an obligation simply to accept such alternative data as may be

[66] We note that the USDOC did accept some aggregate data for purposes of determining affiliation in respect of parties to log transactions in certain provinces. The Section 129 Draft Decision Memorandum (Exh. CDA-6 at pp. 9, 10, 13, 14) indicates that the basis for doing so was certifications provided with the data to the effect that the individual companies included in the aggregate figures were unaffiliated. Thus, our understanding is that it was these certifications, which necessarily concerned only the specific companies involved, that were accepted by the USDOC.

volunteered to them by respondents based on the respondents' assessment that the authorities' information requests are too burdensome.[67]

4.90 Third, Canada has not established that a company-specific and/or transaction-specific analysis is precluded by the rulings and recommendations of the DSB. Although we stated in our Panel Report that we were "not convinced that the need to conduct a pass-through analysis for these transactions would necessarily or inevitably convert every aggregate case into a company-specific case",[68] we certainly did not state that the USDOC should be precluded from proceeding on a company-specific basis if it chose to do so.

4.91 Finally, we recall that Canada has acknowledged that it does not assert that the USDOC rejected outright all of the aggregate information submitted by Canadian respondents.[69]

4.92 For the above reasons, we reject Canada's claim that the USDOC improperly disregarded all aggregate transaction and pricing data submitted by the Canadian respondents.

3. Sawmill-to-sawmill transactions

(a) Arguments of the parties

4.93 Canada claims that in the Section 129 Determination, the USDOC continued to presume pass-through in respect of all log transactions between tenured sawmills. Canada's claim is based on its assertion that, in the Section 129 Determination, the USDOC did not investigate sales of logs between tenured sawmills. Canada asserts that the original Panel and Appellate Body findings provide no basis for refusing to conduct a pass-through analysis simply because the purchasing sawmill holds tenure.

4.94 Canada also claims that in the First Assessment Review, USDOC presumed pass-through in respect of all sawmill-to-sawmill transactions since it failed to request information on any purchases of logs by sawmills from other sawmills.

4.95 Regarding the USDOC's Section 129 Determination, the United States asserts that the scope of the Appellate Body's ruling was limited – by footnote 151 of the Appellate Body's report – to sales of logs to sawmills that "do[] not hold a stumpage contract", i.e., to sawmills that do not hold tenure. According to the United States, the Appellate Body therefore only upheld the original panel's finding that the USDOC should have conducted a pass-through analysis with respect to transactions between tenured timber harvester/sawmills and unrelated, non-tenure holding sawmills. The United States submits that the USDOC properly implemented the rulings and recommendations of the DSB by following the specific direction issued by the Appellate Body.

4.96 The United States does not respond to Canada's claim concerning the scope of the information requested by USDOC in the First Assessment Review.

(b) Evaluation by the Panel

4.97 We shall first address Canada's claim regarding the scope of the information requested by the USDOC in its Section 129 Determination. We shall then examine Canada's claim regarding the First Assessment Review.

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[67] In this regard, we consider that the accuracy of certain aggregate data in respect of affiliation is not informative of whether the substance of the aggregate data in terms of volume and price is either representative or accurate. These are entirely separate issues.

[68] Panel Report, para. 7.98.

[69] See footnote 45 *supra*.

(i) Section 129 Determination

4.98 As a preliminary matter, we note that Canada's claim does not cover purchases of logs by sawmills from tenured timber harvesters that do not themselves produce lumber. Canada's claim concerning the scope of the USDOC's investigation is restricted to sawmill-to-sawmill transactions.[70]

4.99 On substance, we note that the United States' defence to this claim is based on the definition of "sawmill" found at footnote 151 of the Appellate Body Report. That definition explicitly restricts the term "sawmill" as used in the Appellate Body Report to "an enterprise that processes logs into softwood lumber and does not hold a stumpage contract". Our Panel Report, however, does not adopt the same definition of "sawmill" as employed by the Appellate Body. Rather, our findings regarding inter-sawmill transactions concerned purchases by all sawmills, whether or not they hold a stumpage contract. [71] Furthermore, in the panel proceedings, neither party suggested that the definition of "sawmill" should be restricted in any way.

4.100 Second, we recall that the Appellate Body did not explicitly modify our finding at para. 7.99 of the Panel Report concerning inter-sawmill transactions. Rather, our finding was explicitly upheld by the Appellate Body. The United States submits that, because of the definition of "sawmill" set forth at footnote 151 of the Appellate Body Report, our finding regarding inter-sawmill transactions (as set forth at para. 7.99 of the Panel Report) was only upheld by the Appellate Body in so far as it concerned log purchases by sawmills that did not hold a stumpage contract. We disagree.

4.101 The considerations that we highlight at para. 4.80, *supra*, in respect of the issue of *implicit modification* of a panel's findings are equally pertinent here, to the extent that the US argues that the Appellate Body made such an implicit modification. We do acknowledge the possibility that the Appellate Body's use of a different, narrower definition of "sawmill" in its report than we did in the Panel Report may have led to a certain ambiguity as to the scope of the Appellate Body's, and thus the DSB's rulings, and it is not clear to us why the Appellate Body introduced this narrower definition. That said, however, the practical effect of the definition set forth at footnote 151 of the Appellate Body Report is that the Appellate Body's findings regarding inter-sawmill transactions were restricted to transactions involving purchases by sawmills that did not hold a stumpage contract. In other words, the Appellate Body made no findings regarding our conclusion concerning inter-sawmill transactions involving purchases by sawmills that did hold a stumpage contract. In the absence of any findings by the Appellate Body regarding this latter category of transactions, our findings regarding such transactions stand, and form the sole basis for the DSB's recommendations and rulings in respect of these transactions.

4.102 We note the US argument in this regard that in its notice of appeal, the United States challenged "the entirety of the findings of the original panel that Commerce had to conduct a pass-through analysis with respect to transactions between producers of subject merchandise"[72]. We understand the United States to argue that the scope of its appeal therefore covered the Panel's findings regarding purchases by all sawmills, whether or not they hold a stumpage contract, and that the Appellate Body's findings should therefore reflect the scope of the US appeal. This would mean that our conclusion regarding log purchases by sawmills that do hold a stumpage contract would somehow be subject to the findings of the Appellate Body. While we see merit in such an argument (in the sense that the scope of the Appellate Body's findings should normally reflect the scope of the

[70] Thus, at para. 55 of its first written submission (see Annex A – 1), Canada accuses the United States of ignoring the findings of the original panel and Appellate body concerning "sawmill-to-sawmill transactions" . Canada does not complain, in the context of this claim, that the USDOC failed to investigate sales by tenured timber harvesters that do not produce lumber.

[71] In order to avoid any uncertainty, in these proceedings we continue to use the term "sawmill" to refer to an enterprise that processes logs into softwood lumber, whether or not it holds a stumpage contract.

[72] See US Response to Question 1 from the Panel.

appellant's appeal), we note that the Appellate Body's "sawmill" definition would appear to apply to the entirety of the Appellate Body Report, including the section entitled "Claims of Error by the United States – Appellant". In that section, the Appellate Body states that the United States "contends that the Panel erred in finding that a pass-through analysis is required in respect of sales of *logs* from tenure-holding sawmills producing softwood lumber to unrelated **sawmills**".[73] Furthermore, in describing the "Scope of the Issue Appealed", the Appellate Body states that "[t]his appeal thus concerns the situations where: (i) a tenured timber harvester owns a sawmill and processes some of the logs it harvests into softwood lumber, but at the same time sells at arm's length some of the logs it harvests to unrelated **sawmills** for processing into lumber ...".[74] Notwithstanding the terms of the US Notice of Appeal, therefore, the issue addressed by the Appellate Body, and therefore the scope of the Appellate Body's findings, was explicitly restricted (as a result of footnote 151 of the Appellate Body's Report) to inter-sawmill transactions involving log purchases by sawmills not holding a stumpage contract. Inter-sawmill transactions involving log purchases by sawmills holding a stumpage contract were therefore not covered by the Appellate Body's findings.[75] Accordingly, our finding regarding such transactions could not have been reversed or otherwise modified by the Appellate Body.

4.103 Since our finding at para. 7.99 of the Panel Report regarding inter-sawmill transactions involving log purchase by sawmills holding a stumpage contract could not have been reversed or otherwise modified by the Appellate Body, that finding must be reflected in the scope of the rulings and recommendations of the DSB. Thus, by failing in the Section 129 Determination to analyse pass-through in respect of inter-sawmill transactions involving purchases by (unrelated) sawmills that hold a stumpage contract, the United States failed to properly implement the rulings and recommendations of the DSB regarding such transactions.

(ii) First Assessment Review

4.104 Canada submits that, in its administrative review, the USDOC failed to request information on any sawmill-to-sawmill transactions. Canada asserts that, in its only request for information on arm's length log transactions, the USDOC restricted its request in its initial questionnaire to the volume and value of Crown logs sold by independent harvesters (i.e., "by any person or company that did not own or operate a sawmill" or "by non-mill-owning tenure holders") to softwood lumber producers. Canada refers in this regard to the questionnaires sent by the USDOC to various Canadian provinces (Exhibit CDA-9), and the USDOC's Preliminary Assessment Review Determination Exhibit CDA-10).

4.105 The United States did not respond to Canada's claim, which concerns the conduct of the First Assessment Review. When asked a question regarding this claim, the United States responded on the basis of the information requested by the USDOC in the Section 129 Determination, rather than the First Assessment Review.[76] We presume that the United States declined to respond in respect of the First Assessment Review because of its view that the latter measure falls outside the scope of the present proceedings. We recall, however, our finding that the First Assessment Review does fall within the scope of these proceedings insofar as the pass-through issue is concerned. We also recall that we warned the parties at our substantive meeting with them in the present proceeding that, in the

[73] Appellate Body Report, para. 16 (italic emphasis in original, bold emphasis supplied).
[74] Appellate Body Report, para. 128 (emphasis supplied).
[75] The scope of the appeal is described in the penultimate sentence of para. 124 of the Appellate Body Report. That sentence refers to certain sales of logs and lumber "to sawmills". Since the word "sawmills" is qualified by the abovementioned footnote 151, it is clear that the scope of the appeal was restricted to certain sales of logs and lumber to "enterprise[s] that process[] logs into softwood lumber and do[] not hold a stumpage contract".
[76] See US Response to Question 4 from the Panel.

absence of any ruling on the US preliminary request at that time, the parties should assume in their arguments and submissions that the First Assessment Review falls within these proceedings.

4.106 We find that Canada has *prima facie* established, on the basis of the abovementioned Exhibits, that the USDOC failed in the First Assessment Review to investigate pass-through in respect of any sawmill-to-sawmill transactions. Given the original panel and Appellate Body findings regarding sawmill-to-sawmill transactions, we do not see how the USDOC could have properly implemented the rulings and recommendations of the DSB in this case without also analysing pass-through in respect of sales of logs between sawmills in the First Assessment Review. In the absence of any argumentation concerning this matter by the United States, we find on the basis of the above that Canada has established a *prima facie* case that the United States has failed to properly implement the rulings and recommendations of the DSB by excluding sawmill-to-sawmill transactions from the pass-through analysis in the First Assessment Review.

C. THE BENCHMARKS USED IN THE USDOC'S PASS-THROUGH ANALYSIS

1. Arguments of the parties

4.107 In its first submission, Canada challenges the benchmarks used by the USDOC in determining whether subsidy benefits passed through in certain log sales between unrelated parties. In particular, Canada challenges the import price data used by the USDOC (in conjunction with price data for logs purchased from private holders of forested land) in constructing the market price benchmarks for determination of benefit.

4.108 The United States disputes this challenge on two grounds. First, the United States asserts that this issue is outside the Panel's terms of reference as it is not referred to in Canada's request for establishment of a panel. Second, the United States argues that even if the issue were properly before the Panel, it has no substantive merit, as the import data used by USDOC were reasonable, and Canada has pointed to no provision of any covered agreement that has been violated by the use of these data.

2. Evaluation by the Panel

4.109 Turning to whether this challenge is outside our terms of reference, we recall that Canada's request for establishment refers to four specific alleged failures by the United States to comply with the DSB's recommendations and rulings, which can be summarized as (1) excluding certain categories of transactions from pass-through analysis; (2) presuming that certain transactions were not at arm's length and thus that benefits passed through; (3) applying the results of the pass-through analysis to a countervailing duty cash deposit rate that had been invalidated in judicial review procedures under US law[77]; (4) failing to conduct a pass-through analysis in the first administrative review of the lumber CVD measure.

4.110 None of these four alleged failures refers to or has any evident connection with either the methodology or the data that USDOC used in its *calculations* of pass-through of benefits in respect of those transactions where it performed such calculations. Rather, this issue is distinct from and independent of the four listed allegations. While Canada, in response to a question from us, asserts that "Canada identified its challenge to the pass-through benchmarks in its panel request", it points to no specific language in the request in this regard, and we find no such reference. Canada's argument seems to be, rather, that the statement in the request that the United States' measure(s) taken to comply are "inconsistent with Articles 10 and 32.1 of the SCM Agreement and Article VI:3 of the GATT 1994" is sufficient to bring this challenge within our terms of reference. We disagree.

[77] We have already expressed our view that Canada has effectively abandoned this claim, or at least failed to establish a *prima facie* case in support thereof. See note 47 above.

Canada's request describes the four specific alleged violations (legal claims), none of which has to do with the benchmarks used, and then identifies the various measures which in Canada's view are inconsistent by virtue of these alleged violations. Thus, we find that the issue of the market benchmarks used by USDOC represents a separate challenge, not referred to in the request for establishment. It therefore falls outside our terms of reference.

4.111 In light of the above, we reject Canada's claim regarding the benchmarks used by the USDOC in its pass-through analysis.

D. COUNTERVAILING DUTY AMOUNT

1. Arguments of the parties

4.112 Canada submits that the effect of the failure by the United States to comply with the recommendations and rulings of the DSB is an impermissible inflation of the amount of its countervailing duties. Canada submits that the United States is now required to do one of two things: either (1) conduct an appropriate pass-through analysis for all Crown log transactions involving unrelated parties, including through the use of aggregate data; or (2) exclude from the calculation of the overall *ad valorem* subsidy rate amounts of subsidy that have been presumed to pass through such transactions.

4.113 The United States submits that the USDOC properly calculated the revised countervailing duty rate by reducing the numerator of the *ad valorem* subsidy rate by C$ 28,344,121.

2. Evaluation by the Panel

4.114 We have identified a number of deficiencies in the USDOC's implementation of the rulings and recommendations of the DSB regarding *US – Softwood Lumber IV*, in particular in respect of the pass-through issue in both the Section 129 Determination and the First Assessment Review.

4.115 As a result of such failures to properly implement the rulings and recommendations of the DSB, the USDOC included in its numerator transactions for which it had not demonstrated that the benefit of subsidized log inputs had passed through to the processed product. As in the original proceeding, we find that this results in the imposition of countervailing duties in a manner inconsistent with Articles 10 and 32.1 of the SCM Agreement, and Article VI:3 of the GATT 1994.

V. CONCLUSIONS AND RECOMMENDATIONS

5.1 In light of the above, we reject:

- the US request for a preliminary ruling that the First Assessment Review falls outside the scope of the present DSU Article 21.5 proceeding, insofar as the pass-through analysis is concerned;

- Canada's claim that the USDOC improperly disregarded all aggregate transaction and pricing data submitted by the Canadian respondents;

- Canada's claim against the benchmarks used by the USDOC in its pass-through analysis;

5.2 We uphold Canada's claims that:

- in the Section 129 Determination, and in the treatment of pass-through in the First Assessment Review, the United States failed to properly implement the recommendations and rulings of the DSB in this dispute by failing to conduct a pass-through analysis in respect of sales, found

by USDOC not to be at arm's length, of logs by tenured timber harvesters, whether or not they also produce lumber, to unrelated lumber producers, whether or not they hold a stumpage contract; and

- in the Section 129 Determination, and in the First Assessment Review, the USDOC therefore included in its subsidy numerator transactions for which it had not demonstrated that the benefit of subsidized log inputs had passed through to the processed product.

5.3 We do not consider it necessary to make any conclusion regarding the claim identified in Canada's Request for Establishment of a panel regarding USDOC "applying the results of the 'pass-through' analysis to a countervailing duty cash deposit rate invalidated as a result of judicial review proceedings conducted in accordance with US law, and failing to apply the results to a valid rate".

5.4 We therefore conclude that the United States remains in violation of Article 10 and 32.1 of the SCM Agreement, and Article VI:3 of the GATT 1994.

5.5 Under Article 3.8 of the DSU, in cases where there is infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment of benefits under that agreement. Accordingly, we conclude that, to the extent the United States has acted inconsistently with the provisions of the SCM Agreement and of GATT 1994, and failed to properly implement the recommendations and rulings of the DSB in this dispute, it has nullified or impaired benefits accruing to Canada under that Agreement. Pursuant to Article 19.1 of the DSU, therefore, we recommend that the United States bring its Section 129 Determination and First Assessment Review into conformity with these provisions.

5.6 Pursuant to DSU Article 19.1, Canada has requested that we suggest ways in which the United States could implement our recommendation. In particular, Canada suggests[78] that the United States do one of the following two things:

- It should refund the amount of the countervailing duties it imposed to offset alleged subsidy amounts impermissibly presumed to pass through;

or

- It should revise its measures to meet its WTO obligations and refund the amount of the countervailing duties it imposed to the extent that they exceeded the amount of the alleged subsidy demonstrated to have passed through to the production of softwood lumber.

5.7 Given the complexities of the issue at hand, we consider that in the first instance the modalities of the implementation of our recommendation are for the United States to determine. We therefore decline to make the suggestions proposed by Canada.

_____

[78] Canada's suggestion is made at para. 58 of its oral statement (see Annex A – 3). That paragraph also contains a request for a recommendation which differs from the request set forth at para. 72 of Canada's first written submission (see Annex A – 1). We understand that para. 58 of Canada's oral statement is intended to amend and replace para. 72 of Canada's first written submission. This was certainly the understanding expressed by the United States at our meeting with the parties, to which Canada did not object.

ANNEX A

Submissions of Canada

ANNEX A-1

FIRST WRITTEN SUBMISSION OF CANADA

24 February 2005

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Canada – Aircraft	*Canada – Measures Affecting the Export of Civilian Aircraft*, Report of the Appellate Body, WT/DS70/AB/R, adopted 20 August 1999.
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US – Countervailing Measures on Certain EC Products	*United States – Countervailing Measures Concerning Certain Products from the European Communities*, Report of the Appellate Body, WT/DS212/AB/R, adopted 8 January 2003.
US – Lead and Bismuth II	*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 and Corr.2, adopted 7 June 2000.
US – Lead and Bismuth II	*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.
US – Softwood Lumber III	*US – Preliminary Determinations with Respect to Softwood Lumber*, Report of the Panel, WT/DS236/R, adopted 2 November 2002.

TABLE OF ABBREVIATIONS USED IN THIS SUBMISSION

Alberta 21 May 2004 Pass-Through Questionnaire Response	Response of the Government of Alberta to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (May 21, 2004) (Exhibit CDA-13).
Alberta 15 September 2004 Supp.Pass-Through Questionnaire Response	Response of the Government of Alberta to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004) (Exhibit CDA-14).
Alberta 12 November 2003 AR Questionnaire Response	Response of the Government of Alberta to the Department's 12 September 2003 Questionnaire (12 November 2003) (Exhibit CDA-38).
B.C. 15 September 2004 Supp. Pass-Through Questionnaire Response	Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004) (Exhibit CDA-32).
B.C. 12 November 2003 AR Questionnaire Response	Response of the Government of British Columbia to the Department's 12 September 2003 Questionnaire 12 (November 2003) (Exhibit CDA-33).
Draft Section 129 Determination	USDOC Memorandum from J. Jochum to J. May, *Draft Decision Memorandum, 129 Proceeding for the WTO Appellate Body finding in the Final Countervailing Duty Determination, Certain Softwood Lumber from Canada* (19 November 2004) (Exhibit CDA-6).
DSB	Dispute Settlement Body
DSU	*Understanding on Rules and Procedures Governing the Settlement of Disputes*
Final AR Determination	*Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber from Canada*, C-122-839 (13 December 2004) (Exhibit CDA-11).
Final AR Determination Notice	*Notice of Final Results of Countervailing Duty Administrative Review and Rescission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce, 20 December 2004) (Exhibit CDA-8).
Final Section 129 Determination	USDOC Memorandum from J. Jochum to B. Tillman, *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada* (6 December 2004) (Exhibit CDA-5).
GATT 1994	*General Agreement on Tariffs and Trade 1994*
Kalt 2004a	J.P. Kalt and D. Reishus, *Statement for the First Administrative Review*, Attachment 1 to Letter from British Columbia Lumber Trade Council to USDOC (15 March 2004) (Exhibit CDA-21).
Kalt 2004d	J.P. Kalt and D. Reishus, *Economics of Arms's Length Transactions and Subsidy Pass-Through*, submitted as Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Exhibit BC-PT-39 (Exhibit CDA-20).
Manitoba 21 May 2004 Pass-Through Questionnaire Response	Response of the Government of Manitoba to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (May 21, 2004) (Exhibit CDA-43).

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

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

I. INTRODUCTION

1. This case is about the failure of the United States to implement the recommendations and rulings of the DSB in respect of its obligation to demonstrate whether, and to what extent, an input subsidy passes through arm's-length sales of input products. Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement require the United States to demonstrate such a "pass through" as a precondition to imposing countervailing duties on downstream products produced from those inputs. The original panel and the Appellate Body in this dispute found that where the United States presumes, rather than demonstrates, a pass-through, it impermissibly imposes countervailing duties where no subsidy has been determined to exist.

2. On the facts of this dispute, the alleged input subsidy is the provision of goods – standing timber – by Canadian provincial governments for less than adequate remuneration. The input product is a log, which is produced from standing timber harvested from public lands (Crown logs). The downstream processed product is softwood lumber, which is produced from Crown logs.

3. The United States is imposing countervailing duties on imports of Canadian softwood lumber products. Accordingly, it must demonstrate how, and to what extent, any subsidy to Crown logs is *also* an indirect subsidy to softwood lumber in every instance where, on the facts of this dispute, the producer of the Crown log and the producer of the softwood lumber are unrelated.

4. The USDOC has failed to make any such demonstration. Despite the recommendations and rulings of the DSB requiring a demonstration of pass-through, the USDOC continues to presume that pass-through occurred for virtually all arm's-length transactions. Based on this presumption, the USDOC included the subsidy amount attributable to the production of the *log* in its calculation of the amount of the subsidy attributable to the production of *softwood lumber*, thereby significantly inflating the overall amount of the countervailing duty imposed on softwood lumber.

5. A pass-through analysis in this dispute would involve comparisons of log input sale prices to a market benchmark price, to establish whether, and to what extent, a benefit within the meaning of Article 1.1(b) of the SCM Agreement is conferred upon the recipients that used the inputs in the production of softwood lumber. Because the USDOC failed to consider virtually all of the arm's-length log transactions at issue, it did not make such comparisons. The USDOC therefore presumed that log producers lowered the price of logs by the full amount of the alleged input subsidy in their sales to unrelated softwood lumber producers.

6. The USDOC failed to consider arm's-length log transactions for three reasons.

7. First, it refused to collect or analyze record evidence pertaining to log transactions between tenured sawmills.

8. Second, the USDOC ignored record evidence concerning pricing submitted by the Canadian respondents because the information was in aggregate form. Although the USDOC used aggregate data to conduct the softwood lumber investigation, and consistently refused throughout the investigation to consider company-specific information, it nevertheless deemed aggregate data inappropriate for a pass-through analysis. No exception exists in the GATT 1994 or in the SCM Agreement allowing the USDOC to refuse to conduct the required pass-through analysis on the grounds that available data are in aggregate form.

9. Third, with respect to the evidence of log transactions that the USDOC did consider, it deemed there to have been a full pass-through of the alleged log subsidy if any of five factors it identified existed. Nothing in the original panel or Appellate Body reports suggests that these factors are relevant to a pass-through analysis. Those reports confirm that an investigating authority must establish the existence and amount of a benefit pass-through where a subsidy is received by someone

other than the producer or exporter of the investigated product; this obligation is without further qualification. The USDOC reliance on such factors to reject log transactions as being not at arm's length also is contrary to generally accepted economic principles.

10. The USDOC applied the results of the limited pass-through analysis that it did conduct to the countervailing duty rate established in the original investigation, which long before had been invalidated as a result of judicial review proceedings conducted in accordance with US law. A few days later, the USDOC imposed a new countervailing duty rate based on the results of its administrative review, in which it conducted no pass-through analysis at all.

11. In order to bring its imposition of duties into conformity with US obligations under the GATT 1994 and the SCM Agreement, the USDOC must establish, and not presume, whether and to what extent the benefit from the alleged log subsidy flows through to the production of softwood lumber where the parties to the log transaction are unrelated. The USDOC has not done so. Instead, it has claimed that for the vast majority of transactions no such analysis was required. This claim of compliance has no basis, and Canada asks the Panel to so determine.

12. Canada begins this submission with a description of the relevant facts underlying the dispute. Canada then addresses the US obligations at issue, the violation of these obligations, and the consequential effect on the US countervailing duties that continue to be imposed.

II. FACTUAL BACKGROUND

A. Procedural History

13. On 17 February 2004, the DSB adopted the recommendations and rulings in the reports of the original panel and the Appellate Body in *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*.[1]

14. On 5 March 2004, the United States notified the DSB, pursuant to Article 21.3 of the DSU, of its intention to implement these recommendations and rulings.[2] Canada and the United States agreed shortly afterward on a ten-month "reasonable period of time", beginning 17 February 2004, for the United States to implement the recommendations and rulings of the DSB.[3]

15. At the DSB meeting of 17 December 2004, the United States informed the DSB that it had complied with its recommendations and rulings. Canada subsequently requested the establishment of an Article 21.5 compliance panel.[4]

16. The DSB established this Panel at its meeting of 14 January 2005, and referred the matter of suspension of concessions to Article 22.6 arbitration.[5]

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[1] DSB, *Minutes of Meeting (17 February and 19 March, 2004)*, WT/DSB/M/165, 30 March 2004, at 4(a), para. 49. See also Appellate Body Report and Panel Report.

[2] *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada, Communication from the United States*, WT/DS257/12, 9 March 2004.

[3] *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada, Agreement under Article 21.3(b) of the DSU*, WT/DS257/13, 30 April 2004.

[4] *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada, Recourse to Article 21.5 of the DSU by Canada, Request for Establishment of a Panel*, WT/DS257/15, 4 January 2005; and *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada, Recourse to Article 22.2 of the DSU by Canada*, WT/DS257/16, 4 January 2005.

[5] *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada, Recourse by Canada to Article 21.5 of the DSU, Constitution of the Panel*, WT/DS257/19, 14 February 2005; and *United States – Final Countervailing Duty Determination With Respect to Certain*

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

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

18. On the basis of these facts, the original panel found that the USDOC was required to conduct subsidy "pass-through" analysis where:

- tenured timber harvesters who do not produce softwood lumber provide logs to unrelated downstream lumber producers ("independent harvester" transactions);

- tenured timber harvester/lumber producers provide logs to other unrelated lumber producers ("sawmill-to-sawmill" transactions); and

- tenured timber harvester/lumber producers sell lumber to unrelated downstream lumber re-manufacturers ("re-manufacturer" transactions).[8]

19. The panel concluded:

> that the USDOC's failure to conduct a pass-through analysis in respect of upstream transactions for log and lumber inputs between unrelated entities was inconsistent with Article 10 SCM Agreement and Article VI:3 of GATT 1994, and we therefore *uphold* Canada's claim that the United States' imposition of countervailing duties in respect of such transactions was inconsistent with Articles 10 and 32.1 SCM Agreement and Article VI:3 of GATT 1994 (…).[9]

Softwood Lumber from Canada, Recourse by the United States to Article 22.6 of the DSU, Constitution of the Arbitrator, WT/DS257/20, 14 February 2005.

[6] These obligations are imposed through complex tenure and licensing agreements.

[7] Panel Report, at para. 7.84 ("In considering Canada's pass-through claim in detail, we recall that countervailing measures are applied to imports of certain products (the subject merchandise), which in the countervailing duty investigation in dispute before us comprises softwood lumber products produced by sawmills from logs, and re-manufactured softwood lumber products produced by re-manufacturers from lumber obtained from sawmills."); Appellate Body Report, at para. 124 ("We found above that the stumpage programmes of Canadian provinces at the heart of this case provide standing timber to timber harvesters, allegedly conferring a benefit. The standing timber eventually becomes felled trees or logs, which are processed into softwood lumber as well as remanufactured lumber products. USDOC defined the product subject to the investigation at issue as 'certain softwood lumber', which includes 'primary' lumber and 'remanufactured' lumber. The United States imposed countervailing duties on imports of these softwood lumber products from Canada."). See also *US – Softwood Lumber III*, at paras. 7.68-7.69.

[8] Panel Report, at para. 7.99.

[9] Panel Report, at para. 8.1(c) [emphasis in original].

20. On appeal, the United States accepted these findings and conclusions, as applied to independent harvester transactions.[10] However, the United States asked the Appellate Body to reverse the panel's findings regarding sawmill-to-sawmill transactions and re-manufacturer transactions. The Appellate Body reversed the panel's findings on re-manufacturer transactions[11], but upheld the panel's findings on sawmill-to-sawmill transactions:

> [T]he Appellate Body… upholds the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *logs* by tenured harvesters/sawmills to unrelated sawmills is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.[12]

21. The DSB subsequently adopted the Appellate Body report and the panel report and recommended that the United States bring its measure into conformity with its obligations under the SCM Agreement and the GATT 1994.[13]

C. US Action Taken to Address Pass-Through Subsequent to the Recommendations and Rulings of the DSB

1. Section 129 Determination

22. The United States has enacted legislation that provides for proceedings to address DSB recommendations and rulings concerning a US countervailing duty measure. Section 129(b) of the *Uruguay Round Agreements Act* authorizes the USDOC to "issue a second determination … to respond to the recommendations in a WTO panel or Appellate Body report."[14] Section 129 proceedings may involve the issuance of new questionnaires and application of new methodologies. The section 129 process represents one way in which the United States may bring the imposition of its countervailing duties into conformity with its obligations.

23. As a result of the DSB recommendations and rulings concerning the US failure to demonstrate a pass-through for independent harvester and sawmill-to-sawmill transactions, the USDOC initiated section 129 proceedings.

24. In questionnaires issued by the USDOC, the Canadian respondents were requested to identify the volume of Crown timber purchased by sawmills in independent harvester transactions. With respect to sawmill-to-sawmill transactions, the USDOC request for information was limited to only a small subset of such transactions.[15] The Canadian respondents replied to these questionnaires, providing a detailed breakdown of the volume of independent harvester transactions and, in many

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[10] Appellate Body Report, at para. 127, and footnote 154. ("The United States notes that it 'does *not appeal* the Panel's finding that, where the subsidy is received by independent harvesters, *i.e*., entities that do *not* produce [softwood lumber] product[s] under investigation and operate at arm's length, a pass through analysis would be required to determine if the subsidy received by the independent harvesters was indirectly bestowed on production of softwood lumber'."[emphasis in original])

[11] Appellate Body Report, at paras. 165, 167(f).

[12] Appellate Body Report, at para. 167(e) [emphasis in original].

[13] DSB, *Minutes of Meeting (17 February and 19 March, 2004)*, WT/DSB/M/165, 30 March 2004, at 4(a), para. 49.

[14] SAA, at 1022 (Exhibit CDA-1). See also *Uruguay Round Agreements Act*, Pub. L. No. 103-465, § 129(b), 108 Stat. 4838, *codified at* 19 U.S.C. § 3538(b) (2000) (Exhibit CDA-2).

[15] Letter from USDOC to Embassy of Canada, *Certain Softwood Lumber Products from Canada*: WTO "Pass-Through" Questionnaire (14 April 2004), Question 2, at 11 (Exhibit CDA-3). ("Of the total volume of Crown timber entering sawmills reported by the province, what portion does the province claim was sold in arm's length transactions by tenured timber sawmills to sawmills that do not have a tenure and, therefore, requires an analysis to determine if the purchaser received a subsidy benefit?")

cases, comprehensive data on sawmill-to-sawmill transaction volumes.[16] Annex I contains a detailed explanation of the volumes of record evidence submitted by Canadian provinces and industry associations. For example, British Columbia provided the USDOC with a survey demonstrating that 11.6 per cent of Crown logs consumed in B.C. sawmills were purchased from unrelated non-lumber-producing tenure holders.[17] The survey also demonstrated that an additional 6.2 per cent of Crown logs consumed in B.C. sawmills were purchased in arm's-length transactions from unrelated lumber-producing tenure holders.[18]

25. The USDOC also requested company- or transaction-specific information for each individual log transaction, such as copies of the applicable log purchase agreements and confirmation of which party paid the stumpage fee.[19] In many instances, the Canadian respondents provided sample data, explaining that much of the information was impossible to collect as it involved hundreds of thousands of arm's-length transactions by thousands of companies in Canada. The USDOC nevertheless refused to provide reasonable alternatives even after Canadian respondents explained the impossibility of the USDOC request both in writing and in meetings with USDOC officials, and rejected all information provided in aggregate form.[20]

26. The USDOC then eliminated from consideration most of the transactions for which individual company data were provided on a transaction-by-transaction basis, claiming that "… a significant portion of the transactions included in the claims by Alberta, British Columbia, Manitoba, Ontario and Saskatchewan are not arm's-length sales."[21] The USDOC found that transactions between unrelated parties were not at "arm's length" if any of the following factors existed in the province: (1) limitations on log sales in Crown tenure contracts; (2) wood supply commitment letters; (3) the payment of stumpage fees by the downstream log purchaser; (4) log purchase agreements of a certain structure; or (5) fibre exchange agreements between tenured sawmills. Where any of these "factors" existed, the USDOC did not undertake any price comparisons to establish the pass-through of the log subsidy benefit or its amount.[22] These factors eliminated the vast majority of log transactions remaining after the USDOC had already excluded all aggregate data reported on the record, including all transactions in British Columbia and roughly 90 per cent of the transactions in Alberta.

27. The USDOC maintained that a pass-through analysis was therefore required for only a small fraction of the log transactions occurring between unrelated parties.[23] This analysis led to a reduction

[16] The "Canadian respondents" comprise the Government of Canada, the Canadian provincial governments, the industry associations and certain Canadian lumber producers.

[17] See Annex I, at para. 79.

[18] *Ibid*.

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

[20] See Letter from Weil, Gotshal & Manges to USDOC (16 September 2004), at 2 (Exhibit CDA-4). See also Final Section 129 Determination, at 3-4 (Exhibit CDA-5) ("For sales not conducted at arm's length or for which respondents failed to provide sufficient data to determine whether they were conducted at arm's length, we did not conduct any further pass-through analysis and the volume of these sales was not removed from the numerator of the subsidy calculations."); and Comment 8, at 12-13 ("Although the surveys and sample data provided by the Canadian parties are sufficient for certain analyses undertaken in the context of the aggregate case, such data is not sufficient for the purposes of our pass-through analysis.").

[21] Final Section 129 Determination, at 6 (Exhibit CDA-5). See also Draft Section 129 Determination, at 7 (Exhibit CDA-6).

[22] Final Section 129 Determination, at 4 (Exhibit CDA-5) ("[W]here we determined that any of the sales reported by the Canadian parties were affected by one or several of the five factors listed above, we concluded that transactions were not conducted at arm's length."); and at 6-7 ("If, based on the evidence on the record, we were unable to ascertain that the amount qualified as an arm's-length transaction or that the stumpage for the log was paid by the harvester, we did not compare the price per cubic meter with the benchmark input price and the numerator was not reduced by that volume."). See also Draft Section 129 Determination, at 5, 7-8 (Exhibit CDA-6).

[23] Final Section 129 Determination at 7 (Exhibit CDA-5). ("We determine that the evidence on the record sufficiently demonstrates that, during the POI, there were some arm's-length log sales between sawmills

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

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

2. The Administrative Review

29. The United States uses a "retrospective" duty assessment system to periodically review the amount of any countervailing duty imposed as a result of an original final countervailing duty determination. Where no administrative review is requested by an "interested party", final assessment occurs at the amount of the countervailing duty established in the original determination. Where an administrative review is conducted, the USDOC reviews data for a period of approximately one year from the date of first imposition of final duties (the "period of review"). The revised amount of the countervailing duty established through an administrative review applies, for final assessment purposes, to imports made during that period of review.[26] The revised amount also serves as the amount of duties imposed on imports made after the results of the review come into force, and takes the form of a cash deposit required pending final assessment.

30. As they did for the section 129 proceeding, the Canadian respondents provided the USDOC with all the information necessary to conduct a pass-through analysis in the administrative review. Annex I contains a detailed explanation of this record evidence, which confirmed that a significant volume of log transactions required a pass-through analysis. Here, the USDOC's request for information was limited exclusively to independent harvester transactions.[27]

31. On 14 June 2004, nearly four months after the adoption of the recommendations and rulings of the DSB, the USDOC published the preliminary results of its administrative review.[28]

32. The USDOC's preliminary results did not contain a pass-through analysis for any of the log volumes in question. Instead, the USDOC rejected all record evidence provided by the Canadian respondents for reasons similar to those in its section 129 determination. For example, the USDOC rejected record evidence from Alberta, British Columbia and Ontario because, in some log

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and tenured harvesters/sawmills in Alberta, Manitoba, Ontario and Saskatchewan. … The result of these calculations is that only a small portion of the Crown harvest volume originally included in the numerator is excluded from the numerator of our revised subsidy calculations.")

[24] *Notice of Implementation under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures concerning Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,305, at 75,306 (Dept. Commerce, 16 December 2004) (Exhibit CDA-7).

[25] Final AR Determination Notice, 69 Fed. Reg. at 75,919-75,920 (Exhibit CDA-8).

[26] The amount of duty applies only to those imports that represent merchandise entered or withdrawn from warehouse for consumption during this period. See, *e.g.*, Final AR Determination Notice, 69 Fed. Reg. at 75,919-75,920 (Exhibit CDA-8).

[27] See Annex I at para. 77. See *e.g.*, Letter from USDOC to Embassy of Canada, *Countervailing Duty Administrative Review: Certain Softwood Lumber Products from Canada* (12 September 2003), Questionnaire for the Province of Alberta, Question III (J) at III-6 (Exhibit CDA-9) ("Did the Government of Alberta (GOA) permit any person or company that did not own or operate a sawmill and was not affiliated with a sawmill to harvest Crown timber during the [period of review]?").

[28] Preliminary AR Determination, 69 Fed. Reg. 33,204 (Exhibit CDA-10).

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

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

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

III. LEGAL ARGUMENT

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

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

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

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

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

[29] *Ibid*., at 33,208-33,209.
[30] Final AR Determination (Exhibit CDA-11).
[31] Compare Final Section 129 Determination, at 5-7 (Exhibit CDA-5) with Final AR Determination, at 46-47 (Exhibit CDA-11).
[32] Final AR Determination, at 7.

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

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

A. GATT 1994 and the SCM Agreement Prohibit the United States From Imposing Countervailing Duties To Offset Subsidization That Has Not Been Demonstrated To Exist

41. In this section, Canada sets out the basic WTO obligations requiring the United States to demonstrate, rather than presume, the existence and amount of a subsidy. Canada also sets out how these obligations have already been interpreted in this dispute as applying in a pass-through context.

42. A Member must establish that a subsidy exists before it may impose countervailing duties, and it may not impose such duties in an amount greater than the amount of the subsidy demonstrated to exist. Article VI:3 of the GATT 1994 sets out this fundamental obligation:

> No countervailing duty shall be levied on any product of the territory of any contracting party imported into the territory of another contracting party *in excess* of an amount equal to the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product ... The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of *offsetting* any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export of any merchandise. [emphasis added]

43. Under this provision, any countervailing duty levied on a product that has not been determined to have been subsidized is necessarily, and fully, "in excess" and there is no lawful "offset".[33] The obligation is reaffirmed in Article 10 of the SCM Agreement:

> Members shall take all necessary steps to ensure that the imposition of a countervailing duty[36] on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement. Countervailing duties may only be imposed pursuant to investigations initiated [footnote omitted] and conducted in accordance with the provisions of this Agreement and the Agreement on Agriculture.
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>
> [36] The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise, as provided for in paragraph 3 of Article VI of GATT 1994.

44. Finally, Article 32.1 of the SCM Agreement confirms that the imposition of duties is unlawful where a Member fails in this obligation. It provides that "[n]o specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement."

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[33] The ordinary meaning of the verb "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*". See *New Shorter Oxford English Dictionary* (Oxford: Clarendon Press, 1993), at 1985 (Exhibit CDA-12) [emphasis added].

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

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

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

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

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[34] See Panel Report, at paras. 7.90-7.91 ("[B]oth of these provisions make explicit that there must be direct or indirect *subsidization* in relation to the manufacture, production or export of a *product* for a 'countervailing duty' in the sense of the [SCM] Agreement and GATT Article VI to be imposed on that product." [emphasis in original]. See also *US – Softwood Lumber III*, at paras. 7.75, 8.1(c), and *US – Countervailing Measures on Certain EC Products*, Panel Report, at paras. 7.41-7.44, as upheld in *US – Countervailing Measures on Certain EC Products*, Appellate Body Report, at paras. 139 and 161(a), and *US – Lead and Bismuth II*, Panel Report, at para. 6.56, as upheld in *US – Lead and Bismuth II*, Appellate Body Report, at para. 63.

[35] The relationship between the definition in Article 1.1 of the SCM Agreement and the obligations under Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement has been explained by the original panel. See Panel Report, at para. 7.88 ("[Footnote 36 to Article 10 of the SCM Agreement] defines what a countervailing duty is, and in so doing makes explicit the link between a 'subsidy' to a recipient in the sense of Article 1.1 and the manufacture, production or export of a *product* that is the subject of a CVD investigation and ultimately a countervailing duty. [emphasis in original]").

[36] Panel Report, at para. 7.53; *Canada – Aircraft*, at para. 154.

[37] The original panel considered this issue in detail in the context of other claims in this dispute. See *e.g.*, Panel Report, at paras. 7.53-54. See also *Canada – Aircraft*, at para. 157.

[38] That pass-through analysis required pricing analysis had been established as far back as the *US – Canadian Pork* dispute. This GATT panel determined that:

> [G]iven the existence of separate industries for swine and pork production in Canada operating at arm's length, the subsidies granted to swine producers could be considered to be bestowed on the production of pork only if they had led to a decrease in the level of prices for Canadian swine paid by Canadian pork producers below the level they have to pay for swine from other commercially available sources of supply.

US – Canadian Pork, at para. 4.9.

[39] Panel Report, at para. 7.91. The original panel also explained that a Member may not simply presume whether and to what extent any subsequent "benefit" passed through an input transaction where the transacting parties are unrelated. In agreeing with the findings of the GATT panel in *US – Canadian Pork*, the panel stated:

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

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

> Where a subsidy is conferred on input products, and the countervailing duty is imposed on processed products, the initial recipient of the subsidy and the producer of the eventually countervailed product, may not be the same. In such a case, there is a *direct recipient* of the benefit – the producer of the *input* product. When the input is subsequently processed, the producer of the *processed product* is an *indirect recipient* of the benefit – provided it can be established that the benefit flowing from the input subsidy is passed through, at least in part, to the processed product. Where the input producers and producers of the processed products operate at *arm's length*, the pass-through of input subsidy benefits from the direct recipients to the indirect recipients downstream cannot simply be presumed; it must be established by the investigating authority. In the absence of such analysis, it cannot be shown that the essential elements of the subsidy definition in Article 1 are present in respect of the *processed product*.[41]

50. Despite the clarity of these findings, the United States, in purporting to bring the imposition of its countervailing duties into conformity with this obligation, ignored this obligation entirely with respect to some transactions and unilaterally re-defined the circumstances under which this obligation arises with respect to all other transactions.

B. The United States Continues to Impose Countervailing Duties Based On an Impermissible Presumption of Subsidization

51. Applied to the two factual situations at issue in this dispute, both the original panel and the Appellate Body have made abundantly clear to the United States that it is required under Article VI:3 of the GATT 1994 and under Articles 10 and 32.1 of the SCM Agreement to perform a benefit analysis under Article 1.1(b) for both independent harvester and sawmill-to-sawmill transactions. It has not done so.

> That panel found, as we do, that investigating authorities had the affirmative obligation to make a determination of subsidization in respect of *a product*, and could not simply assume such subsidization where the subsidies were bestowed in respect of a product (the input product) that was different from the *product subject to countervailing duty*, and where the input producers were unrelated to the producers of that subject merchandise. [emphasis in original]
> [at para. 7.92]

[40] Appellate Body Report, at paras. 140-141. See also *US – Softwood Lumber III*, at paras. 7.74-7.75.

[41] Appellate Body Report, at para. 143 [emphasis in original]. See also Panel Report, at para. 7.92. The United States had even agreed with the original panel. As noted by the Appellate Body:

> [T]he United States accepts that a pass-through analysis is required where a subsidy is bestowed *indirectly* on producers of products subject to the investigation ("subject products"). Thus, if a subsidy is received directly by an entity *other* than a producer of subject products, and that entity subsequently sells inputs to producers of subject products, the investigating authority is required to determine whether at least some of that subsidy is passed through in the sale to the producers of such products.

Appellate Body Report, at para. 129 [emphasis in original], *US – Softwood Lumber III*, at para. 7.70.

52. Instead, the United States has attempted at every turn to avoid its obligations to perform the required analysis and make the required demonstration. This non-compliance with the recommendations and rulings of the DSB has allowed the United States to continue to illegally inflate the amount of its countervailing duties on softwood lumber.

1. The United States Failed to Conduct Pass-Through Analysis for Log Transactions Between Unrelated Parties

53. The USDOC failed to conduct the required pass-through analysis for three reasons.

54. First, it presumed a full pass-through of the alleged input subsidy for all log transactions between tenured sawmills. In its section 129 determination, the USDOC restricted its request to the following information:

> Of the total volume of Crown timber entering sawmills reported by the province, what portion does the province claim was sold in arm's length transactions *by tenured timber sawmills to sawmills that do not have a tenure* and, therefore, requires an analysis to determine if the purchaser received a subsidy benefit?[42]

55. By restricting its request to log purchases by "sawmills that do not have a tenure", the USDOC inexplicably excluded information on transactions in which the purchasing sawmill had tenure – transactions that constitute the vast majority of sawmill-to-sawmill transactions in Canada. Nowhere did the USDOC make any request for information relating to purchases by sawmill owners that *did* hold tenure. It simply ignored the findings of the original panel and the Appellate Body with respect to such sawmill-to-sawmill transactions, which provide no basis for refusing to conduct a pass-through analysis simply because the purchasing sawmill holds tenure.[43]

56. The transaction volumes between tenured sawmills were excluded by the USDOC despite explicit calls for their inclusion. For example, Alberta noted at the outset of an initial questionnaire response that it believed "that the Department also should be requesting data on arm's length sales of logs between tenureholders where both the buyer and seller are sawmillers" and that it "stands ready to collect and supply this additional information on an expedited basis".[44] These calls went unanswered.

57. In its administrative review, the USDOC failed to request information on any sawmill-to-sawmill transactions. In its only request for information on arm's-length log transactions, the USDOC restricted its request in its initial questionnaire to the volume and value of Crown logs sold by independent harvesters to softwood lumber producers ("by any person or company that did not own or operate a sawmill" or "by non-mill-owning tenure holders").[45]

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[42] Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO "Pass-Through" Questionnaire (April 14, 2004), Question 2 (Exhibit CDA-3) [emphasis added].

[43] Appellate Body Report, at para. 167(e); Panel Report, at paras. 7.99 and 8.1(c).

[44] Alberta 21 May 2004 Pass-Through Questionnaire Response, at AB-1 (Exhibit CDA-13); See also Alberta 15 September 2004 Supp. Pass-Through Questionnaire Response, at 1 (Exhibit CDA-14). ("At the outset, Alberta wishes to note that Alberta's response to the original questionnaire of 14 April 2004 did not provide all the relevant data on arm's length sellers of Crown logs, due to the constraints imposed by the Department's narrow questions. Specifically, in the original questionnaire on this subject, the Department told Alberta to limit our responses to those sellers of softwood logs harvested from provincial lands who did not own sawmills themselves.")

[45] Letter from USDOC to Embassy of Canada, *Countervailing Duty Administrative Review: Certain Softwood Lumber Products from Canada* (September 12, 2003), attaching Questionnaire for the Province of Alberta, Questions III (J), (K), and (L), at III-6; Questionnaire for the Province of British Columbia, Questions III (K), (L), and (M), at IV-7; Questionnaire for the Province of Manitoba, Questions III, (D), (E) and (F), at V-5; Questionnaire for the Province of Ontario, Questions III, (K) and (L), at VI-6; and Questionnaire for the

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

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

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

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

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

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

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

See also Final AR Determination, at 47 (Exhibit CDA-11) ("In this proceeding we are examining subsidies that directly benefit the lumber manufacturing process in Canada *on an aggregate basis*" [emphasis added]).

[48] Panel Report, at para. 7.98 ("[W]e are not convinced that the need to conduct a pass-through analysis for these transactions would necessarily or inevitably convert every aggregate case into a company-specific case.") and footnote 170 ("For example, inquiry into possible relationships between the entities concerned, and the use of sampling or other statistical techniques in respect of the relevant transactions at issue, might offer possible approaches to be explored.").

[49] Final Section 129 Determination, Comment 8, at 12 (Exhibit CDA-5).

[50] *Ibid.*, at 2 ("[T]o determine whether transactions are at arm's-length requires information about the relationship between the parties to the transaction (e.g. affiliations) *and the circumstances surrounding the transactions*."[emphasis added]). See also Draft Section 129 Determination, at 3 (Exhibit CDA-6).

Final Section 129 Determination, at 4 (Exhibit CDA-5) ("We first examined whether any of the log sale transactions at issue were between affiliated parties, as defined by section 771(33) of the Tariff Act of 1930, as amended. If any of the log sales reported by the Canadian parties were determined to have been between affiliated parties, we concluded that these were not arm's-length transactions and no further pass-through analysis was conducted"). See also Draft Section 129 Determination, at 5 (Exhibit CDA-6).

section 129 determination and did reject all transactions in its administrative review based on the second condition.[51]

61. The second condition in the USDOC test has no foundation under the GATT 1994 or the SCM Agreement, nor does it accord with basic economics. Under this condition, the USDOC excluded from examination any reported independent harvester and sawmill-to-sawmill transactions that included any of the following five "factors", chosen arbitrarily as exclusive criteria: (1) limitations on log sales in Crown tenure contracts; (2) wood supply commitment letters; (3) payment of the stumpage fees by the downstream lumber producers; (4) the structure of certain log purchase agreements; or (5) fibre exchange agreements between Crown tenure holders.[52] The USDOC concluded, without any demonstrative analysis, that these factors "affect" the outcome of these transactions.[53] The USDOC conclusion has no basis and should be rejected.

62. A transaction between unrelated parties is by definition an arm's-length transaction.[54] Because the external factors identified by the USDOC do not transform an arm's-length transaction into one that is not at arm's length, the existence of any such factors cannot excuse the United States from its obligation to conduct the required benefit pass-through analysis. As the original panel and the Appellate Body confirmed, such analysis is required in every instance where the subsidized input producer is unrelated to the producer of the subject merchandise.[55] The creation of this new definition of "arm's length" by the USDOC is nothing more than an attempt to resurrect US arguments that failed before the panel in *Canada – Softwood Lumber III*.[56]

63. The USDOC refusal to conduct a pass-through analysis on the basis of these factors is also inconsistent with basic economics. Extensive economic evidence placed on the record demonstrated that none of the factors identified by the USDOC alters the fact that sellers of Crown logs attempt to obtain the best price available in transactions with unrelated purchasers.[57] These factors do not make

[51] See *e.g.*, Draft Section 129 Determination, at 9 ("The Department accepted the certifications that the transactions listed in the PWC's survey results submitted by the [Government of Alberta] were transactions between unaffiliated parties.") and at 10 ("In its 25 October 2004 questionnaire response, the [Government of British Columbia] explained that the Norcon survey controlled for affiliation between the 74 participating mills and independent harvesters based on the Department's statutory test, which we accepted."). The US law standard that the USDOC directed the Canadian respondents to rely on to certify that transactions occurred between unrelated parties was section 771(33) of the *Tariff Act of 1930* (19 U.S.C. § 1677(33)). See Exhibit CDA-17.

[52] The United States relied on the same factors in both its section 129 determination and its administrative review determination.

[53] Final Section 129 Determination, at 4 (Exhibit CDA-5) ("Evidence on the record indicates that government-mandated restrictions affect many of the log transactions that Canada reported as arm's-length sales."). See also Final AR Determination, at 47 (Exhibit CDA-11), where the USDOC states, in the absence of any prior demonstration, that "[t]he government mandates at issue here are conditions that are placed on the tenure licenses that have a direct impact on the disposition of Crown logs sold by independent harvesters."

[54] See *e.g.*, *New Shorter Oxford English Dictionary* (Oxford University Press: New York, 1993) at 114 (Exhibit CDA-18) ("at arm's length… (of dealings) with neither party controlled by the other"); *Black's Law Dictionary*, 6th ed. (St. Paul, Minn.: West, 1990), at 109 (Exhibit CDA-19) ("Arm's-length transaction… [one that is] negotiated by unrelated parties, each acting in his or her own self interest; the basis for a fair market value determination."). The SAA also defines an arm's length transaction as a transaction between unrelated parties "or between related parties such that the terms of the transaction are those that would exist if the transaction had been negotiated between unrelated parties." See SAA, at 928 (Exhibit CDA-1).

[55] Panel Report, at para. 7.92 ("…where the input producers were unrelated to the producers of that subject merchandise"); Appellate Body Report, at para. 140 ("Where the producer of the input is not the same entity as the producer of the processed product..."). See also *US – Softwood Lumber III*, at para. 7.74 ("… here a downstream producer of subject merchandise is unrelated to the allegedly subsidized upstream producer of the input ...").

[56] See *ibid.*, at paras. 4.289-4.291, and 7.79.

[57] See Kalt 2004d (Exhibit CDA-20). See also Kalt 2004a, at 43-48 (Exhibit CDA-21).

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

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

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

2. In the Few Instances Where the United States Did Perform Pass-Through Analysis, It Used Inappropriate Benchmarks That Produced Results That Were Subsequently Nullified

66. Even in the few instances in its section 129 determination where the USDOC considered log transactions, it nevertheless failed to conduct proper analyses under Article 1.1(b) of the SCM Agreement.

67. In conducting pass-through analyses in its section 129 determination, the USDOC relied on benchmarks that do not reflect a comparison to the "marketplace".[62] The USDOC, for example, derived its benchmark, in part, from log imports that were: (1) extremely small and highly variable in volume; (2) largely unrepresentative of the species harvested in each province; and (3) extraordinarily high in value and unrepresentative of prices paid in each province for logs used in softwood lumber production. Accordingly, these prices did not reflect market conditions in Canada during the period of investigation. The Canadian respondents urged the USDOC to correct its use of benchmarks, but these comments were disregarded.[63]

68. The marginal decrease the USDOC made to the amount of its countervailing duties as a result of this flawed benefit analysis in its section 129 determination was in any event overtaken ten days later, and after the end of the reasonable period of time to implement, by full re-inflation of the countervailing duty amount as a result of its administrative review determination. As explained above, the United States undertook no pass-through analysis for any of the log transactions identified

[58] See *e.g.*, Kalt 2004a, at 43-46.
[59] *Ibid.*, at 48-51; Kalt 2004d, at 9-10 (Exhibit CDA-20).
[60] Kalt 2004d, at 4-7.
[61] *Ibid.*, at 8-9.
[62] See *e.g.*, Panel Report, at para. 7.53-54. See also *Canada – Aircraft*, at para. 157. The USDOC used as a benchmark company-specific prices that individual purchasing sawmills paid for other logs it obtained from private lands or for logs it imported. Where actual company-specific purchase data were not available, the USDOC used a weighted-average of private log prices and imported log prices. See Final Section 129 Determination, at 6 (Exhibit CDA-5).
[63] See Letter from Weil, Gotshal & Manges to USDOC (26 November 2004), at 5 (Exhibit CDA-22).

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

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

69. The effect of the failure by the United States to comply with the recommendations and rulings of the DSB is an impermissible inflation of the amount of its countervailing duties. Because the USDOC calculated the amount of the subsidy going to the production of softwood lumber based on the entire volume of the Crown harvest that entered sawmills, *either directly or indirectly*, it is now required to do one of two things: either (1) conduct an appropriate pass-through analysis for all Crown log transactions involving unrelated parties, including through the use of aggregate data; or (2) exclude from the calculation of the overall *ad valorem* subsidy rate amounts of subsidy that have been presumed to pass through such transactions.

70. More particularly, should the USDOC choose not to conduct the required pass-through analysis, it must exclude from the numerator of the subsidy rate calculation benefit amounts derived from the following transaction volumes:

- Crown logs purchased in independent harvester transactions; and
- Crown logs purchased in sawmill-to-sawmill transactions.

71. Only by taking these steps will the United States comply with the recommendations and rulings of the DSB.

IV. REQUEST FOR FINDINGS AND RECOMMENDATIONS

72. The United States failed to implement the recommendations and rulings of the DSB in respect of its obligation to demonstrate whether, and to what extent, a subsidy to the production of Crown logs passes through transactions between unrelated parties. As such, Canada requests that the Panel:

- Find that the US imposition of countervailing duties in respect of the Crown log transactions identified in this dispute is inconsistent with Article VI:3 of GATT 1994 and Articles 10 and 32.1 of the SCM Agreement;
- Recommend in accordance with Article 19.1 of the DSU that the United States: (1) refund the amount of the countervailing duties imposed to offset alleged subsidy amounts presumed to pass through; or, (2) revise its measures to meet the requirements of Article VI:3 GATT 1994 and Articles 10 and 32.1 of the SCM Agreement and refund the duties to the extent that they exceed the amount of the alleged subsidy demonstrated to have passed through to the production of softwood lumber; [64] and
- Recommend that the United States bring its measures into conformity with its WTO obligations.

[64] See *US – Canadian Pork*, at para. 4.11.

ANNEX I: RECORD EVIDENCE

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

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

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

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

[66] See *e.g.*, Final 129 Determination, at 9 (Exhibit CDA-5) ("Based on the certifications and information provided by the relevant companies and the [Government of Alberta], the Department accepted the data reported to be from unaffiliated parties."). See also Draft 129 Determination, at 9 (Exhibit CDA-6) ("The Department accepted the certifications that the transactions listed in the PWC's survey results submitted by the [Government of Alberta] were transactions between unaffiliated parties"); at 10 ("In its October 25, 2004 questionnaire response, the [Government of British Columbia] explained that the Norcon survey controlled for affiliation between the 74 participating mills and independent harvesters based on the Department's statutory test, which we accepted."); at 12 ("The Department accepts the [Government of Manitoba]'s claim that the transactions were conducted between unaffiliated parties"); at 13 ("The Department accepts the certifications that the transactions listed in the [Government of Ontario]'s breakdowns [are between unaffiliated parties]"); and at 15 ("The Department accepts the [Government of Saskatchewan]'s claim that the transactions were conducted between unaffiliated parties.").

[67] Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Supplemental "Pass-Through" Questionnaire (17 August 2004) (Exhibit CDA-23); Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Second Supplemental "Pass-Through" Questionnaire (5 October 2004) (Exhibit CDA-24).

[68] See Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO "Pass-Through" Questionnaire (April 14, 2004), Question 1(c), Question 2(c), at 10-11 (Exhibit CDA-3); Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Supplemental "Pass-Through" Questionnaire (August 17, 2004), British Columbia, Questions 3, 9(b), at 3-4; Alberta, Question 1, at 8; Manitoba, Question 2, at 10; and Saskatchewan, Question 3, at 12 (Exhibit CDA-23); and Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Second Supplemental "Pass-Through" Questionnaire (October 5, 2004), British Columbia, Questions 3, 4, at 3-5; Alberta, Question 1, at 8 (Exhibit CDA-24).

[69] See Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO "Pass-Through" Questionnaire (April 14, 2004), Question 1(b), Question 2(b), at 10-11 (Exhibit CDA-3); Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Supplemental "Pass-Through" Questionnaire (August 17, 2004), British Columbia, Questions 2, 4, 6-7, 9, at 3-5; Ontario, Questions 1-4, at 6; Alberta, Questions 2-3, 6-7, at 8-9; Manitoba, Question 3, at 10; and Saskatchewan, Questions 4, 6, at 12-13; and Pass-Through Appendix, at 9-17 (Exhibit CDA-23); and Letter from USDOC to Embassy of Canada, Certain Softwood Lumber Products from Canada: WTO Second Supplemental "Pass-Through" Questionnaire (October 5, 2004), British Columbia, Questions 1, 6-7, 9, at 3-5;

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

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

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

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

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

[72] See Letter from USDOC to Embassy of Canada, *Countervailing Duty Administrative Review: Certain Softwood Lumber Products from Canada* (12 September 2003), attaching Questionnaire for the Province of Alberta, Questions III (J), (K), and (L), at III-6; Questionnaire for the Province of British Columbia, Questions III (K), (L), and (M), at IV-7; Questionnaire for the Province of Manitoba, Questions III, (D), (E) and (F), at V-5; Questionnaire for the Province of Ontario, Questions III, (K) and (L), at VI-6; and Questionnaire for the Province of Saskatchewan, Questions III, (D), (E) and (F), at VIII-4 (Exhibit CDA-9); and Preliminary AR Determination, 69 Fed. Reg. at 33, 208 (Exhibit CDA-10) ("During the underlying investigation, the Canadian parties claimed that a portion of the Crown logs processed by sawmills were purchased by the mills in arm's-length transactions with independent harvesters. Canada further claimed that such logs must be excluded from the subsidy calculation unless the Department determines that the benefit to the independent harvester passed through to the lumber producers. In anticipation of a similar claim in this administrative review, we requested in the original questionnaire that each of the Canadian provinces report the volume and value of Crown logs sold by independent harvesters to unrelated parties during the [period of review].").

[73] See Letter from Weil Gotshal & Manges to USDOC, *Certain Softwood Lumber from Canada: First Administrative Review, Pass Through of Benefit to Arm's Length Purchasers of Logs and Lumber Inputs* (24 May 2004) (Exhibit CDA-28). See also Norcon C (Exhibit CDA-29), as revised in Letter from Steptoe & Johnson to USDOC (April 26, 2004) (Exhibit CDA-30); and Kalt 2004a, at 43-50 (Exhibit CDA-21).

[74] Preliminary AR Determination, 69 Fed. Reg., at 33,208-33,209 (Exhibit CDA-10); Final AR Determination, at 45-48 (Exhibit CDA-11).

78. What follows is a brief summary of the record evidence for each province in both the section 129 proceedings and the administrative review.

A. British Columbia

79. In the section 129 proceeding, British Columbia provided the USDOC with a study by Norcon Forestry Ltd. and the accounting firm PricewaterhouseCoopers ("Norcon A") of 74 sawmills representing approximately 53 per cent of the total volume of the Crown timber harvest, which reviewed thousands of log purchase transactions with unrelated parties. Norcon A was supplemented by a further study by Norcon Forestry Ltd. ("Norcon B"). Norcon B demonstrated that 11.6 per cent of Crown logs consumed in B.C. sawmills were purchased from independent harvesters that held tenure.[75] These surveys also demonstrated that an additional 6.2 per cent of Crown logs consumed in B.C. sawmills were purchased in arm's-length sawmill-to-sawmill transactions.[76] The USDOC accepted that the surveys controlled for affiliation based on the affiliation standard under section 771(33) of the *Tariff Act of 1930*.[77] In addition to providing the aggregate results of these surveys, British Columbia provided detailed transaction-specific information on the thousands of transactions included in the surveys, including information on volume, value, the types of logs sold, the purchaser and the seller, for both private and Crown log purchases. The company-specific evidence provided in these surveys was equivalent to the information the USDOC requested in its supplemental questionnaires and could have been used to calculate pass-through using the USDOC's price-to-price comparison methodology.[78] British Columbia also provided hundreds of pages of sample log purchase agreements and tenure agreements, as well as three economic studies demonstrating that the factors identified by USDOC do not alter the arm's-length nature of the transactions at issue.

80. British Columbia also commissioned Norcon Forestry Ltd. to conduct an additional, larger survey of sawmills for the administrative review ("Norcon C"). Norcon C surveyed 132 sawmills, receiving responses that accounted for 87 per cent of the logs consumed by sawmills in 2002.[79] Norcon C demonstrated that 20 per cent of logs consumed in sawmills were harvested from Crown lands and purchased from independent harvesters.[80] In addition, British Columbia also provided evidence that 5.7 per cent of logs consumed in sawmills were purchased in sawmill-to-sawmill transactions.[81] In total, British Columbia demonstrated that a minimum of 25.7 per cent of logs harvested from Crown lands and consumed in sawmills were purchased from unrelated parties during the period of review.[82] The USDOC subsequently verified the evidence contained in Norcon C.[83]

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[75] Norcon A (Exhibit CDA-31), as revised in B.C. 15 September 2004 Supp. Pass-Through Questionnaire Response, at 2, note 1 (Exhibit CDA-32) and Norcon B, at 2 (Exhibit CDA-15).

[76] Norcon A, at Appendix III (Exhibit CDA-31); Norcon B (Exhibit CDA-15). Purchases under fibre exchange agreements were not within the scope of the surveys.

[77] Draft 129 Determination, at 10 (Exhibit CDA-6).

[78] Norcon B (Exhibit CDA-15); and B.C. October 25, 2004 Supp. Pass-Through Questionnaire Response, Narrative, at BC-PT-22 and Exhibit BC-PT-55 (Exhibit CDA-25). The public versions of Norcon B and Exhibit BC-PT-55 do not contain the company-specific evidence referred to, as it is business proprietary information that is not susceptible to public summarization.

[79] Norcon C (Exhibit CDA-29).

[80] *Ibid*.; as amended in Letter from Steptoe & Johnson to USDOC (April 26, 2004) (Exhibit CDA-30).

[81] *Ibid*.

[82] *Ibid*. As further corroboration of the substantial percentage of the B.C. harvest yielding logs traded in arm's-length transactions, the record of the administrative review also establishes that, over the past three years, between 26 and 30 per cent of the logs from timber harvested on the B.C. Coast was sold through the Vancouver Log Market. Similarly, in the B.C. Interior, logs accounting for about 26 per cent of the total harvest were sold domestically rather than internally consumed by integrated companies. See B.C. 12 November 2003 AR Questionnaire Response, Log Export Response at BC-LER-8, Exhibit BC-LER-1 (Exhibit CDA-33).

B. Alberta

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

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

C. Saskatchewan

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

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

[84] Alberta September 15, 2004 Supp. Pass-Through Questionnaire Response, Exhibit AB-S-78; revising Alberta 21 May 2004 Pass-Through Questionnaire Response, Narrative at AB-2, Exhibit AB-S-75, and Exhibit AB-S-76 (Exhibit CDA-35). The public versions of Exhibit AB-S-76 and Exhibit AB-S-78 do not contain the cited business proprietary information as it is not susceptible to public summarization.

[85] As Alberta does not have a category for "sawlogs", Alberta's submissions use "Section 80/81" logs as a basket category of coniferous volume used to produce either lumber products, pulp or roundwood.

[86] Alberta 15 September 2004 Supp. Pass-Through Questionnaire Response, AB-S-78; revising Alberta 21 May 2004 Pass-Through Questionnaire Response, at Exhibit AB-S-76 (Exhibit CDA-35). The public versions of Exhibit AB-S-76 and Exhibit AB-S-78 do not contain the cited information as it is business proprietary and not susceptible to public summarization.

[87] *Ibid.*

[88] See Government of Alberta Verification Exhibit GOA-6, Amended Table 50 (18 April2004) (Exhibit CDA-36).

[89] Government of Alberta Verification Exhibit GOA-7, Amended Table 59 (Exhibit CDA-37).

[90] See Bearing Point, *Timber Damage Assessment (TDA) Table – 2003 Update* (17 October 2003), at 9, submitted in Alberta 12 November 2003 AR Questionnaire Response, Exhibit AB-S-69 (Exhibit CDA-38).

[91] Saskatchewan 21 May 2004 Pass-Through Questionnaire Response, at SK-1, Exhibit SK-S-29 (Exhibit CDA-39). The public version of Exhibit SK-S-29 does not contain the cited business proprietary information as it is not susceptible to public summarization.

[92] Saskatchewan May 21, 2004 Pass-Through Questionnaire Response, at SK-3-4 (Exhibit CDA-39).

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

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

D. Manitoba

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

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

E. Ontario

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

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

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

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

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

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

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

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

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

88. In the first administrative review, Ontario provided evidence demonstrating that approximately 6,465,085 cubic metres (or 42 per cent of the total timber harvested from Crown land) was harvested by independent harvesters.[101] In addition, in response to the USDOC's request at verification, Ontario provided detailed evidence concerning the largest 25 sawmills in Ontario log purchases from unrelated tenure holders during the period of review.[102] As the USDOC verified, those 25 sawmills purchased 31 per cent or 4,391,708 cubic metres of Crown softwood logs from unrelated tenure holders.[103] The 4,391,708 cubic metres of Crown softwood logs from unrelated tenure holders equal 29 per cent of the total Crown softwood volume harvested during the period of review.

[100] OFIA/OLMA 16 September 2004 Supp. Questionnaire Response (Exhibit CDA-49) and OFIA/OLMA 25 October 2004 Supp. Questionnaire Response (Exhibit CDA-50).

[101] See Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Service of Government of Ontario Verification Exhibits on Petitioner's Counsel (6 April 2004), Minor Corrections, at 16-127 (Exhibit CDA-51). The "Minor Corrections" verification exhibit is not included in Exhibit CDA-51 as it contains business proprietary information that is not susceptible to public summarization. See also Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Factual Submission (15 March 2004), Exhibit 9 (final version of Exhibit ON-STATS-1) (Exhibit CDA-52).

[102] See Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Service of Government of Ontario Verification Exhibits on Petitioner's Counsel (6 April 2004), Ownership Interest Data, at 4750-4760 (Exhibit CDA-51). The "Ownership Interest Data" verification exhibit is not included in Exhibit CDA-51 as it contains business proprietary information that is not susceptible to public summarization. See also *ibid*., Minor Corrections, at 16-127 and Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Factual Submission (March 15, 2004), Exhibit 9 (final version of Exhibit ON-STATS-1) (Exhibit CDA-52).

[103] See Letter from Hogan & Hartson to USDOC, *Certain Softwood Lumber Products from Canada*: Service of Government of Ontario Verification Exhibits on Petitioner's Counsel (6 April 2004), Ownership Interest Data, at 4756 (Exhibit CDA-51).

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

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

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

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

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

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

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

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

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

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

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

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

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

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

CDA-25 Response of the Government of British Columbia to the Department's 5 October 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (25 October 2004), Narrative at BC-PT-22 and Exhibit BC-PT-55.

CDA-26 *Initiation of Antidumping and Countervailing Duty Administrative Reviews and Request for Revocation in Part*, 68 Fed. Reg. 39,055 (Dep't Commerce 1 July 2003).

CDA-27 *Certain Softwood Lumber Products from Canada: Extension of Time Limit for Preliminary Results of Countervailing Duty Administrative Review*, 69 Fed. Reg. 2,568 (Dep't Commerce 16 January 2004).

CDA-28 Letter from Weil, Gotshal & Manges to USDOC, *Certain Softwood Lumber from Canada*: First Administrative Review, Pass-Through of Benefit to Arm's-Length Purchasers of Log and Lumber Inputs (24 May 2004).

CDA-29 Norcon Forestry Ltd., *Survey of Primary Sawmills' Arm's Length Log Purchases in British Columbia* (15 March 2004), submitted with Letter from Steptoe & Johnson to USDOC (15 March 2004).

CDA-30 Letter from Steptoe & Johnson to USDOC (26 April 2004), recording minor corrections to the *Norcon Arm's Length Log Survey*.

CDA-31 Response of the Government of British Columbia to the Department's 14 April 2004 Questionnaire Concerning Pass Through of Alleged Benefits (21 May 2004), Exhibit BC-PT-18 (Letter from Steptoe & Johnson to Akin, Gump, Strauss, Hauer & Feld (20 May 2004) attaching *Survey of Primary Sawmills' Arm's Length Log Purchases In the Province of British Columbia* filed with Letter from Steptoe & Johnson to US Department of Commerce (21 December 2001)).

CDA-32 Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (15 September 2004), Narrative at 2, note 1.

CDA-33 Response of the Government of British Columbia to the Department's 12 September 2003 Questionnaire (12 November 2003), Log Export Response Narrative at BC-LER-7 – BC-LER-9 and Exhibit BC-LER-1.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

ANNEX A-2

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

31 March 2005

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I. INTRODUCTION

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

[2] US First Submission and Request for Preliminary Rulings, at para. 14. See also *EC – Bed Linen (Article 21.5 – India)* Appellate Body Report, at para. 78 ("We agree with the Panel that it is, ultimately, for an Article 21.5 panel – and not for the complainant or the respondent – to determine which of the measures listed in the request for its establishment are 'measures taken to comply'.").

[3] First Written Submission of Canada, at paras. 53-60.

[4] *Ibid.*, at paras. 3-5.

[5] *Ibid.*, at paras. 28, 68.

[6] An examination of the "existence" of something, according to the ordinary meaning of that term, includes assessing "Reality, as [opposed] to appearance" and establishing "[t]he fact or state of existing". *The New Shorter Oxford English Dictionary* (Oxford: The Clarendon Press, 1993), at 882. (Exhibit CDA-53)

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

> We addressed the function and scope of Article 21.5 proceedings for the first time in *Canada – Aircraft (Article 21.5 – Brazil)*. (…) We explained there that the mandate of Article 21.5 panels is to examine either the "existence" of "measures taken to comply" or, more frequently, the "*consistency with a covered agreement*" of implementing measures. This implies that an Article 21.5 panel is not confined to examining the "measures taken to comply" from the perspective of the claims, arguments, and factual circumstances relating to the measure that was the subject of the *original* proceedings.[7]

14. In *Australia – Leather II (Article 21.5 – US)*, the United States itself argued that measures that undo implementation appropriately fall within the scope of Article 21.5 of the DSU:

> Under Article 21.5, this panel is to consider "the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings." Plainly, if this Panel can determine the "existence" of measures taken to comply with the recommendations, it can consider whether the measures purportedly taken to comply were effectively rendered non-existent.[8]

15. As discussed, the compliance panel in that case found the government replacement loan at issue was within their terms of reference under Article 21.5 of the DSU.

16. The panel in *EC – Bed Linen (Article 21.5 – India)* shared the view that the scope of Article 21.5 is wide. In declining to include certain EC measures in its compliance review, that panel specifically noted that India "does not argue that the subsequent two measures undo the compliance effectuated by the first measure."[9]

17. Because the final results of the administrative review undo the pass-through analysis and resulting adjustment provided in the section 129 determination, the final results are properly before the Panel.

C. The Final Results of the Administrative Review Are Inextricably Linked to the Recommendations and Rulings of the DSB and Are Therefore "Measures Taken to Comply"

18. The final results of the administrative review are properly before the Panel also because they are inextricably linked to the recommendations and rulings of the DSB and to what the United States claims as being its "measures taken to comply".

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[7] *EC – Bed Linen (Article 21.5 – India)*, Appellate Body Report, at para. 79 [italics in original].

[8] *Australia – Automotive Leather II (Article 21.5 – US)*, Annex 1-2, at para. 30. See also Third Party Submission of China, at paras. 12-18.

[9] *EC – Bed Linen (Article 21.5 – India)*, Panel Report, at para. 6.21. See also Third Party Submission of the European Communities, at para. 26, citing *Dominican Republic – Cigarettes*, at paras. 7.11-7.21 ("The Panel also considers it necessary to examine Law 2-04 to secure a positive solution to the matter mandated to this Panel since Decree 636-03 has been replaced by Law 2-04."); and, *e.g.*, *Chile – Price Band System*, at para. 144. ("[A] complaining party should not have to adjust its pleadings throughout dispute settlement proceedings in order to deal with a disputed measure as a 'moving target'.")

19. As explained in Canada's first written submission, the treatment by USDOC of the pass-through issue in the final results of its administrative review is nearly identical to its section 129 pass-through determination.[10] The USDOC reproduced in the former the discussion of the five "factors" from the latter nearly word for word.[11] Moreover, these discussions apply to the same Canadian exports over the same period. In addition, the USDOC published preliminary results for the administrative review containing a "pass-through" section nearly four months after the DSB made its recommendations and rulings, and issued final results nearly ten months after those recommendations and rulings.[12]

20. The United States, recognizing the complete identity of issues in both determinations and the relevance of their timing, is left with arguing before the Panel that form ought to prevail over substance. The United States argues that assessment reviews and original investigations are different proceedings, and that while the administrative review attempted to address the pass-through issue, the review itself was initiated prior to the recommendations and rulings of the DSB.[13] In doing so, the United States ignores the fact that, under US law, the USDOC may implement the recommendations and rulings of the DSB concerning an original investigation through a subsequent administrative review.[14]

21. Article 21.5 of the DSU requires a compliance panel to examine the substance of a Member's measures notwithstanding any argument that the form of the measures could preclude compliance review. In *Australia – Automotive Leather II (Article 21.5 – US)*, for example, the panel rejected Australian claims that a government loan issued to an automotive leather producer as a replacement measure for a previous grant, which the DSB had recommended be withdrawn, was not a measure "taken to comply". The panel confirmed that the subsequent loan was within its jurisdiction to examine under Article 21.5 of the DSU because it was "inextricably linked to the steps taken by Australia in response to the DSB's ruling in this dispute, in view of both its timing and its nature."[15]

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[10] First Written Submission of Canada, at para. 33.

[11] Compare USDOC Memorandum from J. Jochum to B. Tillman, *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada* (6 December 2004), at 5-7 (Exhibit CDA-5) with *Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber from Canada*, C-122-839 (13 December 2004), at 46-47 (Exhibit CDA-11).

[12] First Written Submission of Canada, at paras. 31, 33-34. The USDOC also recognized that arguments from the Canadian respondents regarding the need to conduct pass-through analyses were based on the recommendations and rulings of the DSB in this respect. See *Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber from Canada*, C-122-839 (13 December 2004), at 43 (Exhibit CDA-11). ("They argue that, in accordance with recent WTO Appellate Body and Panel findings, the Department should conduct a pass-through analysis of logs purchased at arm's length by lumber producers to determine whether the alleged subsidy to timber harvesters from provincial stumpage benefited those lumber producers.")

[13] US First Submission and Request for Preliminary Rulings, at paras. 21-23.

[14] See "Statement of Administrative Action" in *Message from the President of the United States Transmitting the Uruguay Round Agreements, Texts of Agreements Implementing Bill, Statement of Administrative Action and Required Supporting Statements*, H.R. Doc. No. 103-316, vol. 1 at 656 (Exhibit CDA-1), at 356-357. ("Furthermore, while subsection 129(b) [of the Uruguay Round Agreements Act] creates a mechanism for making new determinations in response to a WTO report, new determinations may not be necessary in all situations. In many instances, such as those in which a WTO report merely implicates the size of a dumping margin or countervailable subsidy rate (as opposed to whether a determination is affirmative or negative), it may be possible to implement the WTO report recommendations in a future administrative review under section 751 of the Tariff Act.")

[15] *Australia – Automotive Leather II (Article 21.5 –US)*, at para. 6.5. ("In our view, the [new] loan cannot be excluded from our consideration without severely limiting our ability to judge, on the basis of the United States' request, whether Australia has taken measures to comply with the DSB's ruling.")

22. In *Australia – Salmon (Article 21.5 – Canada)*, the panel was faced with a sub-national ban on certain imported Canadian salmon products, which was introduced subsequent to national measures that Australia declared were taken to comply. Australia argued that the sub-national ban was not a measure "taken to comply" within the meaning of Article 21.5 of the DSU. The panel rejected the Australian argument, reasoning that:

> … an Article 21.5 panel cannot leave it to the full discretion of the implementing Member to decide whether or not a measure is one "taken to comply". If one were to allow that, an implementing Member could simply avoid any scrutiny of certain measures by a compliance panel, *even where such measures would be so clearly connected to the panel and Appellate Body reports concerned, both in time and in respect of the subject-matter, that any impartial observer would consider them to be measures "taken to comply"*.[16]

23. The United States avoids such rationale and attempts to shield its administrative review results from examination by the Panel by selectively quoting from the panel findings in *EC – Bed Linen (Article 21.5 – India)*.[17] The US reliance on *EC – Bed Linen (Article 21.5 – India)*, however, is misplaced. As the EC notes in its third party submission, the panel in that dispute found that the EC measures in question were not "taken to comply" within the meaning of Article 21.5 of the DSU because they did not deal with the subject matter upon which the DSB had made recommendations and rulings.[18] Indeed, the panel expressly noted that "[t]he situation might be different had there been a claim in the original dispute challenging the cumulative assessment of the effects of imports from India, Egypt, and Pakistan."[19]

24. The United States also attempts to confuse the issue by claiming that an Article 21.5 panel does not have jurisdiction to evaluate USDOC treatment of additional record evidence concerning exports subject to a US definitive countervailing duty.[20] This assertion misses the point entirely. The Panel's assessment "as to the existence or consistency with a covered agreement of measures taken to comply" under Article 21.5 of the DSU necessarily involves an examination of new factual information. As stated by the Appellate Body in *EC – Bed Linen (Article 21.5 – India)*:

> [A]n Article 21.5 panel is not confined to examining the "measures taken to comply" from the perspective of the claims, arguments, and factual circumstances relating to the measure that was the subject of the *original* proceedings. Moreover, the relevant facts bearing upon the "measure taken to comply" may be different from the facts relevant to the measure at issue in the original proceedings. It is to be expected, therefore, that the claims, arguments, and factual circumstances relating to the "measure taken to comply" will not, necessarily, be the same as those relating to the measure in the original dispute. Indeed, a complainant in Article 21.5 proceedings may well raise *new* claims, arguments, and factual circumstances different from those

[16] *Australia – Salmon (Article 21.5 – Canada)*, at para. 7.10(22) [emphasis added]. See also *EC – Bed Linen (Article 21.5 – India)*, Panel Report, at para. 6.17.

[17] US First Submission and Request for Preliminary Rulings, at paras. 15-16.

[18] Third Party Submission of the European Communities, at para. 17 ("It is important to note that the two measures in *EC – Bed linen* were not dismissed from the scope of that 21.5 proceeding because they were 'review measures'. They were dismissed because they did not relate to the original dispute between the EC and India.").

[19] *EC – Bed Linen (Article 21.5 – India)*, Panel Report, at para. 6.18, fn. 36.

[20] US First Submission and Request for Preliminary Rulings, at para. 24.

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

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

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

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

27. The US request, taken to its logical conclusion, would require Canada to make a series of identical claims to address an unchanging issue under Article VI:3 of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") and Articles 10 and 32.1 of the SCM Agreement. The US obligation to demonstrate whether, and to what extent, alleged subsidies to log production pass through arm's-length log purchases *before* imposing duties on softwood lumber products would remain in dispute for each annual assessment review under Article 21 of the SCM Agreement during the potential five-year life (or longer) of the US definitive countervailing measure. Such a result would leave the DSB in the absurd situation of having made numerous identical recommendations and rulings concerning a definitive countervailing duty for which compliance may never be secured. Were the Panel to allow the US request in this case, it would effectively insulate US countervailing measures from compliance with the recommendations and rulings of the DSB concerning pass-through.

28. The EC has noted the absurdity of the US request in this respect in its third party submission:

> Accepting the US view that the administrative review is not subject to a DSU 21.5 Panel review would turn the US system of duty assessment into a moving target that escapes from countervailing duty disciplines. Each administrative review would have to be subject to a new panel request, and by the time the panel, Appellate Body and implementation procedure was completed, another administrative review would have overtaken the results of any Section 129 determination.[23]

29. Acceding to the US request would therefore preclude any "prompt settlement of situations" under Article 3.3, "positive solution to a dispute" under Article 3.7, or "prompt compliance" under Article 21.1 of the DSU. In *Australia – Salmon (Article 21.5 – Canada)*, the United States paradoxically took the following position:

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[21] *EC – Bed Linen (Article 21.5 – India)*, Appellate Body Report, at para. 79 [italics in original]. See also EC Third Party Submission, at para. 28, referring in addition to the Appellate Body's report in *US – Shrimp (Article 21.5 – Malaysia)*, at para. 86.

[22] Third Party Submission of China, at paras. 14-15.

[23] Third Party Submission of the European Communities, at para. 29.

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

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

III. REBUTTAL SUBMISSION OF CANADA

31. Canada established in its first written submission that in both the section 129 determination and in the administrative review, the USDOC continued to presume, rather than demonstrate, a pass-through of a subsidy in arm's-length purchases of logs by sawmills in violation of US obligations under Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement.

32. The United States responds to the entirety of Canada's claims in only two paragraphs.[25] In these paragraphs, the United States contends that the USDOC properly determined that the overwhelming majority of log purchase transactions were not at arm's length and properly rejected significant volumes of record evidence. It also claims that the "recommended analysis" was performed for transactions that were found to be at arm's length, using "appropriate log prices as benchmarks". Finally, the United States claims that the recommendations and rulings of the DSB concerned only those sawmill-to-sawmill transactions in which the purchaser did not hold tenure.

33. Canada addresses each of these US assertions in turn.

34. First, the reliance by the USDOC on the five "factors" as a pretense to reject arm's-length log transactions is not supported by the GATT 1994, or the SCM Agreement, nor does it accord with basic economics. As a matter of well-established economic principles, transactions do not have to take place in a regulatory vacuum, if such a marketplace even exists, to be "at arm's length".

35. Second, where the USDOC accepted that transactions were at arm's length, it failed to perform proper market comparisons.

36. Third, neither the original panel nor the Appellate Body restricted the requirement for a pass-through analysis to log transactions where the purchasing sawmills did not hold tenure, and nowhere in the original proceeding or appeal did Canada or the United States argue that a pass-through analysis should be restricted to such transactions.

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[24] *Australia – Salmon (Article 21.5 – Canada)*, Third Participant Submission of the United States, 9 December 1999, at para. 5. (Exhibit CDA-54)

[25] US First Submission and Request for Preliminary Rulings, at paras. 33-34.

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

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

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

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

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

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

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[26] First Written Submission of Canada, at paras. 47-50.
[27] Canada First Submission, at paras. 3-5, 26.
[28] US First Submission and Request for Preliminary Rulings, at para. 33.
[29] Final Section 129 Determination, at 9 (Exhibit CDA-5).
[30] First Written Submission of Canada, at paras. 62-64.
[31] J.P. Kalt and D. Reishus, *Statement for the First Administrative Review*, Attachment 1 to Letter from British Columbia Lumber Trade Council to USDOC (15 March 2004), at 42-43, 48-51, 55 (Exhibit CDA-21); J.P. Kalt and D. Reishus, *Economics of Arms's Length Transactions and Subsidy Pass-Through*, submitted as Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (September 15, 2004), Exhibit BC-PT-39, at 9-10 ["Kalt 2004d"] (Exhibit CDA-20).
[32] Kalt 2004d, at 10.
[33] *Ibid.*, at 4-5.
[34] *Ibid.*, at 6-7.

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

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

43. Moreover, the United States cannot be excused from its obligation to conduct the required pass-through analysis on the pretense that transaction-specific information, which was not reasonably required to perform the analysis, was not available. Given that the investigation and review were conducted on an aggregate basis, it is particularly incongruous for the United States to refuse to consider such information with respect to its pass-through analysis. The Canadian respondents provided all information that was reasonably available, including aggregate information sufficient to conduct the analysis.[36]

B. The USDOC Improperly Relied on Log Import Transactions in Performing Its Pass-Through Analysis

44. In the few instances where the USDOC purported to perform a pass-through analysis, it used benchmarks derived from log import transactions that did not reflect "market" conditions.[37] As the Appellate Body and the original panel made clear, the USDOC was required to establish whether the alleged stumpage subsidy conferred on timber harvesters was passed through the arm's-length log transaction. The section 129 determination benchmarks, however, which included prices for imported logs, were unrepresentative of the timber and market conditions in these provinces for which they were being used.

45. Specifically, the USDOC used extremely small and highly variable log imports relied on to calculate the benchmark for Saskatchewan. For all provinces other than Québec, log import volumes are extremely low, representing only 22.85 per cent of imports into Canada.[38] Accordingly, the use of import prices in benchmarks for Saskatchewan (which accounted for only 0.00175 per cent of imports during the period of investigation) necessarily resulted in the introduction of unrepresentative values. The USDOC did not investigate whether this small volume of imported logs was representative of the Crown harvest, and should not have assumed that it was.

46. Additionally, log import prices are extraordinarily high in value because they typically involve special purchases. The prices are unrepresentative of prices paid for logs used in softwood lumber production. The tariff categories that apply to logs are overly inclusive and capture products used as inputs for high-end applications. Tariff item 4403 of the Canadian *Customs Tariff*, "wood in the rough" is a catch-all category for rough wood items not otherwise specified. Subheading 4403.20 – "other coniferous" – refers to a broad category – coniferous wood in the rough that is untreated.

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[35] Kalt 2004d, at 8-9.

[36] First Written Submission of Canada, at paras. 76, 79.

[37] USDOC Memorandum from Robert Copyak to James Terpstra, *"Pass-Through" Analysis Calculations for the Province of Saskatchewan, 129 Proceeding for the WTO Appellate Body Finding in the Final Countervailing Duty Determination, Certain Softwood Lumber from Canada* (6 December 2004) (Exhibit CDA-59); USDOC Memorandum from Robert Copyak to James Terpstra, *"Pass-Through" Analysis Calculations for the Province of Ontario, 129 Proceeding for the WTO Appellate Body Finding in the Final Countervailing Duty Determination, Certain Softwood Lumber from Canada* (6 December 2004) (Exhibit CDA-60).

[38] Response of the Government of Canada to USDOC's November 24, 2003 Supplemental Remand Questionnaire Response (3 December 2003), at GOC-2 and Exh. GOC-GEN-59 (Exhibit CDA-55).

While the category may include untreated logs, it can also include logs that have been debarked, sawn logs such as roughly squared logs, house logs, pulp logs, round logs for veneer production, tree stumps and roots of special woods, and 'certain growths' for making special furniture veneers or smoking pipes. Many of these products are of higher value and are of a higher price than untreated logs destined, for example, for housing construction and many are not used for lumber production at all.[39] As a result, these import prices did not reflect a "market" price for logs used in softwood lumber production and should not have been used to derive benchmarks.

47. Accordingly, the use by the USDOC of these unrepresentative log import prices in the section 129 determination distorted the results of its limited pass-through analysis.

C. US Arguments Concerning Sawmill-to-Sawmill Transactions Have No Basis in the Findings of Either the Original Panel or the Appellate Body

48. Finally, the United States contends that the recommendations and rulings of the DSB were limited to a particular category of sawmill-to-sawmill transactions, even though no such argument was made by either Canada or the United States during the original proceedings, and neither the original panel nor the Appellate Body made any such distinction.[40] The United States seeks to place tenured sawmills on one side of the transaction, but non-tenured sawmills on the other.[41] The United States, through this limitation, is attempting in yet another creative way to avoid its obligation to conduct the pass-through analysis identified by both the original panel and the Appellate Body under Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreement.

49. The original panel concluded that a pass-through analysis is required for all arm's-length log transactions between unrelated sawmills:

> [T]he USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to unrelated sawmills producing subject softwood lumber … was inconsistent with Article 10 and thus Article 32.1 SCM Agreement, and with Article VI:3 of GATT 1994.[42]

50. The Appellate Body agreed and upheld:

> … the Panel's finding, in paragraph 7.99 of the Panel Report that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *logs* by tenured harvesters/sawmills to unrelated

[39] See also Response of the Government of Alberta to the USDOC's 25 September 2003 Questionnaire (14 October 2003), at AB-17 ("To repeat, it is critical to note that the statistics [used by the Department] ...are for 'wood in the rough,' which would include roughly squared timbers, untreated telephone poles and other such processed wood products and may not include any logs in the round, with bark attached.") (Exhibit CDA-56)l Response of the Government of British Columbia to the USDOC's September 25, 2003 Questionnaire (14 October 2003), at BC-19 (Exhibit CDA-57); and Response of the Gouvernement du Québec to the USDOC's 25 September 2003 Questionnaire (October 14, 2003), at 14 (Exhibit CDA-58).

[40] In footnote 151 of its report, the Appellate Body indicates that the term "sawmill" refers to "an enterprise that processes logs into softwood lumber and does not hold a stumpage contract." Appellate Body Report, at para. 124, fn. 151. The Appellate Body also cites to record evidence on independent harvester transactions Canada provided before the original panel as confirming the existence of arm's-length sales of logs by "… tenured timber harvesters/sawmills to unrelated sawmills not holding stumpage rights …", Appellate Body Report, at para. 150.

[41] First Submission and Request for Preliminary Ruling of the United States, at para. 34.

[42] Panel Report, at para. 7.99.

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

51. The Appellate Body, therefore, upheld the conclusions of the original panel that a pass-through analysis was required for all arm's-length log transactions between sawmills. There is no qualifier in the Appellate Body's decision that purchasing sawmills must be "non-tenured", and there is no such qualifier in the original panel decision that it upheld. There would be no legal or economic reason to restrict the requirement to conduct a pass-through analysis to purchasing sawmills without tenure, and had the Appellate Body intended to restrict the scope of its ruling in this manner, it would have done so explicitly.

52. Whether the purchasing sawmill holds or does not hold stumpage rights is irrelevant to the Appellate Body's reasoning. The crux of the Appellate Body's reasoning relates to the fact that the transaction concerns an input product (*i.e.*, a log). Where a lumber producer sources its log input other than from its own timber harvesting and *log production*, the receipt of an alleged stumpage subsidy is necessarily indirect and requires pass-through analysis before it may be countervailed as an alleged subsidy to *lumber production*.[44] The Appellate Body did not condition its conclusion on circumstances concerning the purchasing sawmills.

II. CONCLUSION

53. Canada requests that the Panel determine the final results of the first administrative review are within the jurisdiction of the Panel under Article 21.5 of the DSU. Canada also requests the Panel to reject as unfounded the claims made by the United States in its first written submission.

[43] Appellate Body Report, at para. 167(e) [italics in original].
[44] Appellate Body Report, at paras. 146-47, 156-59.

TABLE OF EXHIBITS

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ANNEX A-3

ORAL STATEMENT OF CANADA

21 April 2005

I. INTRODUCTION

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

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

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

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

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

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

7. The United States' purported compliance measure took effect on 10 December 2004. But then, three days later, the United States issued another determination covering the same products over the same period. In this new determination, which was made pursuant to the United States' administrative review process, the United States definitively set the countervailing duties for the softwood lumber covered by the DSB's ruling using the same flawed that it used reasoning in its section 129 determination. Yet this time it conducted no pass-through analysis at all, not even the extremely circumscribed analysis of the section 129 determination.

8. This administrative review determination took effect on December 20, 2004 and superseded the section 129 determination. That is, the section 129 determination ceased to be effective after just ten days, and just three days after the United States informed the DSB that it had complied with its recommendations and rulings by properly conducting a pass-through analysis.

9. In sum, the United States' section 129 determination did not redress its non-compliance with its obligations under the GATT and the SCM Agreement. Moreover, to the extent that it even partially complied with these obligations, it rendered that limited compliance non-existent by the administrative review.

10. Despite this, the United States continues to insist that it has complied with the recommendations and rulings of the DSB. It insists, as well, that its administrative review determination is not properly before this panel, regardless of how that determination has undone even the United States' purported compliance measure in this case, the section 129 determination.

11. Canada's response to the United States' request for a preliminary ruling has addressed why the administrative review determination is properly within the scope of your review. The third party submission of the European Communities reaches the same conclusion. So too does the third party submission of China, although it takes a different path to get there. In Canada's view, this issue is crucial, as it goes directly to the ability of the United States to impose a non-compliant measure while relying on its domestic anti-dumping and countervail regime to evade its WTO obligations. Canada will be pleased to take questions on this matter, but because it has been thoroughly canvassed in previous submissions and in the third party submissions, Canada will not take up time today with further affirmative argument on it.

12. Canada will focus today on the assertions made by the United States in its second written submission. First, Mr. Cochlin will explain why the US presumption of pass-through is contrary to its obligations under the GATT and the SCM Agreement and why the threshold test the United States has devised is both incorrect and unfounded. Then, Mr. Owen will explain that the United States had all the available information it required to perform the pass-through analysis mandated by the DSB's ruling, and how Canada nevertheless made considerable efforts to comply with the unreasonable and irrelevant US demands for additional information.

II. COMMERCE CONTINUED TO PRESUME, RATHER THAN DEMONSTRATE, INDIRECT SUBSIDIZATION

13. Mr. Chairman, Members of the Panel, the central question in dispute before you is this: did the United States continue to *presume* the pass-through of alleged stumpage subsidies in violation of Article VI:3 of the GATT and Articles 10 and 32.1 of the SCM Agreement?

14. Contrary to the numerous, repeated assertions by the United States, a presumption of pass-through is exactly what the United States Department of Commerce ("Commerce") applied where it, first, rejected transactions based on its contrived "arm's-length" threshold test; second, refused to

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

15. The issue of "pass-through" arises in this case because, in many instances, sawmills could have only received the alleged stumpage subsidy *indirectly* – through purchases of Crown log inputs from unrelated harvesters or other sawmills. Indirect subsidization of softwood lumber production therefore would occur only if the input subsidy "passed through" from the log seller to the purchasing sawmill.

16. Both the original panel and the Appellate Body made clear that Commerce is required to demonstrate – and not presume – such alleged indirect subsidization before it could lawfully impose countervailing duties under Article VI:3 of the GATT and Articles 10 and 32.1 of the SCM Agreement.[1] Commerce must demonstrate that the alleged direct subsidy to *log* production passes through and becomes an indirect subsidy to *lumber* production. Such analysis involves demonstrating, by making appropriate market comparisons, that the purchasing sawmills received a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

17. The United States does not contest that it has an obligation to conduct a pass-through analysis in this case.[2] Indeed, for a small fraction of the log transactions identified in its section 129 determination, Commerce compared log prices to market benchmarks to demonstrate the existence and amount of a pass-through.[3] In most respects, Canada does not contest this limited analysis.

18. However, for the vast majority of log transactions covered by its section 129 determination, and for all transactions covered by its administrative review results, Commerce performed no such analysis. Instead, it attempted at every turn to avoid the obligation to demonstrate a pass-through.

19. For all log volumes rejected by Commerce, it presumed, rather than demonstrated, a pass-through. It deemed – without proof or analysis – that the alleged subsidy to the upstream log producer *automatically* becomes a subsidy to the unrelated downstream purchasing sawmill.

20. The United States goes to great lengths to divert the Panel's attention from Commerce's presumption of a pass-through.[4] It wants the Panel to believe that it is operating within its discretion, and that it is aggressively trying to meet its pass-through obligations. The fact remains, however, that without having done pass-through analyses and without having employed a presumption, Commerce would have been required to limit its numerator to only Crown timber going *directly* to softwood lumber production. As the United States explains, however, Commerce instead established the numerator of its subsidy calculation by requesting and using the total volume of all harvested Crown timber entering sawmills either directly *or indirectly*.[5]

III. COMMERCE APPLIED A CONTRIVED "ARM'S LENGTH" TEST TO AVOID PERFORMING THE REQUIRED PASS-THROUGH ANALYSES

21. The primary way in which Commerce avoided having to perform a pass-through analysis was by devising a novel test for determining whether a transaction was at arm's length. The United States no longer claims that it had no obligation to conduct any pass-through analysis at all, as it did in the original proceedings. It now claims, instead, that the obligation only arises where Canada can demonstrate that a transaction has occurred not only between unrelated parties, but also outside any

[1] First Written Submission of Canada, at paras. 41-50.
[2] Second Written Submission of the United States, at para. 35-36.
[3] *Ibid.*, at para. 39.
[4] *Ibid.*, at paras. 15, 40-42.
[5] *Ibid.*, at paras. 7 and 9, footnote 12.

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

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

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

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

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

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

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

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

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

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

30. Similarly, a barter arrangement in the form of a fibre exchange agreement merely provides that the buyer is paying the consideration owed to the seller in goods rather than in cash. Indeed, barter is perhaps the oldest form of market transaction. This factor is irrelevant to determining whether the seller is able to extract from the buyer the value of what the seller provides, and hence whether any subsidy has passed through.

31. Second, with respect to Commerce's "log purchase agreement" factor, the United States in its rebuttal submission cites various possible contractual arrangements to explain Commerce's failure to conduct a pass-through analysis.[17] These contractual terms are part of the agreed structure of a transaction between unrelated parties, and as Canada has explained, simply reflect the results of the bargain reached.[18]

32. Finally, Canada explained that provincial regulations imposing "limitations on log sales" and "wood supply agreements"[19] do not dictate the material terms of the log sale agreement, such as price, delivery arrangements, or timing. A regulatory vacuum is not a prerequisite for arm's-length transactions.[20] Were it so, no sale could ever be found to be at arm's-length.

33. By way of conclusion to this section, we note that the United States to date has offered no justification regarding Commerce's presumption of a pass-through for all transactions in the administrative review; it argues only that the measure is not properly before the Panel.[21] Accordingly, up to this point, the United States here has essentially conceded that the failure by Commerce to perform a pass-through analysis in the administrative review was inconsistent with US obligations.

[14] Second Written Submission of the United States, at para. 22, footnote 29, and at para. 23.
[15] First Written Submission of Canada, para. at 64; Rebuttal Submission of Canada, at para. 41.
[16] Second Written Submission of the United States, at para. 23.
[17] *Ibid.*, at para. 22.
[18] First Written Submission of Canada, at paras. 64; Rebuttal Submission of Canada, at para. 42.
[19] Second Written Submission of the United States, at para. 21.
[20] First Written Submission of Canada, at paras. 64; Rebuttal Submission of Canada, at para. 40.
[21] Second Written Submission of the United States, at paras. 46-47.

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

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

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

36. As justification here, the United States claims that the Appellate Body reversed, rather than upheld, the original panel's conclusion in paragraph 7.99 of its report.[22] Allow me to quote directly from paragraph 7.99:

> "[T]he USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to unrelated sawmills producing subject softwood lumber… was inconsistent with Article 10 and thus Article 32.1 SCM Agreement, and with Article VI:3 of GATT 1994."

37. The original panel's conclusion covers transactions where the purchasing sawmills held tenure. There is no reversal of this conclusion in the Appellate Body's report; to the contrary, there are pages of reasoning in support.[23]

38. In an attempt to explain Commerce's exclusion of these transactions, the United States offers only that, "tenure-holding sawmills are direct subsidy recipients".[24] This statement fails entirely to explain how the alleged stumpage subsidy passes from upstream timber harvesters to downstream purchasing sawmills. Commerce simply presumed the pass-through.

39. The only other reason the United States offers for Commerce's refusal to conduct the required analysis is that the Canadian respondents failed to provide necessary data. As my colleague Mr. Owen will now explain, the US claims in this respect are false, and the Canadian respondents provided more than sufficient evidence to allow Commerce to conduct a pass-through analysis in both determinations.

V. THE RECORD EVIDENCE WAS SUFFICIENT TO PERFORM A PROPER PASS-THROUGH ANALYSIS

A. The Canadian Respondents Provided All Available Evidence Necessary for Commerce to Perform a Pass-Through Analysis

40. Mr. Chairman, Members of the Panel, the United States complains that Canada failed to provide the necessary data to allow Commerce to conduct a pass-through analysis and is, in fact, "attempting to restrict" its ability to conduct such an analysis.[25]

41. These assertions are patently false. Commerce had everything it needed and more to conduct a pass-through analysis.[26] The Canadian respondents provided pricing data that was representative of the arm's-length transactions in these provinces and was more than sufficient to conduct a pass-

[22] *Ibid.*, at para. 44.
[23] Rebuttal Submission of Canada, at paras. 51-52.
[24] Second Written Submission of the United States, at para. 44.
[25] *Ibid.*, at paras. 14, 32.
[26] *See* First Written Submission of Canada, at para. 58.

through analysis. Commerce should have used this information to calculate the amount of pass-through applicable to the entire volume of arm's-length transactions for each province.

42. Allow me to briefly outline this information.

43. British Columbia provided Commerce with the name of the seller, volume, value, and species information for each of the more than 3,000 arm's-length purchases by sawmills that accounted for 53 per cent of the Crown harvest in that province.[27] In addition, for these same sawmills, British Columbia provided equally detailed information on more than 2,500 arm's-length transactions involving logs harvested from private lands.[28] These data could have been used to calculate the amount of pass-through for these transactions and an average amount of pass-through for the remaining arm's-length volumes in this province. Instead, Commerce ignored all of these data.

44. Alberta had PricewaterhouseCoopers compile transaction-specific pricing data for approximately 80 per cent of arm's-length transactions for which it claimed a pass-through analysis.[29] Commerce relied on these transaction-specific data to calculate its pass-through adjustment. It failed, however, to use these pricing data to calculate the average pass-through of subsidies – if any – for the remaining volumes of arm's-length transactions.

45. Saskatchewan and Manitoba both provided extensive transaction-specific pricing data. More specifically, Saskatchewan requested Weyerhaeuser – its largest softwood lumber producer – to provide their data. Weyerhaeuser was involved in approximately 40 per cent of independent harvester transactions in this province.[30] Similarly, Manitoba provided Commerce with transaction-specific information from Tembec, an independent harvester which was involved in 51 per cent of the arm's-length transactions in that province.[31]

46. Ontario provided company-specific data relating to sawmills responsible for 91.3 per cent of the Crown harvest.[32] The Ontario industry associations also provided Commerce with transaction-specific information for two of the largest independent harvesters and 23 of the largest sawmills in that province. In fact, Commerce received transaction-specific pricing data from companies accounting for over 90 per cent of the Crown harvest entering sawmills during the period of investigation.[33]

47. In short, Canadian respondents provided Commerce with transaction-specific information for the majority of transactions between independent harvesters and sawmills in most provinces. In addition, Ontario provided company- or sawmill-specific data. Commerce, therefore, had more than enough information to conduct pass-through analyses.

48. No pricing data was requested by Commerce in the administrative review.[34] Moreover, the Canadian respondents had no opportunity to present this information, as Commerce did not request this evidence in the section 129 proceeding until after closure of the factual record in the administrative review. Commerce is now requesting this transaction-specific information in its second administrative review.

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[27] First Written Submission of Canada, at para. 80.
[28] *Ibid.*
[29] *Ibid.*, at para. 81.
[30] *Ibid.*, at para. 83.
[31] *Ibid.*, at fn 96.
[32] *Ibid.*, at para. 87.
[33] *Ibid.*
[34] *Ibid.*, at para. 77.

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

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

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

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

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

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

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

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

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

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

[38] *Ibid.*

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

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

VI. CONCLUSION

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

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

58. Canada therefore requests that the Panel:

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

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

- *Suggest*, in accordance with Article 19.1 of the DSU, that the United States do one of the following two things:

    - It should refund the amount of the countervailing duties it imposed to offset alleged subsidy amounts impermissibly presumed to pass through;

    or

    - It should revise its measures to meet its WTO obligations *and* refund the amount of the countervailing duties it imposed to the extent that they exceeded the amount of the alleged subsidy demonstrated to have passed through to the production of softwood lumber.

ANNEX B

Submissions of the United States

ANNEX B-1

FIRST SUBMISSION AND REQUEST FOR PRELIMINARY RULING OF THE UNITED STATES

10 March 2005

I. Introduction

1. On 6 December 2004, the US Department of Commerce ("Commerce") issued a revised determination ("Section 129 Determination")[1] that implemented the recommendations and rulings of the Dispute Settlement Body ("DSB") in *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber From Canada*.[2] The recommendations and rulings of the DSB at issue relate to Commerce's decision not to conduct a pass-through analysis with respect to certain arm's-length sales of logs in its Final Determination.[3]

2. As discussed further below, Commerce's Section 129 Determination fully implements the recommendations and rulings of the DSB, and is consistent with the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") and the *General Agreement on Tariffs and Trade 1994* ("GATT 1994"). The Panel should find, therefore, that Canada's claims are unfounded.

3. In addition, as set out below, the United States requests a preliminary ruling that the final results of the first assessment review[4] of the countervailing duty order on softwood lumber from Canada, cited by Canada in its request for the establishment of a panel[5], are not "measures taken to comply" with the recommendations and rulings of the DSB under Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU"). Therefore, these results fall outside the scope of Article 21.5, and this Panel lacks jurisdiction to review them.

4. As provided for in the Panel's working procedures, the United States will be providing a rebuttal submission on 31 March 2005.

II. Procedural History

5. On 2 April 2002, Commerce published the Final Determination, finding that provincial stumpage programmes in Canada provided a countervailable subsidy to Canadian lumber producers

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[1] *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*, December 6, 2004 ("Section 129 Determination") (Exhibit CDA-5). "Section 129" refers to the provision of the Uruguay Round Agreements Act that provides procedures for implementing certain DSB recommendations and rulings with respect to countervailing duty investigations.

[2] Appellate Body Report, WT/DS257/AB/R, adopted 17 February 2004, ("Appellate Body Report"); Panel Report, WT/DS257/R, adopted 17 February 2004 ("Panel Report").

[3] *Notice of Final Affirmative Countervailing Duty Determination and Final Negative Critical Circumstances Determination: Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 15545 (2 April 2002), as amended, 67 Fed. Reg. 36070 (May 22, 2002) ("Final Determination"). Exhibit US-1.

[4] An "administrative review", in US parlance.

[5] WT/DS257/15, citing *Notice of Final Results of Countervailing Duty Administrative Review and Recission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce December 20, 2004) (Exhibit CDA-8) and *Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*, December 13, 2004.

and that certain non-stumpage programmes provided countervailable subsidies.[6] Commerce did not conduct a pass-through analysis in the Final Determination.

6. On 3 May 2002, Canada requested consultations with the United States and thereafter the DSB established a panel pursuant to Article 6 of the DSU ("original panel").

7. On 29 August 2003, the original panel found that Commerce's failure to conduct a pass-through analysis in the Final Determination with respect to arm's-length sales to unrelated sawmills and lumber remanufacturers was inconsistent with Articles 10 and 32.1of the SCM Agreement and Article VI:3 of the GATT 1994[7] However, the Appellate Body in its 19 January 2004, report reversed that aspect of the original panel report relating to Commerce's decision in its investigation not to conduct a pass-through analysis in respect of arm's-length sales of lumber by tenured harvesters/sawmills to remanufacturers[8]

8. The Appellate Body upheld, however, the original panel's finding that Commerce acted inconsistently with the SCM Agreement and GATT 1994 by failing in the Final Determination to conduct a pass-through analysis in respect of arm's-length sales of logs by tenured harvesters/sawmills to unrelated sawmills.[9] On 17 February 2004, the DSB adopted its recommendations and rulings.[10]

9. On 5 March 2004, the United States notified the DSB of its intention to implement the recommendations and rulings of the DSB.[11] Thereafter, the United States and Canada established a ten-month "reasonable period of time" ending 17 December 2004, within which the United States agreed to implement the recommendations and rulings of the DSB.[12]

10. On 19 November 2004, Commerce issued a draft Section 129 Determination and provided an opportunity for parties to comment. On 6 December 2004, Commerce issued the Section 129 Determination, which revised the original countervailing duty investigation determination and implemented the DSB's recommendations and rulings, effective for imports on or after 10 December 2004. On 16 December 2004, the notice of implementation was published in the Federal Register.[13]

11. On 17 December 2004, the United States informed the DSB that it had complied with the DSB's recommendations and rulings by properly conducting its pass-through analyses of certain arm's-length log sales occurring during the period of investigation ("POI").

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[6] The Final Determination subsequently was amended on May 22, 2002.

[7] Panel Report, para. 7.99.

[8] Appellate Body Report, para. 167(f). The United States did not appeal the Panel's findings with respect to arm's-length log sales between tenured timber harvesters not owning sawmills and sawmills. Appellate Body Report, fn. 157.

[9] The other issues either appealed by the United States or Canada were decided in favor of the United States. Appellate Body Report, para. 167.

[10] DSB, Minutes of Meeting (17 February and 19 March, 2004), WT/DSB/M/165, 30 March 2004, at 4(a), para. 49.

[11] WT/DS257/12, 9 March 2004.

[12] WT/DS257/13, 30 April 2004.

[13] *Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products From Canada*, 69 FR 75305 (16 December 2004). Exhibit CDA-7.

III. Preliminary Ruling Request with Respect to the Final Results of the First Assessment Review

12. The United States requests a preliminary ruling that the final results of the first assessment review of the countervailing duty order on softwood lumber from Canada, cited by Canada in its request for the establishment of a panel in this dispute[14], are not "measures taken to comply" with the recommendations and rulings of the DSB under Article 21.5 of the DSU. Therefore, these results fall outside the scope of Article 21.5, and this Panel lacks jurisdiction to review them.

A. Article 21.5 Proceedings are Limited to "Measures Taken to Comply" With the DSB's Recommendations and Rulings

13. The subject matter of these proceedings is determined by the Panel's terms of reference and by Article 21.5 of the DSU, which provides that recourse be had to dispute settlement procedures "[w]here there is disagreement as to the existence or consistency with a covered agreement *of measures taken to comply with the recommendations and rulings*." (emphasis added). Therefore, as the Appellate Body has stated, "[p]roceedings under Article 21.5 do not concern just *any* measure of a Member of the WTO; rather Article 21.5 proceedings are limited to those 'measures *taken to comply* with the recommendations and rulings' of the DSB.[15]

14. Although the complaining party in an Article 21.5 proceeding decides the scope of its request for panel establishment, including the measures it wishes to challenge, it is the responsibility of the Article 21.5 panel to determine whether the measure identified is or is not a "measure[ ] taken to comply".[16] If it is not, the measure falls outside of Article 21.5, and the panel lacks jurisdiction to review the measure. As the panel in *EC – Bed Linens* stated, it is neither the complaining nor the responding party that decides which measures are taken to comply: "Rather", said the panel, "this is an issue which must be considered and decided by an Article 21.5 panel".[17] That panel concluded that "[t]o the extent a party may have challenged, in a request for establishment of an Article 21.5 panel, measures which were not 'taken to comply' by the implementing Member, it is our view that a Panel may decline to address claims concerning such measures".[18]

15. And, indeed, in the *EC – Bed Linens* dispute, the panel granted the EC's preliminary ruling request to exclude from consideration certain antidumping duty measures taken by the EC that were cited by India, but that the panel found were not "taken to comply". In that dispute, in which the EC was found to have incorrectly calculated dumping duties in an investigation of bed linens from India, the EC voluntarily applied the revised calculation method to antidumping duties imposed on Pakistan and Egypt. After concluding that no duties should be imposed on bed linens from those sources (as a result of the recalculation), the EC re-examined whether imports from India, considered alone, caused injury to the domestic industry. The EC concluded that they did, and therefore affirmed the imposition of dumping duties on bed linen from India. India challenged this finding of injury and the resulting imposition of duties on bed linen from India as a WTO-inconsistent measure "taken to comply" under Article 21.5.

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[14] WT/DS257/15, citing *Notice of Final Results of Countervailing Duty Administrative Review and Recission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce 20 December 2004) (Exhibit CDA-8) and *Issues and Decision Memorandum: Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*, 13 December 2004.

[15] Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, para. 36.

[16] *See, e.g.*, Panel Report, *European Communities - Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India - Recourse to Article 21.5 of the DSU by India*, WT/DS141/RW, adopted 24 April 2003, as modified by the Appellate Body Report, WT/DS141/AB/RW, ("*EC – Bed Linens (Panel)"*), para. 6.15.

[17] *EC – Bed Linens* (Panel), para. 6.15.

[18] *EC – Bed Linens* (Panel), para. 6.17 (emphasis in original).

16. The panel, in deciding not to review the latter measure, stated that

> [T]he fact that the EC, subsequent to its re-examination of the dumping determinations with respect to imports from Egypt and Pakistan, and in the context of a review initiated on the request of Eurocoton, carried out an analysis of whether injury was caused by imports from India alone does not, *ipso facto*, establish that Regulation 696/2002 is a measure "taken to comply". Rather the opposite would seem to be the case – that Regulation would seem to be an entirely new determination, reached as a result of events subsequent to the EC having adopted a measure to comply with the DSB's recommendation.[19]

17. In sum, Article 21.5 proceedings are limited to "measures taken to comply" with the DSB's recommendations and rulings. As discussed below, the final results of the first assessment review are not "measures taken to comply" and therefore this Panel should decline to review those results.

B. The Final Results of the First Assessment Review Are Not "Measures Taken to Comply"

18. As discussed above, before the original panel, Canada challenged Commerce's Final Determination in the countervailing duty *investigation* on softwood lumber from Canada.[20] After the DSB adopted its recommendations and rulings, and within the agreed "reasonable period of time", the United States made a redetermination – the Section 129 Determination – in which it conducted a "pass through" analysis and recalculated the countervailing duty rate.[21] The new reduced rate was applicable to entries of subject merchandise on or after 10 December 2004.[22]

19. In this Article 21.5 dispute, Canada states that the Section 129 Determination is a "measure[ ] taken to comply with the recommendations and rulings" of the DSB and alleges that it fails to implement the recommendations and rulings of the DSB.

20. But Canada also includes, without explanation, a completely separate Commerce determination, *i.e.*, the results of an *assessment review*, among the "measures taken to comply" which it asks the Panel to examine under Article 21.5. The results of this assessment review are, in no sense, "measures taken to comply" with the recommendations and rulings of the DSB concerning the Final Determination in the original countervailing duty investigation.

21. As an initial matter, original investigations and assessment reviews are different processes which serve distinct purposes. The purpose of an investigation is to determine the existence, degree, and effect of any alleged subsidy; the purpose of an assessment review is to determine the amount of duty to be assessed on previous imports of subject merchandise and the estimated countervailing duty rate to be applied to future imports. Indeed, the distinction between countervailing duty investigations and assessment procedures is explicitly recognized in the SCM Agreement.[23]

22. In May 2003, Canada (among other interested parties) requested such an assessment review, covering entries of subject merchandise during the period 22 May 2002, through 31 March 2003. The resulting assessment review was not taken to comply with the recommendations and rulings of the

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[19] *EC – Bed Linens* (Panel), para. 6.20 (emphasis added).

[20] Panel Report, paras 2.1-2.4.

[21] Section 129 Determination. Exhibit CDA-5.

[22] *Notice of Implementation under Section 129 of the Uruguay Round Agreements Act: Countervailing Measures concerning Certain Softwood Lumber from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce 16 December 2004). Exhibit CDA-7.

[23] *See, e.g.*, SCM Agreement, fn. 52.

DSB. Rather, it resulted from a *separate* affirmative request by Canada, among others, that Commerce review *new* sales and subsidies data for the purposes of assessing countervailing duties for imports during the review period and of setting a new estimated countervailing duty rate for subsequent imports. US law required Commerce to conduct this assessment review once Canada, among others, requested it.[24]

23. Indeed, the assessment review was initiated on 1 July 2003, *eight months* before the recommendations and rulings in this dispute were adopted. This review proceeding, therefore, had nothing whatsoever to do with "implementing" the DSB's recommendations and rulings. For obvious temporal reasons, the results of this assessment review – which was initiated before the DSB issued its recommendations and rulings – cannot be considered "measures taken to comply".

24. Article 21.5 proceedings are by their nature more focused and limited than other panel proceedings under Article 6.2 of the DSU. Notably, instead of six months, the DSU anticipates that Article 21.5 proceedings will normally take no more than 90 days.[25] Canada, for its part, has underscored this aspect of these proceedings by systematically opposing any extensions of time in this proceeding.[26] For this reason, Article 21.5 proceedings are intended to focus, not on *any* measure cited by the complaining Member – as is the case for other dispute settlement proceedings – but only on *measures taken to comply* with DSB recommendations and rulings. It is beyond the scope of such a limited 90-day inquiry to fully examine an entirely new set of assessment review results based on a wholly new administrative record, consisting of new sales, new imports, potentially new respondents and potentially new subsidy programmes.

25. In sum, in this Article 21.5 proceeding, the Panel lacks jurisdiction to review the final results of the assessment review cited by Canada because these results are not "measures taken to comply" with the DSB's recommendations and rulings, adopted on 17 February 2004, related to Commerce's Final Determination in the original countervailing duty investigation.

IV. Canada Bears the Burden of Proving its Claims

26. It is well-established that the complaining party in a WTO dispute bears the burden of coming forward with argument and evidence that establish a *prima facie* case of a WTO inconsistency.[27] If the balance of evidence and argument is inconclusive with respect to a particular claim, Canada, as the complaining party, must be found to have failed to establish that claim.[28] Canada has not met its burden in this proceeding.

27. With respect to the standard of review, Article 11 of the DSU sets forth the standard of review for this Panel. Article 11 calls for panels to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements ... ."

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[24] *See* 19 USC 1675(a). Exhibit US-2.

[25] *Compare* Articles 12.8 and 21.5 of the DSU.

[26] Recall, *e.g.*, statements by the Canadian representative during the Panel organization meeting of 14 February 2005, as well as paragraph 2 of Canada's letter of 15 February 2005, to the Panel regarding its draft working procedures and timetable.

[27] *See, e.g.*, Appellate Body Report, *United States – Measures Affecting Imports of Woven Shirts and Blouses from India*, WT/DS33/AB/R, adopted 23 May 1997, page 14; Appellate Body Report, *European Communities – Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, para. 104; and Panel Report, *Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products*, WT/DS98/R, as modified by the Appellate Body, adopted 12 January 2000, para. 7.24.

[28] *See, e.g.*, Panel Report, *India – Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*, WT/DS90/R, as affirmed by the Appellate Body, adopted 22 September 1999, para. 5.120.

28. With respect to disputes involving a determination made by a domestic authority based upon an administrative record, the Appellate Body, in *Cotton Yarn*, summarized the role of a panel under Article 11 as follows:

> [P]anels must examine whether the competent authority has evaluated all relevant factors; they must assess whether the competent authority has examined all the pertinent facts and assess whether an adequate explanation has been provided as to how those facts support the determination; and they must also consider whether the competent authority's explanation addresses fully the nature and complexities of the data and responds to other plausible interpretations of the data. However, panels must not conduct a *de novo* review of the evidence nor substitute their judgement for that of the competent authority.[29]

29. Thus, the Panel's task is to determine whether a reasonable, unbiased person, looking at the same evidentiary record as Commerce, could have – not would have – reached the same conclusions.

V. Commerce Conducted a Pass-Through Analysis Consistent with the SCM Agreement, the GATT 1994, and the DSB's Recommendations and Rulings

30. As described in detail in the Section 129 Determination, Commerce responded to the DSB's recommendations and rulings by conducting a pass-through analysis, first issuing questionnaires seeking record evidence to determine whether during the period of investigation there were arm's-length sales of logs by independent harvesters to unrelated sawmills and by tenured harvesters/sawmills to unrelated sawmills. Based upon its analysis of the record evidence, Commerce determined that there were such arm's-length log sales. For those arm's-length sales, Commerce then determined whether a benefit was passed through to the purchasing sawmills, using appropriate benchmarks, and removed from the numerator of the aggregate subsidy calculation any benefit that it found did not pass through to the purchasing sawmills.

31. Other sales, however, were determined not to be at arm's length, either because the record facts demonstrated that they were not or because Canada failed to provide sufficient record evidence that would have enabled Commerce to analyze those sales. Ultimately, Commerce's analysis of log sales demonstrated to be at arm's length resulted in a C$28,344,121 reduction in the numerator of the *ad valorem* subsidy rate, which had the effect of reducing the country-wide subsidy rate from 18.79 per cent *ad valorem* to 18.62 per cent *ad valorem*.[30]

32. Canada now challenges Commerce's Section 129 Determination under Article 21.5 of the DSU. This challenge, however, has no basis in the SCM Agreement, the GATT 1994, or the recommendations and rulings of the DSB. Commerce's pass-through analysis was conducted in accordance with the recommendations and rulings of the DSB and is WTO-consistent, and Canada's claims must therefore fail.

33. First, Commerce did not "presume" pass-through. To implement the DSB's recommendations and rulings, Commerce sought data from Canada substantiating its claims that subsidies were not passed through. In some instances, the Canadian respondents provided the requested data and Commerce conducted the recommended analysis, using appropriate log prices as benchmarks. In other instances, however, despite repeated requests by Commerce, Canada failed to provide the necessary data. Lacking sufficient data, Commerce was not able to conduct its analysis for all of the log sales for which Canada requested such an analysis.[31]

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[29] Appellate Body Report, *United States – Transitional Safeguard Measure on Combed Cotton Yarn from Pakistan*, WT/DS192/AB/R, adopted 5 November 2001, para. 74.

[30] *Section 129 Determination, at 1. Exhibit CDA-5.*

[31] *E.g.*, Section 129 Determination, at 3 and 13 (comment 8).

34. Second, Commerce properly investigated and made a determination concerning whether particular sales were at "arm' s length." Contrary to Canada's arguments[32], nothing in the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings supports Canada's argument that an arm's-length analysis should be restricted to, in essence, a *per se* test based on affiliation alone. Further, part of the DSB's recommendations and rulings related only to a particular category of arm's-length log sales: those between tenured harvester/sawmills and unrelated, non-tenured sawmills.[33] The scope of the DSB' s recommendations and rulings should therefore not be broadened to include entities that were not part of those recommendations and rulings.

35. Finally, the results of Commerce's recalculation were applied to the only rate that was before the original panel and Appellate Body, *i.e.*, the 18.79 per cent *ad valorem* rate calculated in the Final Determination. Therefore, Canada's argument that Commerce applied the results of its pass-through analysis to a rate "which long before had been invalidated as a result of judicial review proceedings"[34] is without basis.

VII. Conclusion

36. For the reasons stated above, Canada's claims against US implementation of the DSB's recommendations and rulings have no basis in the SCM Agreement, the GATT 1994, or the recommendations and rulings of the DSB. The United States therefore requests that the Panel find that the United States properly implemented the recommendations and rulings of the DSB and that the Panel reject Canada's claims in their entirety. Further, the United States requests that this Panel find that the results of the first assessment review fall outside the Panel's jurisdiction in this Article 21.5 dispute.

[32] *E.g.*, First Written Submission of Canada, paras. 59 -65.
[33] *E.g.*, Appellate Body Report, para. 167(e).
[34] First Written Submission of Canada, para. 10.

ANNEX B-2

SECOND WRITTEN SUBMISSION OF THE UNITED STATES

31 March 2005

I. Introduction

1. On 10 March 2005, the United States filed its First Submission and Request for Preliminary Ruling. Pursuant to the Panel's working procedures, the United States is now filing its rebuttal submission.

2. To implement the recommendations and rulings of the Dispute Settlement Body ("DSB") in *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber From Canada*[1],, on 6 December 2004, the US Department of Commerce ("Commerce") issued a revised determination ("Section 129 Determination").[2] In accordance with those recommendations and rulings, in the context of its Final Determination[3], Commerce determined the amount of the subsidy that passed through the purchase transaction with respect to certain arm's-length log sales between unrelated parties. Ultimately, Commerce's analysis of log sales demonstrated to be at arm's length resulted in a C$28,344,121 reduction in the numerator of the *ad valorem* subsidy rate, which had the effect of reducing the country-wide subsidy rate from 18.79 per cent *ad valorem* to 18.62 per cent *ad valorem*.[4] Commerce's Section 129 Determination is consistent with the DSB's recommendations and rulings, the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") and the *General Agreement on Tariffs and Trade 1994* ("GATT 1994"), and the Panel should so find.

3. In this proceeding, however, Canada is asking the Panel to find that the United States is subject to conditions and restrictions that are nowhere to be found in the SCM Agreement or GATT 1994, that were not part of the DSB's recommendations and rulings, and that are entirely otherwise unwarranted. In so doing, Canada attempts to deflect attention away from its own failure in many instances to provide Commerce with the data necessary to conduct the analysis recommended by the DSB. Neither Canada' s attempt to prevent Commerce from conducting a meaningful pass-through analysis, nor its failure to provide the requested data, however, translates into a failure by the

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[1] Appellate Body Report, WT/DS257/AB/R, adopted 17 February 2004, ("Appellate Body Report"); Panel Report, WT/DS257/R, adopted 17 February 2004 ("Panel Report").

[2] *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*, 6 December 2004 ("Section 129 Determination") (Exhibit CDA-5). The Section 129 Determination was implemented on 10 December 2005, at the request of the Office of the United States Trade Representative. *See Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products From Canada*, 69 FR 75305 (16 ecember 2004). Exhibit CDA-7. For summaries of provincial claims and the results of Commerce's pass-through determination, *see* "Draft Decision Memorandum" In the Matter of the Section 129 Determination on the Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada ("Draft Section 129 Determination"), 19 November 2005, at 8-15 (Exhibit CDA-6). Any modifications to Commerce's analysis are discussed in the Comment section of the Section 129 Determination. "Section 129" refers to the provision of the Uruguay Round Agreements Act that provides procedures for implementing certain DSB recommendations and rulings with respect to countervailing duty investigations.

[3] *Notice of Final Affirmative Countervailing Duty Determination and Final Negative Critical Circumstances Determination: Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 15545 (2 April 2002), as amended, 67 Fed. Reg. 36070 (May 22, 2002) ("Final Determination"). Exhibit US-1.

[4] Section 129 Determination, at 1. Exhibit CDA-5.

United States to comply with the DSB's recommendations and rulings or results in a measure that is inconsistent with the SCM Agreement or the GATT 1994.

4. As described below, and contrary to Canada's arguments, Commerce conducted its pass-through analysis consistently with the DSB's recommendations and rulings, and the resulting measure at issue is consistent with the SCM Agreement and the GATT 1994.

II. Commerce Conducted a Pass-Through Analysis That is Consistent with the DSB's Recommendations and Rulings and with the SCM Agreement and GATT 1994

5. Canada does not challenge Commerce's general approach of reducing the numerator of the *ad valorem* subsidy rate calculation to eliminate subsidies attributed to arm's-length sales in which no benefit was passed through. Instead, Canada complains that Commerce, rather than conducting a pass-through analysis, "presumed" pass through. A foundation of Canada's "presumption" argument is its assertion that Commerce must adopt an unreasonable definition of the term "arm's length"[5] that would prevent Commerce from conducting a meaningful analysis of whether, in fact, sales are at arm's length. Consequently, whenever Commerce determined that a transaction was not at arm's length, according to Canada's unreasonable definition of arm's length, Commerce improperly "presumed" pass-through of the subsidy. Additionally, Canada argues that Commerce "presumed" pass-through by disregarding aggregate data submitted by Canada[6] and excluding from its analysis sales between tenure-holding sawmills.[7] In making its arguments Canada ignores the necessarily company-specific nature of the analysis undertaken by Commerce and the actual findings of the DSB, including the specific definitions of the categories of companies for which a pass-through analysis had to be performed. As set forth below, Commerce properly conducted its pass-through analysis.

A. Commerce Issued Questionnaires to Obtain Data Necessary to its Analysis

6. To conduct its pass-through analysis, Commerce first had to obtain data from Canada[8] supporting Canada's claim that a portion of the total volume of Crown logs processed into lumber – as reported by Canada – should be reduced to account for arm's-length log sales between unrelated parties in which no benefit passed through. Because Commerce had conducted the original investigation on an aggregate basis and not on a company-specific basis and had not previously conducted such a pass-through analysis, the administrative record did not contain evidence supporting Canada's claims.

7. In the original investigation, Commerce calculated the subsidy benefit from Provincial Crown timber programmes by assessing the extent to which each Province sold timber for less than adequate remuneration. This subsidy benefit is the numerator, which is divided over the relevant sales of lumber and by-products that benefit from the subsidy, the denominator, to determine the countervailable *ad valorem* subsidy rate. Commerce needed specific information and data to calculate any adjustment to this subsidy benefit numerator to account for potentially arm's-length sales of Crown logs between unrelated parties in which the subsidy did not pass through. Specifically, Commerce needed the volume of the log sales in Canada during the period of investigation ("POI") for which Canada sought a pass-through analysis. Additionally, to determine whether the reported log transactions were between unrelated parties, Commerce required information concerning any affiliation between the buyer and seller of the logs. Further, Commerce required information concerning government-mandated restrictions and other factors that could limit or control the terms of

[5] First Written Submission of Canada, February 24, 2005 ("First Written Submission of Canada"), paras. 38, 59-65.

[6] First Written Submission of Canada, para. 58.

[7] First Written Submission of Canada, para. 54-55.

[8] First Written Submission of Canada, para. 6. As acknowledged by Canada, "Section 129 proceedings may involve the issuance of new questionnaires . . . ."

the sale, and thus undermine the arm's-length nature of the sale. Finally, to conduct the "competitive benefit" analysis, through which Commerce measured whether and to what extent any subsidy passes through, Commerce required specific data on prices, species, size, grade, quality, discounts delivery terms, and payment terms.

8. Therefore, Commerce asked Canada, through questionnaires, to identify the volume of log sales subject to its pass-through claims, and to provide specific information necessary to determine whether log sales were between unrelated parties and at arm's length. This would allow Commerce to identify transactions that were eligible for the last phase of the analysis (competitive benefit). The requested information related to, *inter alia*, the relationship between the parties to the specific transactions (such as whether the parties were affiliated) and the circumstances surrounding the subject sales.

9. On 14 April[9], 17 August[10] and 5 October 2004[11] Commerce issued questionnaires and supplemental questionnaires to Canada with respect to this issue. Commerce notified Canada in its initial questionnaire that if a province was claiming that any portion of the volume of Crown logs reported in the numerator[12] was sold in arm's-length transactions and was between unrelated parties and required an analysis to determine if the purchasing sawmill received a subsidy benefit, the province was required to provide an explanation of how the volume was calculated and documentation supporting its claims.[13] The Canadian provincial governments provided questionnaire responses on 21 May 2004. Although the provincial governments provided certain information that had been requested, the responses were incomplete.

10. Therefore, on 17 August 2004, Commerce issued a supplemental "pass-through" questionnaire in which it informed Canada that its 21 May 2004, responses were deficient in a number of respects and that the "information provided in the questionnaire response is insufficient for the Department to complete its 'pass-through' analysis.[14] In that supplemental questionnaire, Commerce requested additional and clarifying information from the provincial governments and from independent harvesters and mills with respect to log sales that they claimed were at arm's length. Responding to Canada's complaint that certain of its requests could not be answered because the provincial governments lacked access to certain data, Commerce modified its requests for information.

11. Notably, Commerce attached a pass-through appendix to the supplemental pass-through questionnaire and requested that the provincial governments provide the appendix to the independent harvesters and sawmills involved in the log sales for which a pass-through analysis was requested. In the pass-through appendix Commerce requested information directly from the sawmills and

[9] *See*, Letter from Department of Commerce to Embassy of Canada, 14 April 2004, Pass-Through Questionnaire. Exhibit CDA-3.

[10] *See*, Letter from Department of Commerce to Embassy of Canada, 17 August 2004, Supplemental Pass-Through Questionnaire. Exhibit CDA-23.

[11] *See*, Letter from Department of Commerce to Embassy of Canada, 5 October 2004, Second Supplemental Pass-Through Questionnaire. Exhibit CDA-24.

[12] The numerator of Commerce's final subsidy calculation consisted of the total benefit received, which was calculated based on the total volume of Crown timber harvested during the POI that actually entered and was processed by sawmills, as reported by each of the provinces.

[13] In accordance with the DSB's recommendations and rulings (Panel Report, at para. 7.99; Appellate Body Report, at para. 167(e)), Commerce specifically requested information relating to the portion of the total volume of Crown timber entering sawmills reported by the provinces claimed to be "sold in arm's length transactions by tenure holders that did not own a sawmill . . ." and "sold in arm's- length transactions by tenured timber sawmills to sawmills that do not have tenure . . ." Exhibit CDA-3, at 10, 11 (questions 1 and 2).

[14] Exhibit CDA-23.

independent harvesters concerning affiliations and corporate relationships, as well as information relating to the terms of the sales, including log sales data and purchase contracts.[15]

12. On 15 September 2004, the Canadian parties submitted their responses to this supplemental questionnaire. Certain sawmills and independent harvesters submitted responses to the pass-through appendix. However, notwithstanding Commerce's earlier notice to Canada that in the absence of the requested data Commerce might not have sufficient data to complete its pass-through analysis, Canada once again provided incomplete responses to Commerce's data requests. Canada posited two reasons for its failure to respond properly to Commerce's requests: first, it claimed that certain of the requests were voluminous and that it was burdensome for it to collect the data; second, it claimed that certain information requested by Commerce was not relevant.[16]

13. On 5 October 2004, Commerce issued a second supplemental pass-through questionnaire and a supplemental pass-through appendix. Because the provincial governments failed to respond adequately to Commerce's earlier questionnaires, Commerce again requested clarifying and additional information. As noted in its second supplemental pass-through questionnaire, Commerce modified certain of its requests, where practicable, in response to Canada's claim that to provide the information was burdensome.[17] With respect to Canada's claim that certain information was not relevant, Commerce reiterated to Canada that it needed the data to conduct the DSB's recommended analysis. The Canadian parties submitted a response to the second supplemental questionnaire on 25 October 2004.

14. By refusing to provide certain of the data requested by Commerce, Canada was and is attempting to restrict Commerce's ability to conduct a meaningful pass-through analysis. Canada contends that Commerce's arm's-length analysis should be nothing more than a simple determination of whether the parties to the transaction are unrelated. Indeed, Canada argues that Commerce erred in not relying upon Canada's "aggregate" data – data that (although limited to sales between unrelated parties) fails to address factors other than affiliation that could render the transactions something other than arm 's length. As discussed below, Commerce's arm's-length analysis properly included examination of issues beyond mere affiliation.

B. Commerce Properly Conducted Its Arm's-Length Analysis as Part of Its Pass-Through Analysis

15. Commerce first analyzed the information provided by Canada to determine whether the sales were between related parties. If they were, no further analysis was conducted, because the DSB's

[15] Exhibit CDA-23, at 1 and Pass-Through Appendix - 1.

[16] *See, e.g.*, CDA-23, at 6 (Ontario question 1); Response of the Government of Ontario to the Department's 17 August 2004 Supplemental Pass-Through Questionnaire (15 September 2004), at ON-PASS-2, -3 ("Ontario September 15 Pass-Through Response"). Exhibit US-3. *See also*, Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of the Alleged Benefits (15 September 2004), at 10 ("British Columbia September 15 Pass-Through Response"). Exhibit US-4.

[17] In the second supplemental questionnaire, Commerce further modified its requests. By way of example, in response to the Government of British Columbia's ("GBC") statement that it did not have access to log purchase agreements for the transactions claimed to be at arm's length, Commerce limited its request to those sawmills that participated in the Norcon Survey that was prepared at the GBC's request. Exhibit CDA-24, page 5 at 6. With respect to a the Government of Alberta's ("GOA") concern that it could not provide all copies of tenure agreements relating to commercial timber permits ("CTPs"), Commerce limited its request to tenure agreements associated with coniferous timber quotas ("CTQs") and certain CTPs that were identified by Commerce. Exhibit CDA-24, page 8 at 1. Similarly, Commerce modified its requests for timber return data from the GOA to those portions containing the text relating to the payment of the stumpage dues. Exhibit CDA-24, page 9 at 7.

recommendations and rulings concerned only sales between unrelated parties.[18] Commerce next analyzed the sales between unrelated parties to determine if they were at arm's length. Canada challenges this necessary step in its entirety, in the apparent and mistaken belief that all sales between formally unrelated parties are necessarily at arm's length. Therefore, according to Canada, by even analyzing whether such sales are, in fact, at arm's length, and then eliminating sales that fail the arm's-length test from the pass-through analysis, Commerce is somehow illegally "presuming" pass-through. This is incorrect. Indeed, it is Canada that is "presuming" no pass through for all sales between unrelated parties. Further, there is nothing in the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings that suggests that Commerce' s analysis of whether sales are at arm's length should be so severely limited, or indeed, eliminated.

1. Commerce's Approach to Determining Whether Sales are at "Arm's Length" – Involving Factors Other Than Mere Affiliation – is Consistent with the DSB's Recommendations and Rulings, the SCM Agreement, and the GATT 1994

16. Canada claims that Commerce "applied a contrived standard"[19] in determining whether its claimed log sales were at arm's length. However, the term "arm's length" is not used or defined in the text of the SCM Agreement; thus, it is unclear on what basis Canada makes its claim that the standard Commerce applied is "contrived". The Appellate Body concluded in this dispute that both the SCM Agreement and the GATT 1994 require that, where subsidies are bestowed directly on producers of an *input* product, while countervailing duties are to be imposed on *processed* products, "*and where input producers and downstream processors operate at arm 's length*," Commerce must establish that the benefit is passed through to the downstream processor.[20] Therefore, where the two producers do not operate at "arm's length", no determination of the amount of the subsidy passing through the transaction is required because the subsidy bestowed on the input producer benefits the producer of the processed product. Whether the entities operate "at arm's length" involves more than just a question of formal affiliation; it involves an analysis of whether one party effectively "controls" the other or whether the parties have roughly equal bargaining power.[21] In other words, if one of the parties controls the other or their dealings are not between entities of equal bargaining power, neither the SCM Agreement nor the GATT 1994 require that the amount of the subsidy passing through the transaction be determined; rather, the investigating authority may regard the subsidy bestowed on the input as benefiting the processed product.[22]

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[18] Canada has not challenged Commerce's affiliation determinations. First Written Submission of Canada, para. 74, fn. 66.

[19] First Written Submission of Canada, para. 59.

[20] Appellate Body Report, para. 146 (emphasis on "arm's length" in original).

[21] *See* BLACK'S LAW DICTIONARY, Seventh Edition (West Group 1999) at 103 ("Of or relating to dealings between two parties who are not related or not on close terms and who are presumed to have roughly equal bargaining power; not involving a confidential relationship. . . ."). Exhibit US-5. *See also*, THE NEW SHORTER OXFORD ENGLISH DICTIONARY, Thumb Index Edition (Oxford University Press 1993) at 114 ("without undue familiarity; (of dealings) with neither party controlled by the other"). Exhibit CDA-18.

In the specific context of a dispute concerning countervailing duties, *see* Panel Report, *Korea - Measures Affecting Trade in Commercial Vessels*, WT/DS273 (7 March 2005), para. 7.135 . *(*European Communities' challenged certain Korean subsidies as prohibited subsidies under Articles. 3.1 and 3.2 of the SCM Agreement). In determining the appropriateness of a market benchmark, the panel considered whether purchasing negotiations were at arm's length when the buyer was able to dictate the source from which a shipyard was to procure an advanced payment refund guarantee (APRG). According to the panel, "[i]n such cases, the designation of the APRG-provider by the buyer means that there is a risk that the APRG is not negotiated at arm's length, since the shipyard is a captive buyer. The rate paid by the shipyard might therefore be higher than it would if the shipyard were able to shop around and compare offers from alternative suppliers."

[22] *See* Appellate Body Report, para. 143 ("Where the input producers and producers of the processed products operate at *arm's length*, the pass-through of input subsidy benefits from the direct recipients to the indirect recipients downstream cannot simply be presumed; . .") (underscored emphasis added).

17. Thus, the issue is not merely one of affiliation. In this regard, the DSB's recommendations and rulings themselves recognize a distinction between arm's length and affiliation presenting arm's-length sales as a subset of sales between unrelated entities. Specifically, the DSB ruled that Commerce should have conducted "a pass-through analysis in respect of *arm's length sales* of *logs* . . . to *unrelated* sawmills".[23] This is completely inconsistent with Canada's contention that an arm's-length analysis requires nothing more than a determination of affiliation.[24]

18. Commerce properly examined, in its pass-through analysis, whether the parties to the log sales were related through common ownership and also whether any of the circumstances surrounding the log sales affected the nature of the sales to such an extent that they could not be considered arm's length. Initially, and as discussed above, Commerce examined whether any of the log sales at issue were between affiliated parties. Consistent with the DSB's recommendations and rulings, when Commerce found that sales were between affiliated parties, it performed no further pass-through analysis.[25] If the sales were between unaffiliated parties, Commerce examined the circumstances surrounding the transactions as part of its "arm's length" analysis.

19. Commerce properly examined the circumstances surrounding the sales Canada reported as occurring between unrelated parties. Although Canada objects to Commerce's approach, Canada can point to no language in the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings that establishes the *per se* affiliation analysis advanced by Canada. Indeed, the record evidence demonstrates that many of the sales that Canada claims are arm's-length sales are affected by government mandates and other conditions that render those sales not at arm's length or otherwise ineligible for the pass-through analysis. These will be discussed in the following section.

2. The Record Demonstrates that Under the Canadian Stumpage System, Many of the Circumstances of the Sales are Controlled by Government Mandates and Other Conditions

20. Canada's simplistic *per se* approach is divorced from the reality of the Canadian stumpage system. With respect to many transactions, record information demonstrates that certain government-mandated restrictions and other factors controlled, limited, or otherwise affected the log sales, warranting Commerce's determination that they were not conducted at arm's length or, in some instances, were not sales at all.

21. Specifically, record evidence demonstrates that the provincial governments impose restrictions upon log sales that affect many of the transactions that Canada reported as arm's-length sales. Commerce identified two such categories of government-mandated restrictions: (1) limitations on log sales that are contained in Crown tenure contracts, such as appurtenancy and local processing requirements, and (2) wood supply agreements.[26] Canada does not suggest that such governmental mandates do not exist, but instead submits that such mandates do not affect the arm's-length nature of the transaction between the parties.[27] According to Canada, the fact that the government dictates the disposition of Crown timber by dictating to whom a seller must sell has no bearing on the actual terms of sale – so long as parties are not formally affiliated, any transaction between them must be considered at arm's length. Despite Canada's protestations to the contrary, under both categories of government-mandated restrictions, log sellers are not free to act in their best interests to choose and negotiate among potential buyers. Where the provincial governments limit the ability of a seller to sell freely and instead dictate to whom the seller must sell, Commerce reasonably determined,

[23] Appellate Body Report, para. 176(e) (emphasis added, except that emphasis on "logs" is in original.)
[24] Appellate Body Report, para. 124. (emphasis added).
[25] Section 129 Determination, at 4. Exhibit CDA-5.
[26] Section 129 Determination, at 4. Exhibit CDA-5.
[27] First Written Submission of Canada, paras. 62-64.

consistent with any reasonable reading of the term "arm's length," that the affected sales were not at arm's length.[28]

22. Further, based on the record, Commerce determined that there was an additional factor[29] – other than the above government-mandated restrictions – that affected many of the Canadian log sales such that they could not be considered to be at arm's length. The actual structure of certain log purchase agreements[30] empowered the purchasing sawmill to control so many aspects of the transaction that Commerce determined that transactions covered by such purchase agreements could not be considered to be arm's length. Specifically, with respect to certain log purchase agreements, the sawmill actively manages all aspects of harvest and delivery. With respect to others, the sawmill finances or provides other goods or services as part of the transaction.[31] To enable Commerce to distinguish log purchase agreements that do represent arm's-length log sales from those that do not, it was necessary for Commerce to review the purchase agreements themselves.

23. Although not exclusively arm's-length issues, Commerce identified two additional factors affecting its pass-through analysis – factors that Canada contends should have had no bearing upon Commerce's analysis. Specifically, Commerce determined that in certain transactions the purchasing sawmills pay the Crown stumpage fees directly to the government for logs obtained from independent harvesters. Because the vehicle by which the Crown bestows the subsidy is through the administered stumpage programmes, when the purchasing sawmill pays the Crown directly for the stumpage, the purchasing sawmill directly receives the benefit and "pass-through" is not at issue.[32] Additionally, excluded from Commerce's analysis were fibre exchanges between Crown tenure holders, which often involved simple exchanges of, for instance, logs for chips, to meet appurtenancy and other harvesting requirements. These exchange agreements are a mechanism for tenured sawmills to deal with various government restrictions concerning the disposition of the harvested timber and are not log sales.[33]

24. The record was replete with evidence that demonstrated that certain government-mandated restrictions and other factors controlled, limited, or otherwise affected the log sales (in fact rendering some of them not sales at all), supporting Commerce's determination to examine more than simple affiliation in analyzing whether sales were at arm's length for the purpose of its pass-through analysis.

[28] *See, e.g.*, Panel Report, *Korea - Measures Affecting Trade in Commercial Vessels*, WT/DS273 (7 March 2005), para. 7.135 ("captive buyer" creates risk that the transaction is not at arm's length.).

[29] Commerce identified three additional factors affecting its pass-through analysis. However, as discussed above, two of the three factors are not exclusively arm's-length issues.

[30] Section 129 Determination, at 5. Exhibit CDA-5. The log purchase agreements that were provided to Commerce are proprietary documents. However, Commerce can state generally that these agreements contained vastly differing conditions and terms of sale. As evidenced by Commerce's reduction in the numerators of Alberta, Ontario and Saskatchewan, there were log purchase agreements that did satisfy Commerce's pass-through analysis.

[31] Section 129 Determination, at 5. Exhibit CDA-5.

[32] Section 129 Determination, at 5. Exhibit CDA-5.

[33] Section 129 Determination, at 5-6. Exhibit CDA-5

C. Commerce Appropriately Required That Canada Provide Company-Specific Information to Determine Whether the Transactions for Which a Pass-Through Analysis Was Requested Were Eligible for Such Analysis

25. Canada contends that Commerce improperly disregarded "aggregate" data that it submitted containing sales information from the provinces that generally identified the purchasers and sellers and the volume and value of sales that Canada identified using its *per se* test as arm's-length transactions.[34] Canada also complains that Commerce refused to rely upon certain "sample" data. As discussed above, however, Commerce correctly determined that the arm's-length component of its pass-through analysis required more than just a determination concerning whether parties were affiliated. Additionally, Commerce correctly determined that other factors affected the pass-through analysis. Thus, Commerce required specific information on each transaction for which Canada requested a pass-through analysis, which necessitated that Canada provide more than just its aggregate data and, in some cases, more than its self-selected sample data.[35] This follows not only from the very nature of the enquiry, but also from the DSB's recommendations and rulings themselves.

26. The DSB's recommendations and rulings required that Commerce determine whether transactions between independent harvesters and sawmills, as well as between tenured harvesters/sawmills and sawmills, "passed through" the benefit from subsidies provided to the independent harvesters or tenured harvesters/sawmills. This is a company-specific issue, *i.e.*, an issue that is specific to each combination of log buyer and log seller, and the DSB recognized it as such.

27. Specifically, for instance, the Appellate Body referred to "the producer of the input" and "the producer of the product processed from the input", finding that, "it would not be possible to determine whether countervailing duties levied on the processed product are *in excess* of the amount of the total subsidy accruing to that product, without establishing whether, and in what amount, subsidies bestowed upon the producer of the input flowed through, downstream, to the producer of the product processed from that input".[36] While noting that the United States, in accordance with Article 19.3 of the SCM Agreement, had conducted an aggregate countervailing duty investigation, both the original panel and the Appellate Body found that this did not excuse Commerce from examining whether the *individual transaction* between the input supplier and the producer passed through the subsidy benefit. Thus, "before being entitled to impose countervailing duties on a processed product, for the purpose of offsetting an input subsidy, a Member must first determine, in accordance with Article 1.1, that a financial contribution exists, and that the benefit conferred directly on *the input producer* has been passed through, at least in part, to *the producer* of the processed product."[37]

28. Finally, the Appellate Body was unequivocal that, where the input transaction is *not* at arm's length, there is no need for the investigating authority to analyze whether the subsidy passed through:

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[34] First Written Submission of Canada, paras. 8, 76.

[35] Commerce did not disregard "sample" data provided by Canada. To the contrary, in response to certain concerns expressed by Canada, Commerce permitted Canada to submit subsets of data responding to its questionnaires. As noted previously, for example, with respect to British Columbia, Commerce limited its request for log purchase agreements to the 74 sawmills that participated in the Norcon Survey that was prepared at the GBC's request. Exhibit CDA-24, page 5 at 6. With respect to the Government of Alberta's ("GOA") concern that it could not provide all copies of tenure agreements relating to commercial timber permits ("CTPs"), Commerce limited its request to tenure agreements associated with coniferous timber quotas ("CTQs") and certain CTPs that were identified by Commerce. Exhibit CDA-24, page 8 at 1. Similarly, Commerce modified its requests for timber return data from the GOA to those portions containing the text relating to the payment of the stumpage dues. Exhibit CDA-24, page 9 at 7.

[36] Report of the Appellate Body, para. 141 (emphasis in original).

[37] Report of the Appellate Body, para. 154 (emphasis added).

> Where countervailing duties are used to offset subsidies granted to producers of input products, while the duties are to be imposed on *processed* products, and where input producers and downstream producers operate at *arm's length*, the investigating authority must establish that the benefit conferred by a financial contribution directly on input producers is passed through, at least in part, to producers of the processed product subject to the investigation.[38]

Commerce implemented these findings by requesting the data necessary to establish whether each independent harvester or tenured harvester/sawmill sold logs at arm's length to each sawmill. Such company-specific information was necessary for Commerce's analysis of whether, in any particular transaction, the subsidy was passed through from the input producer to the producer of the subject merchandise. Indeed, the Appellate Body acknowledges this fact when it reasoned that the administering authority should determine "whether, and in what amount, subsidies bestowed upon the *producer of the input* flowed through, downstream, to the *producer of the product* processed from that input".[39]

29. Canada errs when it states that Commerce "ignored entirely the original panel's view that company-specific data are not necessarily required to conduct [sic] pass-through analysis".[40] The original panel said nothing of the sort. In response to US arguments to the effect that there is a mismatch between an investigation conducted on an aggregate basis and the company-specific nature of the pass-through issue, the panel simply found that pass through can indeed be examined during an aggregate investigation.[41] The panel did not suggest that company-specific information should not be used to analyze whether there was a pass-through of subsidies.

30. Where parties provided the requisite information, Commerce was able to conduct its pass-through analysis.[42] For instance, although the Government of Ontario did not identify all transactions in which the stumpage was paid by the purchasing sawmills rather than the harvesting tenure holders, eight Ontario harvesters and mills did provide such company-specific information in response to Commerce's questionnaires.[43] Using the data provided by those companies, Commerce was able to conduct its pass-through analysis for those sales found, in light of the factors identified in the section above, to be at arm's length.[44] Similarly, with respect to Alberta, eight companies provided Commerce with company-specific data, including sample purchase contracts, information identifying those transactions for which the mill paid the stumpage directly to the Crown, and information concerning purchases from private lands.[45] Just as it did for Ontario, using the company-specific data provided by the Alberta companies, Commerce was able to conduct its pass-through analysis for those sales found to be at arm's length. Commerce was able to conduct its analysis as well with respect to certain company-specific data that it received in response to the pass-through appendices provided to Saskatchewan.[46]

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[38] Report of the Appellate Body, para. 147 (emphasis in original).

[39] Report of the Appellate Body, para. 141 (emphasis added).

[40] First Written Submission of Canada, para. 58 (citing Panel Report, at para. 7.98).

[41] Report of the Panel, para. 7.98.

[42] By way of example, at the request of Commerce, Ontario identified the quantity of sales that were sold to the purchasing mill subject to wood supply agreements. Exhibit CDA-23, at question 2; Ontario 15 September Pass-Through Response, at On-PASS-4, question 2 referring to ON-PASS-6, ON-PASS-7. Exhibit US-3. Because Commerce determined that volume of sales not to be at arm's length, no further analysis was conducted with respect to those sales.

[43] 6 December 2004, "Pass-Through" Analysis Calculations for the Province of Ontario, at 2-4. Exhibit US-6.

[44] Section 129 Determination, at Comment 8. Exhibit CDA-5.

[45] 6 December 2004, "Pass-Through" Analysis Calculations for the Province of Alberta, at 2-5. Exhibit US-7.

[46] 6 December 2004, "Pass-Through" Analysis Calculations for the Province of Saskatchewan, at 2. Exhibit US-8.

31. In many instances, however, Canada failed to provide the requisite information despite repeated requests that it do so. For example, although Commerce limited its request for tenure agreements containing domestic processing or other mandated requirements to those companies that participated in the Norcon Survey, British Columbia failed to provide the copies that Commerce requested.[47] British Columbia did, however, provide *samples* of such tenure agreements, but the domestic processing requirements included in the samples that British Columbia submitted varied widely.[48] Although British Columbia argued that the domestic processing requirements contained in the tenure agreements were outdated, standardized, or otherwise inapplicable during the POI, it failed to provide any record evidence demonstrating that the requirements were not in force during the POI.[49] As a consequence, Commerce was not able to rely upon the sample agreements provided by British Columbia to support its pass-through claim. Additionally, British Columbia failed to identify that portion of the sales subject to its pass-through claim in which the sawmills pay the Crown stumpage fee directly to the government rather than paying the independent harvester from whom they obtained the logs.[50] Finally, although British Columbia did provide certain log purchase agreements it failed to provide the underlying tenure agreements.[51] There were similar deficiencies with respect to Manitoba[52], and to lesser degrees with respect to Alberta, Ontario and Saskatchewan.[53] Where Canada failed to provide the information requested, Canada prevented Commerce from completing its pass-through analysis.[54]

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[47] Exhibit CDA-24, at 3.

[48] Exhibit CDA-6, at 10.

[49] *See* Exhibit CDA-24, at 5, question 5; Response of the Government of British Columbia to the Department's 5 October 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (25 October 2004), at BC-PT-3, -4, -15. ("British Columbia October 25 Pass-Through Response"). Exhibit US-9.

[50] British Columbia September 15 Questionnaire Response, at 10 (Exhibit US-4); British Columbia 25 October Pass-Through Response, at BC-PT-17 -19 (Exhibit US-9). *See also* , Draft Section 129 Determination, at 10-11(Commerce summarizes the data that British Columbia failed to provide). Exhibit CDA-6.

[51] Draft Section 129 Determination, at 11. Exhibit CDA-6.

[52] Manitoba failed to substantiate its claim that 8.70 per cent of the Crown log harvest did not result in a pass-through of subsidies because its data deficiencies precluded Commerce from conducting its pass-through analysis. Draft Section 129 Determination, at 11-12. Exhibit CDA-6. Although one company did respond to Commerce's pass-through appendix, the sales data provided by that company were for sales arising after the POI so Commerce determined that it was not appropriate to include those sales in its analysis. Draft Section 129 Determination, at 12. Exhibit CDA-6. Canada now argues – but has offered no evidence support its assertion – that those sales were not outside the POI. First Written Submission of Canada, para. 85, fn. 96.

[53] As evidenced by the Section 129 Determination, although there were some data issues with respect to Alberta, Saskatchewan, and Ontario that precluded Commerce from conducting its pass-through analysis with respect to the entire volumes for which these provinces claimed no pass through, Commerce was able to use data that had been provided and determined that a certain benefit did not pass through.

[54] Contrary to Canada's argument, Commerce was in fact precluded from conducting its pass-through analysis with respect to the log sales contained in the Norcon Survey – a survey that Canada contends demonstrates that 11.6 per cent of Crown logs consumed in British Columbia mills were purchased from independent harvesters that held tenure. First Written Submission of Canada, para. 79. Although Canada submits that it provided transaction-specific data, it continually failed to provide necessary information concerning government-mandated restrictions and other conditions that Commerce required to complete its analysis. The Norcon Survey and the data that Canada refers to in Annex I of its first written submission obscure the fact that the data could be relied upon for little more than information about *affiliation* between parties to the log transactions. Indeed, as explained in the Norcon Survey itself, "[f]or purposes of this survey, arm's length log purchases were defined as logs purchased by a lumber manufacturer from a person with which it is not affiliated applying the definition of 'affiliated persons' contained in" US law. Exhibit CDA- 31, at 2. As the United States demonstrates above, however, affiliation is only one component of the pass-through analysis. The remaining 6.2 per cent referenced by Canada apparently represent transactions between tenure-holding sawmills. First Written Submission of Canada, para. 79. As discussed below, such transactions were not part of the DSB's recommendations and rulings.

32. The truth is that, although Canada prevailed before both the original panel and the Appellate Body in arguing that Commerce was required to conduct this pass-through analysis, Canada apparently was unprepared to support many of its claims of no pass through with necessary evidence. Instead, Canada seeks to undermine Commerce's ability to conduct a full examination of the pass-through issue. Commerce – reasonably and in accordance with the DSB's recommendations and rulings – found that the subsidy benefit passed through where the evidence indicated that the input transaction was not at arm's-length or where the transaction otherwise was ineligible for a pass-through analysis because it was not a sale or because the purchasing sawmill paid the stumpage to the Crown. Where Commerce found the input transaction to be a sale at arm's length, Commerce completed the pass-through analysis required by the recommendations and rulings.

33. As demonstrated by the Section 129 Determination, when Canada properly supported its claims, Commerce was able to, and did, conduct its analysis. Commerce did not improperly "presume" pass-through – to the contrary, as set forth above, Commerce conducted a pass-through analysis in compliance with the SCM Agreement, the GATT 1994, and the recommendations and rulings of the DSB.

D. Commerce Used Appropriate Benchmarks in its Pass-Through Analysis

34. Canada criticizes Commerce benchmarks but fails to allege any inconsistency with a provision of the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings. Thus, the Panel should reject Canada's argument on this basis alone.

35. In any event, Commerce selected appropriate benchmarks. Where Commerce – upon examining record evidence – determined that the input transaction was at arm's length, it proceeded to determine whether there was a competitive benefit: *i.e.*, whether the benefit "passed through". As previously explained, a subsidy provided to the producer of an input product confers a competitive benefit on a downstream purchaser of the input when the price paid for the subsidized input is lower than the a market determined benchmark price for the same product. In selecting a market determined benchmark, Commerce used, where possible, the actual company-specific prices that the purchasing mill paid for logs harvested from private lands and for imported logs.[55] Where those data were not available, Commerce relied on publicly available prices for logs harvested from private lands and logs imported into the province.[56]

36. Commerce's competitive benefit analysis demonstrated that many of the arm's-length log sales during the POI in Alberta, Ontario, and Saskatchewan, were made at prices below the benchmark prices, and therefore conferred a competitive benefit to the purchasing sawmills. As a result of Commerce's competitive benefit calculations, therefore, only some portion of the Crown harvest volume originally included in the numerator is excluded from the numerator of the revised subsidy calculations.

37. Canada now contends that Commerce relied on benchmarks that do not reflect "a comparison to the marketplace"[57] because they were unrepresentative of both the species harvested and of the prices paid in each province for logs used in lumber production. Canada is incorrect. The benchmark prices Commerce used were observable market-determined prices for logs that were sold in Canada. These prices corresponded to the same species of logs sold in each province for which a competitive benefit analysis was conducted and were otherwise representative of market prices.

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[55] *See*, e.g., Exhibit CDA-23, at 3, 6, 8, 10, 12 and pass-through appendix; Exhibit CDA-24, at 3, 6, 8, 11, 13 and supplemental pass-through appendix.

[56] Final Section 129 Determination, at 6. Exhibit CDA-5.

[57] First Written Submission of Canada, para. 67.

38. For Alberta, Commerce used company-specific prices the mills paid for logs harvested from private lands in the province and logs they imported into the province. Where those company-specific prices were not available, Commerce used the weighted-average price published in the annual 2000 Timber Damage Assessment (TDA) survey conducted by KPMG.[58] For Ontario, Commerce used a weighted-average price of transactions for timber harvested from private lands, as reported in the KPMG the "Delivered wood costs" schedule of the KPMG Report on Ontario Softwood Timber Costs and Sources, 1 April 2000 to 31 March 2001, dated 22 June 2001.[59] For Saskatchewan, which did not provide any company-specific or published provincial log prices, Commerce used a weighted-average price of the domestic and import prices for spruce-pine-fir (SPF), as reported by Alberta, Manitoba, Ontario, and Quebec.[60]

39. In sum, Commerce used as benchmarks observable market-determined prices for logs that were sold in Canada from unsubsidized sources to determine whether and to what extent a subsidy passed through in arm's length sales of logs between unrelated parties. For the reasons described above, the benchmark prices Commerce used to conduct its competitive benefit analysis properly reflected market conditions in Canada during the POI.

E. Commerce Did Not "Presume" Pass-Through

40. As demonstrated above, Commerce thoroughly investigated Canada's claims that no subsidy passed through as a consequence of certain transactions. As a result of its analysis, Commerce removed from the numerator of its *ad valorem* subsidy calculation any subsidy benefits it determined did not pass through in arm's length log sales between independent harvesters and sawmills and between unrelated tenured timber harvesters/sawmills and sawmills. Commerce thus ensured that its Section 129 Determination provided for a countervailing duty only with respect to the benefit from countervailable subsidies demonstrated to exist. Canada's attempt to characterize Commerce's analysis as a "presumption" of pass through is not supported by the record.

41. Indeed, as noted earlier, it is Canada that is "presuming". Under Canada's theory, when it comes to pass-through, responding parties can control the analysis. If the country under investigation chooses to provide proper evidence supporting its pass-through claim, authorities are able to conduct their analysis and, depending upon the determination, reduce the *ad valorem* rate. However, if the country chooses not to provide necessary information, according to Canada, the authorities are precluded from conducting their analysis and must presume no pass-through – *i.e.*, presume that no subsidy is bestowed on the subject merchandise. Consequently, under Canada's theory, once a country under investigation raises a pass-through issue, it would be in a position simply to refuse to provide any evidence supporting its claim, because the authorities would be prohibited from including any of the claimed volume in their calculations.

42. From Canada's perspective, there is a certain simplicity in its argument – Commerce should simply accept Canada's unsubstantiated assertions. For instance, because British Columbia informed Commerce that 11.6%[61] of the log sales were between unrelated parties, according to Canada, Commerce must automatically find that the benefit for that associated volume of log sales did not pass through and must be removed from the numerator. However, nothing in the DSB 's recommendations and rulings, the SCM Agreement, or the GATT 1994 requires that the investigating authority simply accept assertions of the country under investigation. To the contrary, the DSB recommended that

[58] *See, e.g., 6* December 2004, "Pass-Through" Analysis Calculations for the Province of Alberta, at 2. Exhibit US-7.

[59] 6 December 2004, "Pass-Through" Analysis Calculations for the Province of Ontario, at 1-4. Exhibit US-6.

[60] 6 December 2004, "Pass-Through" Analysis Calculations for the Province of Saskatchewan, at 2. Exhibit US-8.

[61] First Written Submission of Canada, para. 79.

Commerce *conduct* a pass-through analysis. Commerce did so and based its determination upon what the record evidence *demonstrated* the facts to be and not upon what Canada *presumed* the result should be for sales between all unrelated parties.

F. Commerce Properly Investigated Categories of Sales Identified by the DSB

43. According to the DSB's recommendations and rulings, Commerce should investigate transactions between independent harvesters and sawmills[62], as well as between tenured harvesters/sawmills and unrelated sawmills.[63] Although Canada claims that Commerce "inexplicably excluded information of transactions in which the purchasing sawmill had tenure"[64] there is nothing inexplicable about it, as these transactions were not part of the DSB's recommendations and rulings. In this respect, there was a specific definition of both "tenured timber harvester/sawmill" and "sawmill". "Tenured timber harvester/sawmill" was defined as "an enterprise holding a stumpage contract that fells trees and produces logs, and also processes logs into softwood lumber."[65] "Sawmill" was defined as "an enterprise that processes logs into softwood lumber and *does not hold a stumpage contract"*..[66]

44. Given these precise definitions that bear directly upon the DSB recommendations and rulings with respect to pass-through, Commerce properly limited this aspect of its pass-through analysis to arm's-length log sales by an enterprise holding a stumpage contract that fells trees and produces logs, and also processes logs into softwood lumber, to an enterprise that processes logs into softwood lumber and does not hold a stumpage contract, *i.e.*, tenured timber harvester/sawmills to unrelated, non-tenured sawmills. As the DSB recommendations and rulings recognized, tenure-holding sawmills are direct subsidy recipients. It is entirely appropriate therefore to include the volume of logs processed by those sawmills in the total subsidy calculation.

G. Commerce Properly Calculated the Revised Rate

45. Contrary to Canada's arguments that Commerce somehow applied its results to an "invalidated" countervailing duty rate[67], Commerce properly calculated the revised rate by removing from the numerator of the *ad valorem subsidy* rate calculation the volume of log sales determined not to have passed through[6868] The numerator of the *ad valorem* subsidy rate was reduced by C$28,344,121. The revision reduced the only rate that was before the original panel and Appellate Body, *i.e.*, the 18.79 per cent *ad valorem* rate calculated in the Final Determination, to 18.62 per cent *ad valorem.*[69] With the exception of this limited pass-through analysis, there are no outstanding DSB recommendations or rulings that would have required further modification of the *ad valorem* rate calculation.

III. The Results of the First Assessment Review are Not Within the Panel' s Jurisdiction

[62] The United States did not appeal the Panel's findings with respect to arm's-length log sales between tenured timber harvesters not owning sawmills and sawmills. Appellate Body Report, fn. 157.

[63] Appellate Body Report, para. 167(e); *see* CDA-3, at questions 1 and 2.

[64] First Written Submission of Canada, para. 55.

[65] Appellate Body Report, fn. 150.

[66] Appellate Body Report, fn. 151 (emphasis added).

[67] First Written Submission of Canada, para. 10.

[68] *See* 6 December 2004, Country-wide Rate Calculations Net of Subsidy Benefits That Did Not Pass-Through - Revised as a Result of Comments Submitted by Parties to the Proceeding, at 2-8. Exhibit US-10.

[69] *See Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products From Canada*, 69 FR 75305 (16 December 2004). Exhibit CDA-7.

46. The United States reiterates its request, set out in its submission of 10 March 2005, that the Panel preliminarily rule that the results of the first assessment review are not "measures taken to comply" and therefore are outside Panel's jurisdiction in this proceeding. In particular, the United States noted in its preliminary ruling request that original investigations and assessment reviews are different processes with different administrative records that serve distinct purposes.[70] In this case, the assessment review was initiated at the behest of Canada, among others, eight months before the recommendations and rulings in this dispute were adopted.

47. This is not a situation like that presented in *Australia – Automotive Leather*, in which a WTO-inconsistent subsidy was both withdrawn and "regranted" in another form on the same day, in "inextricably linked elements of a single transaction".[71] Rather, the assessment review is a completely separate proceeding, based on a different record, designed to assess countervailing duties – a proceeding, moreover, that can be requested by Canada at regular intervals well into the future. Finally, it cannot be seriously asserted that, where there have been DSB recommendations and rulings with respect to the imposition of supplemental duties on a product, any subsequent proceedings related to those duties are "measures taken to comply". A previous panel has already found this not to be the case, in *EC – Bed Linens (Panel).*[72] In sum, the United States reiterates that the results of the first assessment review are neither "measures taken to comply" with recommendations and rulings, nor do they render actual measures taken to comply "non-existent".

IV. The Panel Should Not Make the Specific Recommendations Sought by Canada

48. In its first submission, Canada has asked the Panel to make certain findings and recommendations in the event that it agrees with Canada. Specifically, Canada asks that the DSB find that the imposition of duties by the United States is inconsistent with the SCM Agreement and the GATT 1994 and recommend either that the United States refund the duties collected to offset the amounts determined to pass through or revise its measure to be consistent with the relevant agreements and refund the duties to the extent they exceed the amount of the subsidy determined to have passed-through.[73]

49. The Panel should decline to make such recommendations. The text of DSU Article 19.1 is unequivocal regarding the recommendation that a panel is to make in such a case: "Where a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it *shall* recommend that the Member concerned bring the measure into conformity with that agreement." (Emphasis added). In short, the recommendations that Canada seeks here are not authorized by the DSU.

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[70] *See* Appellate Body Report, *European Communities - Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India - Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW, adopted 24 April 2003, para 123. "(the imposition and collection of anti-dumping duties under Article 9 is a separate and distinct phase of an anti-dumping action that necessarily occurs after the determination of dumping, injury, and causation under Articles 2 and 3 has been made.") Footnotes omitted. Although there is no specific corollary to Article 9 of the Anti-Dumping Agreement in the SCM Agreement, the SCM Agreement recognizes that Members may conduct assessment proceedings to determine the final amount of countervailing duty to be assessed. *See* Footnote 52 of the SCM Agreement.

[71] Panel Report, *Australia – Subsidies Provided to Producers and Exporters of Automotive Leather – Recourse to Article 21.5 of the DSU by the United States*, WT/DS126/RW and Corr.1, adopted 11 February 2000, para. 6.50.

[72] *See* Panel Report, *European Communities - Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India - Recourse to Article 21.5 of the DSU by India*, WT/DS141/RW, adopted 24 April 2003, as modified by the Appellate Body Report, WT/DS141/AB/RW, para. 6.15.

[73] First Written Submission of Canada, para. 72.

V. Conclusion

50. For the reasons stated above, Canada's claims against the measure taken to comply with the DSB's recommendations and rulings have no basis in the SCM Agreement, the GATT 1994, or the recommendations and rulings of the DSB. Thus, the United States requests that the Panel find that the United States properly implemented the recommendations and rulings of the DSB and that the Panel reject Canada's claims in their entirety.

Exhibit List

Number	Name
US-3	Response of the Government of Ontario to the Department's 17 August 2004 Supplemental Pass-Through Questionnaire (15 September 2004) (relevant pages).
US-4	Response of the Government of British Columbia to the Department's 17 August 2004 Supplemental Questionnaire Concerning Pass Through of the Alleged Benefits (September 15, 2004) (relevant pages).
US-5	BLACK'S LAW DICTIONARY, Seventh Edition (West Group 1999) at 103 (definition "arm' s length").
US-6	6 December 2004, "Pass-Through" Analysis Calculations for the Province of Ontario
US-7	6 December 2004, "Pass-Through" Analysis Calculations for the Province of Alberta
US-8	6 December 2004, "Pass-Through" Analysis Calculations for the Province of Saskatchewan
US-9	Response of the Government of British Columbia to the Department's 5 October 2004 Supplemental Questionnaire Concerning Pass Through of Alleged Benefits (October 25, 2004)(relevant pages).
US-10	6 December 2004, Country-wide Rate Calculations Net of Subsidy Benefits That Did Not Pass-Through - Revised as a Result of Comments Submitted by Parties to the Proceeding

ANNEX B-3

ORAL STATEMENT OF THE UNITED STATES

21 April 2005

Introduction

1. Good morning, Mr. Chairman and members of the Panel. Thank you for agreeing to serve as panelists in this proceeding and for the opportunity to appear before you today.

2. We recognize that our statement is lengthy, which flows from the fact that this is our first opportunity to respond to Canada's second submission. We were disappointed that Canada opposed our request for sequential second submissions in this proceeding, which would have helped to avoid this situation. We thank you in advance for your time and attention as we deliver our statement.

3. We will begin this morning by addressing Canada's response to our preliminary ruling request. Then we will explain how the United States properly implemented the recommendations and rulings of the DSB by conducting the appropriate pass-through analysis.

Preliminary Ruling Request

4. As you know, the United States has requested a preliminary ruling that the results of the assessment review are not "measures taken to comply" pursuant to DSU Article 21.5, and are therefore outside this Panel's jurisdiction. As our request notes, the assessment review was a proceeding separate from both the original countervailing duty investigation determination challenged by Canada and the Section 129 Determination at issue here, was initiated prior to the DSB's adoption of recommendations and rulings in this dispute, and had nothing to do with complying with the recommendations and rulings of the DSB.

5. In an attempt to justify sweeping the separate assessment review results into its Article 21.5 panel request, Canada has resorted to relying on the supposed "broad" scope of Article 21.5 and "wide discretion" of the Panel to review measures under Article 21.5.[1] Canada also argues that a failure to include the assessment review results in this compliance proceeding would be contrary to the overall "purpose" of Article 21.5 proceedings.[2]

6. But the issue is simpler than Canada would have us believe. Either a measure is taken to comply – and falls within the terms of Article 21.5 – or it is not, and is thus not within this Panel's jurisdiction. As the Appellate Body stated in *Canada – Aircraft* – and none of the reports cited by Canada are to the contrary – Article 21.5 proceedings "do not concern just *any* measure of a Member of the WTO; rather Article 21.5 proceedings are limited to those 'measures *taken to comply* with the recommendations and rulings' of the DSB."[3]

7. Let us review the facts. Canada's original request for consultations concerned the *final countervailing duty investigation determination* published on 2 April 2002, and its panel request alleged errors in that final investigation determination.[4] The original panel's findings with respect to

[1] E.g., Canada Second Written Submission, paras. 7 - 8.
[2] Canada Second Written Submission, paras. 6, 26 - 30.
[3] Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, para. 36.
[4] WT/DS257/3, 19 August 2002.

pass-through related solely to that final investigation determination. The Appellate Body stated that "[b]efore the Panel, Canada challenged a number of aspects of the final determination by [the Commerce Department] that led to the imposition of duties"[5] and the Appellate Body's findings and conclusions – including those with respect to the need for a "pass-through" analysis – thus related only to that final investigation determination.

8. Therefore, to implement the DSB's recommendations and rulings, Commerce issued a new determination – the Section 129 Determination – that revised the original final investigation determination by conducting the recommended pass-through analysis. By correcting the only "inconsistency" identified by the DSB with respect to the final investigation determination, the United States fully implemented the recommendations and rulings of the DSB to bring the measure into compliance with the SCM Agreement.

9. Long before there were any DSB recommendations and rulings to implement, and pursuant to long-standing, standard procedures, Commerce initiated the first assessment review, at the request of Canada, among others. The purpose of the assessment review was to determine the precise countervailing duties that would be levied on particular entries of merchandise entering the United States after the United States had already imposed the countervailing duty measure (in US parlance, after the publication of the countervailing duty order). This assessment review would have been conducted regardless of the existence of any dispute challenging the original investigation determination and it was nearly half over when the recommendations and rulings in this dispute were adopted.

10. Thus, Canada's repeated assertions that Commerce itself "purported" or "alleged" that it conducted the assessment review to implement the DSB's recommendations and rulings are inaccurate and have no basis.

11. Canada cannot deny that – in contrast to the assessment review – Commerce initiated the Section 129 proceeding for the specific purpose of addressing the DSB's recommendations and rulings. Indeed, the agreement of the parties on the "reasonable period of time" to implement the recommendations and rulings in this dispute was negotiated in the light of, and specifically refers to, the US procedures for implementing WTO reports[6] – that is, the Section 129 procedures.

12. Faced with the undeniable fact that the assessment review results were <u>not</u> taken to comply with the DSB's recommendations and rulings, Canada instead argues that the Panel should nonetheless consider them in this proceeding, because the assessment review results either (a) somehow rendered the Section 129 Determination "non-existent" or (b) were "inextricably linked" to the recommendations and rulings of the DSB.

13. Neither of these assertions is true.

The assessment review results did not render the Section 129 Determination "non-existent"

14. First, in no way did the assessment results render the Section 129 Determination non-existent. The final investigation determination challenged by Canada – a determination of the existence and the amount of the subsidy – established one of the prerequisites under Article 19.1 of the SCM Agreement for the imposition of a countervailing duty. That investigation determination did not establish the amount of duties that would be levied, or assessed, on the imports; that task is undertaken as part of the separate assessment review. The final investigation determination simply

[5] Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 12 February 2004, para. 1 ("Appellate Body Report").

[6] WT/DS257/13.

established one of the bases for imposing countervailing duties. The Panel should recall in this connection that the remedy Canada sought in the dispute before the original panel was the revocation of the countervailing duty order, which was based in part on the final investigation determination.

15. The Section 129 Determination, in implementing the recommendations and rulings of the DSB with respect to the final investigation determination, confirmed that the resulting imposition of countervailing duties on 22 May 2002, was consistent with the SCM Agreement. The assessment review could not, and did not, render that Section 129 Determination non-existent. Indeed, the very fact that Canada is, itself, challenging the Section 129 Determination shows that Canada believes that it is of ongoing effect and relevant to the issue of compliance.

16. Further, the Section 129 Determination was fully implemented, and revised the original final investigation determination in every respect necessary to implement the recommendations and rulings of the DSB. For instance, the Section 129 Determination revised the cash deposit rate established by the final investigation determination – a cash deposit rate that, under US law, stays in effect unless and until a party requests an assessment review. If no assessment review is requested, countervailing duties are assessed at the cash deposit rate.

17. Canada's allegation that the Section 129 Determination was "rendered non-existent" appears to be an allusion to the argument that the United States made in the dispute *Australia – Leather*, where withdrawal of the subsidy was non-existent. The situation there, however, is not at all analogous to the facts of this dispute.

18. First, in *Australia – Leather*, the United States was arguing that the panel should review whether a prohibited subsidy had actually been withdrawn, as specifically required by Article 4.7 of the SCM Agreement, when the repayment of a grant had been contingent on the simultaneous grant of a loan on non-commercial terms. In contrast, this proceeding involves the question of whether a measure has been brought into conformity with a WTO agreement.

19. Second, the *Australia – Leather* panel concluded that the subsidy had not been withdrawn at all, because the supposed repayment and the non-commercial loan were, in effect, a single transaction in which the subsidy simply shifted form. By contrast, in this dispute, the Section 129 Determination and the assessment review results are separate and independent actions. The simple fact is, the Section 129 Determination was made to bring the measure in dispute into conformity with the SCM Agreement as recommended by the DSB, whereas the assessment review was conducted for a completely unrelated reason. As such, the assessment review in no way affects that result of the Section 129 Determination, and Canada has not shown otherwise.

The Results of the Assessment Review are not "Inextricably Linked", either to the Section 129 Determination, or to the Recommendations and Rulings of the DSB.

20. In the alternative, Canada uses three WTO reports to argue that the assessment results are "inextricably linked" to the recommendations and rulings of the DSB, and therefore should be considered "measures taken to comply". These reports, however, only demonstrate further how the assessment review is not within the scope of this Article 21.5 proceeding.

21. We've just discussed one of those disputes, *Australia – Leather*, in which the panel reviewed both the measure that Australia claimed was taken to comply – the repayment of a subsidy grant – and another measure that Australia claimed was not taken to comply – the new non-commercial loan. The panel in that dispute concluded that the subsidy had not been withdrawn, because the supposed

repayment and the non-commercial loan were, as Canada quotes the panel, "inextricably linked elements of a single transaction."[7]

22. But, as we mentioned, that situation is very different from this one. In *Australia – Leather*, the repayment of the grant by the grant recipient was specifically and directly conditioned on the grant recipient receiving the non-commercial loan – there would have been no repayment at all if there had been no loan. It was on that basis that the panel found that the loan was "inextricably linked to the steps taken by Australia in response to the DSB's rulings in [that] dispute, in view of both its timing and nature."[8]

23. In this dispute, by contrast, there is no such connection between the Section 129 Determination and the assessment review results: they were not in any sense contingent on one another, nor were they in any sense part of a single transaction. The assessment review would have taken place regardless of whether there was a Section 129 proceeding under way, and, indeed, regardless of whether there even was a WTO dispute.

24. Canada similarly cites to the dispute *Australia – Salmon*, in which, in response to DSB recommendations and rulings, Australia modified its ban on salmon imports to permit imports that satisfied certain criteria. In what was obviously a response to the modification of the ban, Tasmania, one of Australia's sub-federal units, imposed its own ban. The Tasmanian ban did not arise from a proceeding initiated as a matter of domestic law requirements, irrespective of any WTO challenge. Rather, it was an ad hoc action taken after the DSB had made recommendations and rulings against an Australian import ban and after Australia had taken action to modify the ban. All of the evidence – both in terms of timing and subject matter – pointed to these bans being truly "inextricably linked". Therefore, that panel properly found that the Tasmanian ban was a measure taken to comply.

25. By contrast, in this case, the assessment review was initiated

- upon request of the parties (including Canada), *eight months before* the DSB's recommendations and rulings were even adopted,

- pursuant to a US statutory provision that requires initiation upon request on a specific schedule and under specific deadlines, and

- for the purpose of assessing countervailing duties on entries not previously examined – not for the purpose of implementing any recommendations or rulings.

Unlike the obvious "close connection" in *Australia – Salmon*, there is nothing that links the assessment review to the recommendations and rulings of the DSB in this dispute.

26. Finally, Canada tries to distinguish the findings in *EC – Bed Linens* from this dispute, claiming that the panel excluded the results of a review from that Article 21.5 proceeding because that review did not deal with the same "subject matter" as the original determination. Canada also cites *EC – Bed Linens* as establishing that it is appropriate for this Panel to review Commerce's actions with regard to a subsequent time period characterized by new data, including completely different import entries.

27. To the contrary, however, the *EC – Bed Linens* dispute demonstrates that a new determination that was made in a subsequent segment of an antidumping or countervailing duty proceeding – and

[7] Panel Report, *Australia – Subsidies Provided to Producers and Exporters of Automotive Leather – Recourse to Article 21.5 of the DSU by the United States*, WT/DS126/RW, adopted 11 February 2000, para. 6.50 ("*Australia – Leather*").

[8] *Australia – Leather*, para. 6.5.

not made to implement recommendations and rulings of the DSB – falls outside the jurisdiction of Article 21.5 panels. For instance, the fact that measures taken to comply might involve new facts does not justify expanding Article 21.5 proceedings to encompass measures not taken to comply. Indeed, this Appellate Body discussion cited by Canada has nothing to do with the question of what constitutes "measures taken to comply", but rather the question of whether those measures are "consisten[t] with a covered agreement".

28. In sum, the assessment review that Canada has attempted to sweep into this Article 21.5 proceeding has nothing in common with those measures considered to be "inextricably linked" or "closely connected" in other disputes. To the contrary, the assessment review results have no relation at all to either the Section 129 Determination or the recommendations and rulings. They are simply not measures taken to comply and are therefore outside this Panel's jurisdiction.

Contrary to Canada's arguments, respecting the jurisdictional mandate of Article 21.5 does not "ignore the purpose of compliance proceedings".

29. Canada has failed to show that the assessment review is a measure taken to comply in that it is "inextricably linked" to the recommendations and rulings of the DSB. Nor has Canada shown that measures taken to comply do not exist because the assessment review rendered the Section 129 Determination non-existent.

30. Canada therefore resorts to the argument that limiting the Panel's review only to the measures taken to comply – that is, not sweeping the separate assessment review into the Article 21.5 basket – somehow ignores the "purpose of compliance proceedings". The United States disagrees, for reasons which we will discuss shortly. But regardless, a baseless reference to the general "purpose of compliance proceedings" cannot direct a result that is not supported by a good faith reading of the text, in its context and in light of the object and purpose of the DSU.

31. Further, the United States does not understand how properly applying DSU Article 21.5 can result in "ignor[ing] the purpose of compliance proceedings". Contrary to Canada's arguments, with respect to the only claim found to be WTO-inconsistent – the pass-through analysis conducted in the final investigation determination – a review under Article 21.5 of the Section 129 Determination permits the prompt settlement of disputes: Canada complained about an inconsistency in the final investigation determination, and this Panel will review whether that inconsistency has been corrected.

32. What Canada appears to be seeking is to avoid the need to bring a separate WTO dispute against the United States on the separate assessment proceeding. Canada instead hopes to "kill two birds with one stone" – albeit improperly – by sweeping a review of the separate assessment proceeding into this Article 21.5 proceeding. Canada complains that having to initiate a separate dispute settlement proceeding with respect to an assessment review somehow ignores the purpose of compliance proceedings. However, in negotiating the DSU, Members agreed that the expedited procedures of Article 21.5 would only be available for two very specific questions: (1) the existence or (2) the consistency of measures taken to comply. Members did not agree that the special procedures under Article 21.5 would be available for any claim for which the complaining party felt it would be more convenient to use Article 21.5.

33. If Canada believes that an assessment review is conducted inconsistently with the SCM Agreement, it is within its WTO rights to request consultations with respect to that assessment review and, if appropriate, request a panel. Indeed, assessment reviews can present different legal issues and entail different obligations from final investigation determinations – in addition to involving completely different administrative records – that make a separate set of consultations entirely appropriate.

34. Moreover, Canada appears to suggest that the US system of retrospective duty assessments somehow compels the Panel, in the special case of the United States, to sweep the assessment review into this Article 21. 5 proceeding.[9] But there is nothing in Article 21.5 or in the SCM Agreement that requires a different interpretation of "measures taken to comply" for those Members that employ a retrospective duty assessment system, rather than a prospective one.

35. Canada suggested this morning, in paragraph 33 of its oral statement, that the United States had somehow conceded that the assessment review was inconsistent with US WTO obligations. Canada bases this suggestion on the absence of an explanation in the US submissions or oral statement of the pass-through analysis in the first assessment review. This is untrue. The United States has not discussed the assessment review because it falls outside of this Panel's jurisdiction. The United States does not in any sense concede that the pass-through analysis in the assessment review is inconsistent with WTO obligations.

Conclusion

36. In sum, Mr. Chairman and members of the Panel, the results of the first assessment review are not "measures taken to comply" and therefore fall outside the Panel's jurisdiction in this Article 21.5 dispute. Therefore, we reaffirm our request that the Panel so rule.

Pass-Through Analysis

Canada Bears the Burden of Proof

37. It is important to recall that Canada bears the burden of establishing a prima facie case of a WTO inconsistency. In its panel request, Canada specifically refers to three separate provisions: Articles 10 and 32.1 of the SCM Agreement and Article VI:3 of the GATT 1994.[10] Although Canada concludes that the United States has acted inconsistently with these provisions, it has failed to demonstrate any such inconsistency or to describe why any of the specific actions that form the bases of its arguments are inconsistent with these provisions. For instance, Canada challenges Commerce's arm's-length analysis yet fails to identify how that analysis is inconsistent with any of the cited provisions. Similarly, Canada challenges the pass-through benchmarks Commerce relied upon yet once again fails to identify any way in which these benchmarks are inconsistent with the cited provisions. Consequently, Canada has failed to make its prima facie case and for that reason alone the Panel should reject Canada's claims.

The United States Properly Implemented the DSB's Recommendations and Rulings

38. The substantive issue facing this Panel is whether the United States properly implemented the recommendations and rulings of the DSB in conducting its pass-through analysis with respect to the final investigation determination. The answer is clearly "yes". The positions of the United States with respect to its Section 129 Determination are more fully contained in our written submissions. This morning, we will not repeat all of the points made in those submissions but rather will briefly highlight what we consider to be significant issues as well as respond to the issues raised in Canada's second written submission. As to those issues not raised in this oral statement, we refer the Panel to our written submissions.

39. Initially, we will briefly outline Commerce's pass-through methodology. Next, we will discuss the nature of Commerce's arm's-length analysis and Canada's attempt to truncate that analysis. Then we will focus upon Canada's improper challenge to the benchmarks Commerce relied upon in conducting its pass-through analysis. Finally, we will address Canada's peculiar claim that

[9] Canada Second Written Submission, para. 27.
[10] WT/DS257/15.

US compliance with the express terms of the Appellate Body Report, was an effort by the United States to avoid its WTO obligations.

Pass-Through Methodology

40. The DSB determined that the United States acted inconsistently with certain of its WTO obligations when it failed in its final investigation determination to conduct a pass-through analysis with respect to two categories of arm's-length log sales between unrelated parties. To implement those recommendations and rulings Commerce was first required to obtain additional information from Canada relating to the POI. That information was requested through a series of questionnaires. Specifically, Commerce requested information relating to those log sales for which Canada was claiming that the subsidy did not pass through to the purchasing sawmill.

41. As a threshold matter, Commerce examined the data provided by Canada to determine whether the sales were between affiliated, that is, related, parties. Consistent with the DSB's recommendations and rulings, when Commerce found that the sales were between affiliated parties, it performed no further pass-through analysis. If the sales were identified as being between unaffiliated parties, Commerce examined the circumstances surrounding the transactions to determine whether the parties operated at arm's length. Where Commerce determined that the transaction was at arm's length, it next determined whether there was a competitive benefit, that is, whether the benefit "passed through" to the purchasing mill using market-determined benchmarks. Ultimately Commerce's analysis of arm's-length log sales between unaffiliated parties resulted in a reduction in the numerator of the *ad valorem* subsidy rate which in turn, had the effect of reducing the country-wide subsidy rate.

42. Consistent with the DSB's recommendations and rulings, Commerce conducted a pass-through analysis and based its determination upon what the record evidence demonstrated the facts to be.

Commerce Properly Conducted its Arm's-Length Analysis

43. There is no dispute between the parties that for a transaction to be eligible for consideration in Commerce's pass-through analysis, the DSB determined that the transaction must be between unrelated parties and be at arm's length.[11] Canada does not challenge Commerce's affiliation determinations, so we will not discuss those threshold determinations. Rather, the dispute between the parties concerns the interpretation of the term "arm's length" – a term that is not defined in the text of the SCM Agreement.

44. The Appellate Body found that both the SCM Agreement and the GATT 1994 require that Commerce establish that the benefit is passed through to the downstream processor where subsidies are bestowed directly on producers of an input product while the countervailing duties are to be imposed on processed products, "and where the input producers and downstream processors operate at *arm's length*".[12] Thus, where the two producers do not operate at arm's length, no pass-through analysis is required because the subsidy bestowed on the input producer benefits the producer of the processed product. The United States properly determined that whether entities operate at "arm's length" involves more than simply an examination of formal affiliation – rather, it involves analysis of whether one party effectively controls the other or whether the parties have roughly equal bargaining power.

45. Canada, however, conflates the issues of affiliation and arm's length arguing that an arm's-length determination requires nothing more than a determination of affiliation. Indeed, Canada's *per se* approach to arm's length is set forth in paragraph 62 of its first written submission when it

[11] Appellate Body Report, para 176(e).
[12] Appellate Body Report, para. 146 (emphasis in original).

states "that a transaction between unrelated parties is by definition an arm's-length transaction". Because Canada treats these disparate concepts as one, Canada contends that by analyzing whether such sales are, in fact, at arm's length, and then eliminating sales that are not at arm's-length from the pass-through analysis, Commerce somehow "presumed" pass-through. To the contrary, it is Canada that is presuming no pass through whenever there are sales between unaffiliated parties.

46. By contrast, the DSB recognized a distinction between arm's length and affiliation in its recommendations and rulings, noting that Commerce should have conducted a "pass-through analysis in respect of *arm's length* sales of *logs . . . to unrelated* sawmills".[13] Canada's approach which would end the analysis once affiliation is determined is thus inconsistent with the DSB's recommendations and rulings.

47. In contrast, and consistent with the DSB's recommendations and rulings, Commerce properly examined the circumstances surrounding the sales that Canada reported as occurring between unrelated parties to determine whether those transactions were at arm's length. Where parties to a transaction are not free to bargain with whomever they choose or to bargain on terms not encumbered by government mandates and restrictions that were imposed as a condition of obtaining the logs in the first place, Commerce properly determined that such transactions were not at arm's length.

48. The SCM Agreement, the GATT 1994 and the DSB's recommendations and rulings do not require that Commerce's arm's-length analysis be constrained in the fashion proposed by Canada. Indeed, as previously noted, although Canada generally alleges that Commerce's arm's-length analysis is inconsistent with WTO obligations, it fails to cite to any specific WTO provision that supports its position that an arm's-length analysis can be nothing more than an examination of affiliation.

49. As we will discuss next, the facts presented to Commerce demonstrate that under the Canadian stumpage system, many of the circumstances of the log sales are controlled by government mandates and other conditions that rendered those sales not at arm's length or otherwise ineligible for the pass-through analysis.

Commerce Properly Considered the Circumstances of the Sales in its Arm's Length Analysis

50. In our second written submission we detailed the government mandates and other conditions that Commerce identified in its Section 129 Determination as controlling, limiting or otherwise affecting the subject log sales. Briefly, the government-mandated restrictions include appurtenancy, local processing requirements, and wood supply agreements which dictate to the harvester those entities to which it must sell. These government mandates restrict the ability of a seller to act in its best interests when selecting from among potential buyers. Where parties are not able to negotiate freely, such sales could not be considered to be at arm's length.

51. Additionally, certain log purchase agreements were such that the purchasing mill controls significant aspects of the transaction or provided other goods or services as part of the transaction so that sales under these agreements could not be arm's-length sales. Canada does not deny the existence of these conditions (although the Government of British Columbia does contend, with no support, that it does not enforce the appurtenancy requirements contained in its tenure agreements). Rather, Canada argues that it is basic economics that these restrictions do not affect the arm's-length nature of the transactions between the parties.

52. Canada's view of introductory economics does not amount to a WTO obligation. **Canada's argument glosses over the reality of the system created by these mandates and conditions**. By way of example, where a subsidy is provided to an input producer who can only sell to a particular

[13] Appellate Body Report, para 176(e)(emphasis added, except that emphasis on "logs" is in original.)

purchaser, the purchaser is in a position substantially to dictate the price. Consequently, such a sale would not be at arm's length. The same result obtains where local processing requirements exist.

53. As noted above, these government mandates and other conditions are imposed as a condition of the tenures. Consequently, they go to the very heart of the issue Commerce is investigating. Contrary to Canada's assertion, as evidenced by the fact that Commerce has found arm's-length transactions in Canada's regulated market, Commerce is not requiring a marketplace free from regulation as a prerequisite for finding transactions to be at arm's length. However, because these mandates and conditions substantially control timber transactions in Canada, they were fundamental to Commerce's arm's-length analysis.

54. Finally, Commerce identified two additional factors – that are not exclusively arm's-length issues – that affected its pass-through analysis. Notably, for those transactions in which the purchasing mill paid the Crown stumpage fees directly to the government for logs obtained from the independent harvester, Commerce determined that no pass-through issue arose. Because the stumpage fee is the vehicle through which the Crown bestows the subsidy the purchasing sawmill *directly receives the benefit.* Canada misses the point when it argues that "[a]lthough the party writing the check may affect the observed log price, it will never affect the *value paid* by the sawmill for the logs."[14] Unlike the transactions identified by the DSB, in these transactions the sawmill is the direct recipient of the subsidy and thus there is no need to examine whether the benefit passed through to the purchasing mill. Moreover, because the very essence of the pass-through analysis is determining with whom the benefit resides, Canada's analogy to a situation in which a party generally satisfies an outstanding lien on behalf of another is irrelevant.[15]

55. Additionally, Commerce properly excluded from its analysis fiber exchange agreements between Crown tenure holders, which often involved, by way of example, exchanges of logs for chips, to meet appurtenancy and other harvesting requirements. These exchange agreements are not log sales but rather are tools by which tenured sawmills satisfy their appurtenancy and local processing requirements. Because such exchanges are not "sales" at all, there was no need for Commerce to conduct an arm's-length analysis of the transactions.

56. In sum, Canada has not established that Commerce's arm's-length analysis is in any way contrary to the SCM Agreement, the GATT 1994 or the DSB's recommendations and rulings.

The Panel Should Decline to Consider Canada's Challenge to Commerce's Benchmarks and in Any Event, Commerce Used Appropriate Market-Determined Benchmarks

57. Canada criticizes Commerce's benchmarks as not reflecting "market" conditions, but has thus far failed in its written submissions to specify in what way the benchmarks were inconsistent with the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings. More significantly, Canada failed to even identify its challenge to the pass-through benchmarks in its panel request. Consequently, not only has Canada failed to make a *prima facie* case that there is a WTO inconsistency, this claim is outside the Panel's terms of reference.

58. In terms of the substance, and as explained in the second written submission of the United States, a subsidy provided to the producer of an input product confers a competitive benefit on a downstream purchaser of the input when the price paid for the subsidized input is lower than a market-determined benchmark price for the same product. Thus, to determine whether a benefit "passed through" to the purchasing mill, that is, whether there was a competitive benefit to the purchasing mill, Commerce required market-determined benchmarks. Canada does not dispute the

[14] Canada Second Written Submission, para. 41 (emphasis in original).
[15] Canada Second Written Submission, para. 41.

necessity for such benchmarks but rather, argues that because Commerce's benchmarks include import prices, the benchmarks are not representative of market conditions in Canada.

59. In selecting market-determined benchmarks, Commerce used, where possible, the actual company-specific prices that the purchasing mill paid for logs harvested from private lands and for imported logs. Commerce requested in its supplemental pass-through questionnaires and accompanying pass-through appendices that Canada provide such data to assist Commerce in developing market benchmarks. As evidenced by Commerce's calculations, where those company-specific purchase data were available, Commerce used them. Where such data were not available, Commerce used publicly available prices for logs harvested from private lands and for imported logs.

60. Canada raises two separate challenges to the US benchmarks in its second submission. The first challenge relates solely to the benchmark developed for Saskatchewan. The second challenge relates to Commerce's inclusion of import prices in its benchmarks generally. We will discuss Canada's general challenge to the inclusion of import prices in the benchmarks before discussing Canada's specific challenge relating solely to Saskatchewan.

61. In developing its benchmarks, Commerce determined to use prices based on market conditions in Canada. Import log prices, like domestic log prices, reflect prices that purchasers in Canada paid for logs during the POI. Consequently, Commerce included import prices in its benchmarks. Despite the fact that these import prices are actual Canadian transaction prices, Canada argues that Commerce must ignore these prices. There is no basis, however, for doing so.

62. Moreover, Canada's claim that the import data are taken from an excessively broad tariff classification is misplaced. Canada collects data on several categories of imports of "wood in the rough . . . Other, coniferous" - "Poles," "Piles and fence posts," "Logs for pulping," and "Other," (the "Other" category is broken down by species).[16] Logs used for lumber production thus fall into this last category, which was the only category Commerce included in its benchmarks. **Although Canada speculates that other higher value products may also have been included in this last category, the evidence is to the contrary. For example, Canada states that imports of high-value veneer logs would also fall into this category. But Quebec - the province with by far the largest value of log imports - reported that veneer mills in Quebec used zero imported softwood logs during the period of investigation.[17] Additionally, contrary to Canada's statement in paragraph 46 of its second submission, pulp log imports were reported separately by Statistics Canada and were not included in Commerce's calculation.**

63. With respect to Saskatchewan, Canada provided no data regarding prices of private log sales in the province, and – as Canada notes – only very limited data on log imports. Accordingly, there was insufficient data on prices for logs purchased by sawmills in Saskatchewan. Commerce therefore developed a proxy based on prices paid by mills in Canada for logs of the same species as found in Saskatchewan. As elsewhere, Commerce treated all log purchases consistently, irrespective of whether they were purchased from domestic or imported sources.

64. In sum, the United States developed market-determined benchmarks which included import prices, where available, for use in its pass-through analysis. As previously noted, Canada has failed to allege any WTO inconsistency in Commerce's development of the benchmark.

[16] GOC 17 October 2003, Questionnaire Response at Exh. GOC-GEN-51 (relevant pages). Exhibit US – 11.

[17] GOC 28 June 2001, Questionnaire Response, Exhibit QC-S-5, at QC-11, and Quebec Exhibit 5. Exhibit US – 12.

65. As a final point, there is an error in paragraph 39 of the second written submission of the United States. Specifically, the word "unsubsidized" should be deleted from the first sentence of that paragraph.

Commerce Properly Investigated Categories of Sales Identified by the DSB

66. As discussed in both our first and second written submissions, the two transaction categories subject to Commerce's pass-through analysis were the transactions identified in the DSB's recommendations and rulings. Consistent with those recommendations and rulings, Commerce properly conducted a pass-through analysis with respect to transactions between unrelated (i) independent harvesters and sawmills, and (ii) tenured timber harvesters/sawmills and non-tenured sawmills. Canada alleges that Commerce's investigation of the second of these categories was nothing more than a "creative way" for the United States to avoid its obligation to conduct the pass-through analysis contained in the DSB's recommendations and rulings.

67. Canada is wrong. The Appellate Body specifically defined the second category of transactions for which it recommended a pass-through analysis. The term "sawmill", the purchasing mill in the second category, was defined as "an enterprise that processes logs into softwood lumber *and does not hold a stumpage contract*".[18] The seller in the second category was specifically identified as a "tenured timber harvester/sawmill".[19]

68. Canada, in effect, asks this Panel to find that in evaluating whether there is compliance with the DSB's recommendations and rulings, the Panel should ignore the express language used in those recommendations and rulings. Canada's approach makes no sense. Instead, consistent with the DSB's recommendations and rulings, Commerce accorded those terms the definitions established by the DSB. This Panel should do the same.

Conclusion

69. In conclusion, we want to thank the Panel again for this opportunity to respond to Canada's arguments in its written submissions, and we look forward to responding to any questions that the Panel may have.

[18] Appellate Body Report, fn. 151 (emphasis added).
[19] Appellate Body Report, fn. 150 (emphasis added).

ANNEX C

Submissions of Third Parties

ANNEX C-1

THIRD PARTY SUBMISSION OF CHINA

17 March 2005

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I. Introduction

1. China welcomes this opportunity to present its views in these proceedings involving the United States' compliance with the DSB recommendations and rulings in *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada*. China believes these proceedings relate to the correct understanding of Article 21.5 of the DSU and Article VI:3 of GATT 1994 as well as the rulings by the original Panel and the Appellate Body in the original dispute in which China has systemic interests.

2. In this third party submission, China will focus on the following two key issues:

(i) the threshold issue of whether the USDOC administrative review determination is properly before this Panel;

(ii) whether the five external factors identified by the USDOC can be used to exempt the US from conducting pass-through analysis as required by the rulings of the original panel and the Appellate Body with respect to sales of logs between tenured harvesters/sawmills and unrelated sawmills.

II. Whether the USDOC Administrative Review Determination Is Properly Before This Compliance Panel

A. The Threshold Issue Presented in These Proceedings

3. In the *Request for Establishment of A Panel*, Canada refers to the following measures by the US: (i) the Section 129 Determination[1]; and (ii) the First Administrative Review Determination (the "Review Determination")[2]. In its First Written Submission, Canada argues that the US, by adopting these "measures taken to comply", "continues to violate its obligations under Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the SCM Agreements"[3] and failed to implement the recommendations and rulings of the DSB. The US, in turn, request a preliminary ruling that the Review Determination is not a "measure[] taken to comply" and thus falls outside the scope of these Article 21.5 proceedings[4].

4. Thus, a threshold issue presented in this dispute is whether the Review Determination is properly before this compliance panel.

B. Terms of Reference of An Article 21.5 Panel

5. In China's view, WTO jurisprudence establishes that the mandate of an Article 21.5 panel is subject to two limitations.

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[1] *Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,305; *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*; *Notice of Amended Final Affirmative Countervailing Duty Determination and Notice of Countervailing Duty Order: Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 36,070.

[2] *Notice of Final Results of Countervailing Duty Administrative Review and Rescission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917; and *Issues and Decision Memorandum*: *Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*.

[3] First Written Submission of Canada, paras. 35~40.

[4] First Submission and Request for Preliminary Ruling of the United States (the "First Submission of the US"), para. 12.

6. First, the mandate of a compliance panel shall be confined by the coverage of the measures referred to by the complaining party in its panel request. If the parties to a dispute do not agree otherwise, a compliance panel, as an ordinary panel, shall have the standard terms of reference set forth in Article 7.1 of the DSU. Specifically, the outer edge of the terms of reference of a compliance panel shall be the scope of the panel request by the complaining party at a given dispute. This has been confirmed by many compliance panels.[5]

7. Second, the mandate of a compliance panel shall be limited by the scope of "measures taken to comply" with DSB recommendations and rulings. The Appellate Body in *Canada – Aircraft (Article 21.5 – Brazil)* held that,

> Proceedings under Article 21.5 do not concern just *any* measure of a Member of the WTO; rather, Article 21.5 proceedings are limited to those "measures *taken to comply* with the recommendations and rulings" of the DSB[6]. (original emphasis)

In *EC - Bed Linen (21.5)*, the Appellate Body explicitly stated that "[i]f a *claim* challenges a *measure* which is not a 'measure taken to comply', that *claim* cannot properly be raised in Article 21.5 proceedings."[7] (Original Emphasis)

8. Practically, there may be fewer disputes over whether a measure is cited by the complaining party in its panel request. Rather, many of the disputes rest with whether a particular measure, although cited by the complaining party, is a "measure[] taken to comply". This is exactly the case in this dispute.

C. China's Views on The Threshold Issue

9. In these proceedings, both parties seem to have no dispute on whether the Review Determination was cited by Canada in its panel request. As noted on the document WT/DS257/19, the parties to this dispute agreed that the Panel should have standard terms of reference. As a result, the Panel's terms of reference shall be defined by Canada's Request for Establishment of a Panel (WT/DS257/15). In that document, Canada manifestly referred to the Review Determination issued by the USDOC. However, "Article 21.5 proceedings are limited to those 'measures *taken to comply* with the recommendations and rulings' of the DSB"[8] and "it is, ultimately, for an Article 21.5 panel — and not for the complainant or the respondent — to determine which of the measures listed in the request for its establishment are "measures taken to comply"[9]. Therefore, the threshold issue in this dispute is whether the Review Determination cited by Canada in its panel request is properly before this panel.

10. In this dispute, it may be argued, on the one hand, that the Review Determination was made in a totally separate investigation procedure and based on the import data that is irrelevant to that of the original investigation. On the other hand, it is arguable that the two determinations at issue were made under the framework of the same set of proceedings which effectively affects import of softwood lumber from Canada and the Review Determination supersedes the Section 129 Determination. In China's view, the first argument relates to the question of whether the Review Determination is a "measure[] taken to comply" while the second argument concerns the matter whether the Section 129 Determination is rendered non-existent.

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[5] *EC - Bananas (21.5)*, WT/DS27/RW/ECU, para.6.5; *Australia - Leather (21.5)*, WT/DS126/RW, para.6.3.

[6] *Canada – Aircraft (Article 21.5 – Brazil)*, WT/DS70/AB/RW, para 36.

[7] *EC - Bed Linen (21.5)*, WT/DS141/AB/RW, para.78.

[8] *Canada – Aircraft (Article 21.5 – Brazil)*, WT/DS70/AB/RW, para 36.

[9] *EC Bed Linen (Article 21.5 – India)*, WT/DS141/AB/RW, para 78.

11. Initially, the Review Determination may not be properly categorized as a "measure[] taken to comply". This point has been elaborated by the US in its First Submission. The date of commencement of the review process was well before the date when the DSB adopted the panel and Appellate Body report. The Review Determination was not issued under the US domestic proceedings that are specifically enacted to address its violation of WTO rules concerning a countervailing duty measure (Section 129(b) of the *Uruguay Round Agreements Act*).

12. However, in China's view, the fact that the Review Determination is not a "measure[] taken to comply" does not lead to a decisive answer to the question of whether this measure is properly before this panel. China recalls that, on the basis of the plain language of Article 21.5, the purpose of the proceedings under this provision is to review and solve the dispute on "the *existence* or *consistency* with a covered agreement of measures taken to comply with the recommendations and rulings" of the DSB. China believes that "existence" and "consistency" are two distinct aspects of the subject measure. The latter involves review that is not only "limited to 'the issue of whether or not [a Member] has implemented the DSB recommendation'"[10], but also "in the light of any provision of any of the covered agreements."[11] On the other hand, the former relates to the status of the revised new measure. Both aspects are equally important though the "existence" matter is crucial in solving the threshold issue in these proceedings.

13. The dispute of *Australia – Automotive Leather (21.5 – US)* demonstrates similar fact pattern that deserves the reference by this Panel. In that dispute, Australia, subsequent to the DSB recommendations and rulings, ordered the repayment of the grants of A$8.065 million from Howe on 14 September 1999 and reported to the DSB that it had carried out the recommendations and rulings of the DSB. However, on the same date, Australia provided a loan of A$13.65 million on non-commercial terms to Howe's parent company, ALH. The U.S. requested an Article 21.5 panel and submitted that "it is clear that if the Panel can determine the "existence" of measures taken to comply with the ruling, it can consider whether the measures purportedly taken to comply were effectively rendered non-existent".[12] Australia maintained that the loan of A$13.65 was not part of the implementation of the DSB's rulings and recommendations which was not even notified to the DSB.[13] In considering this issue, the compliance panel said,

> The 1999 loan is inextricably linked to the steps taken by Australia in response to the DSB's ruling in this dispute, in view of both its timing and its nature. In our view, the 1999 loan cannot be excluded from our consideration without **severely limiting** our ability to judge, on the basis of the United States' request, whether Australia has taken measures to comply with the DSB's ruling. In the absence of any compelling reason to do so, we decline to conclude that a measure specifically identified in the request for establishment is not within our terms of reference. [14].

In China's view, in an Article 25.1 procedure, if the complaining party submits that a "measure[] taken to comply" is invalidated by a subsequent measure, the compliance panel should at least assess this claim that relates to the "measure[] taken to comply" on the basis of relevant facts – the subsequent measure. To exclude the second measure would put the panel at the risk of failing to make a comprehensive and well-founded judgement on the **existence** of a measure taken to comply with DSB recommendations and rulings.

14. As China understands, the US applies a retrospective countervailing duty assessment system. Under such a system, the results of a review (if conducted), not only determine the duty that shall be

[10] *Canada - Aircraft (21.5)*, WT/DS70/AB/RW, para.40.
[11] *Australia - Salmon (21.5)*, WT/DS18/RW, para.7.10.
[12] *Australia – Automotive Leather (21.5 – US)*, WT/DS126/RW, para. 6.2.
[13] *Australia – Automotive Leather (21.5 – US)*, WT/DS126/RW, para. 6.1.
[14] *Australia – Automotive Leather (21.5 – US)*, WT/DS126/RW, paras. 6.5.

assessed on the goods imported during the period of review, but also establish the amount of cash deposit for future imports of the subject product following the review. In this sense, the results of a review may be deemed to replace the original determination except in certain extraordinary cases (e.g., in case where the amount of subsidization found to be zero in a review the result of which will not lead to the termination of the original determination). Thus, China believes, due to the countervailing duty assessment system adopted by the US, the results of an administrative review may, at least in form, replace the original final determination.

15. In the particular factual circumstance of this dispute, the Review Determination was announced ten days after the Section 129 Determination took effect. Thus, the Review Determination established a new rate for cash deposit for the goods from Canada and replaced the rate in the Section 129 Determination. Such changes in the applicable duty rate deserve further consideration on whether the Review Determination, **in substance**, rendered the non-existence of the Section 129 Determination. Therefore, China is of the view that the facts presented by Canada in these proceedings, at least, have demonstrated that there is likelihood that the Review Determination may nullify the Section 129 Determination.

16. On the basis of the above, it follows that if the Review Determination is found not to be a "measure[] taken to comply", it is still of importance to establish whether, as a matter of fact, the Section 129 Determination is nullified by the Review Determination and therefore, no "measure[] taken to comply" exists. In China's opinion, in order to perform the duty of "mak[ing] an objective assessment of the matter before it" as required by Article 11 of the DSU, it is advisable for the Panel to keep the Review Determination within its terms of reference instead of disregarding it at the very beginning of the procedure. In the meantime, however, China wishes to emphasize that, if the Review Determination is held not to be a measure taken to comply, the panel need only review the Review Determination to the extent that it can make a ruling on whether the Section 129 Determination was rendered non-existent and it is not the task of this Panel to review the Review Determination as a "measure[] taken to comply" in parallel with the Section 129 Determination.

17. Furthermore, it has been consistently ruled by compliance panels that it may be appropriate to consider events occurring until the date of panel request.[15] Such a view supports the position that this Panel should consider the Review Determination, as relevant facts, which happened prior to the panel request.

18. In summary, China is of the opinion that, although the Review Determination may not be a measure taken to comply, it is closely linked to and may have an important effect on the existences of the purported measure taken to comply – the Section 129 determination. On such basis, China believes it is the mandate of this Panel to consider the Review Determination in these proceedings. China suggests that the Panel may assess: (i) whether Section 129 Determination fully implements the DSB recommendations and rulings and is consistent with the covered agreements; and (ii) if it does, whether the Review Determination invalidates the Section 129 Determination and consequently renders the non-existence of the latter.

III. Whether "Arm's-Length Transaction" and "Non-affiliation" Are One and The Same Condition or Two Separate Conditions to Necessitate A Pass-through Analysis

19. In its First Written Submission, Canada argues that the US failed to conduct pass-through analysis for three reasons, one of which is the USDOC imposed two conditions to limit the number of log transactions requiring analysis. These two conditions are: (i) the transacting parties are unrelated;

[15] See, *e.g.*, *EC – Bed Linen (21.5)*, WT/DS141/RW, para. 6.28; *US – Shrimp (21.5)*, WT/DS58/RW, paras. 5.12~5.13.

and (ii) none of the external factors identified by the USDOC exists.[16] The US, in its First Submission, does not deny its application of these two conditions.[17]

20. In the following, China would like to share with the parties to this dispute as well as this Panel its views on this disputed issue.

A. The Analysis of the Appellate Body

21. In the course of reaching its conclusion, the Appellate Body largely relied on the interpretation of Article VI:3 of the GATT 1994. In its report, the Appellate Body stated that,

> The phrase "subsid[ies] bestowed ... indirectly", as used in Article VI:3, implies that financial contributions by the government to the production of inputs used in manufacturing products subject to an investigation are not, in principle, excluded from the amount of subsidies that may be offset through the imposition of countervailing duties on the processed product. Where the producer of the input is **not the same entity** as the producer of the processed product, it cannot be presumed, however, that the subsidy bestowed on the input passes through to the processed product. In such case, it is necessary to analyze to what extent subsidies on inputs may be included in the determination of the total amount of subsidies bestowed upon processed products. For it is only the subsidies determined to have been granted upon the processed products that may be offset by levying countervailing duties on those products.[18] (original emphasis in italic and added emphasis in bold)

The Appellate Body seemed to be of the view that if subsidies are bestowed on an entity different from the producer of the subject product, pass-through of subsidies cannot be presumed. In this respect, the Appellate Body did not emphasize that the transactions between the two entities shall be free of interference by any external factor. In addition, the Appellate Body found further supports from the definition of subsidy in Article 1 of the SCM Agreement as well as its interpretation of "benefit" in Canada – Aircraft.[19] In such analysis, the Appellate Body also focused on whether the cumulative condition in Article 1 of the SCM Agreement are met for the producer of the subject products and whether the producer of the subject product is an indirect recipient. All such legal analysis, in China's view, relies on the presumption that the two entities, producer of the input and producer of the subject product, are not the same entity.

22. The Appellate Body, in its analysis, did mention from time to time the term "arm's-length transactions". However, it did not put forward the implication of this term. Neither did it base its analysis on the presumption that the transactions at issue are free from influence by any external factors.

B. The Rulings of the Original Panel and the Appellate Body

23. Paragraph 167(e) of the Appellate Body Report is as follows,

> upholds the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of logs by

[16] First Written Submission of Canada, paras. 53 and 59.

[17] See the First Submission of the US, para. 34. The US argues that "[c]ontrary to Canada's arguments, nothing in the SCM Agreement, the GATT 1994, or the DSB's recommendations and rulings supports Canada's argument that an arm's-length analysis should be restricted to, in essence, a per se test based on affiliation alone".

[18] *US – Lumber CVDs Final*, WT/DS257/AB/R, Para. 140.

[19] *US – Lumber CVDs Final*, WT/DS257/AB/R, Paras. 142~143

> tenured harvesters/sawmills to unrelated sawmills is inconsistent with Articles 10 and 32.1 of the SCM Agreement and Article VI:3 of the GATT 1994;

This ruling does mention the terms "arm's length sales" and "unrelated" in parallel. However, referring to paragraph 7.99 of the original Panel Report would easily exclude any potential confusion that may be caused by the use of these two terms, which reads,

> We therefore conclude that, for the reasons set forth above, the USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to **unrelated** sawmills producing subject softwood lumber; (emphasis added)

The above ruling does not refer to "arm's-length transactions" as an extra condition to necessitate pass-through analysis. The condition is only that the tenure-holding timber harvesters are unrelated to sawmills. If the Appellate Body intended to insert "arm's-length transaction" as an addition condition, it should have said so and should have partially reversed the original panel's ruling on this matter. Therefore, the term "arm's-length transactions" in the ruling of the Appellate Body can be understood to bear the same meaning as that of "unrelated".

C. China's View on the Issue of Pass-through

24. In China's view, under the particular factual circumstances of this dispute and the countervailing duty investigation on softwood lumber, it is not necessary to satisfy the test of five external factors identified by the USDOC in order to require for a pass-through analysis.

25. First, China agrees with the analysis by the Appellate Body that an instance that require for pass-through analysis is one where the direct recipient of the subsidies at issue is not the same entity as the producer of the countervailed subject product. In this respect, the meaning of the so-called "same entity" is obvious – both entities are not related to or affiliated with each other in any other way so that they cannot be treated as one and the same. Such an instance does not imply that the transactions at issue should be free of interference by any of the five external factors identified by the USDOC.

26. Second, it is possible that the five external factors may affect the transactions between the separate entities and thereby influence the pass-through of the direct subsidies on the production of logs. For example, due to limitations on log sales in Crown tenure contracts, the tenured harvester may not sell its products to the sawmills at fair market value. As a result, the transaction price may be lower than fair market value through which, subsidies on logs pass through to the production of the subject products. In China's view, it is the external factors and, potentially, other unknown factors that cause the transaction price to be below fair market value and thereby, result in pass-through of subsidies.

27. China further submits that the influence by any external factor can be fully taken into account if a proper pass-through test is carried out. By choosing a permissible market benchmark, the investigating authorities could precisely calculate the part of benefits that are passed through to the purchasers of logs. Conversely, if the investigating authorities rule that, due to the existence of external factors, pass-through of subsidies need not be analyzed and can be presumed in its totality, the calculated subsidy amount would not reflect the actual amount of benefits that are actually bestowed indirectly on the production of the subject product. Such an approach would most likely lead to imposition of countervailing duty in excess of subsidies bestowed "directly, or indirectly" on the subject product in violation of Article VI:3 of the GATT 1994.

28. On the basis of the above, China is of the view that the five external factors identified by the USDOC could not exempt the US from conducting pass-through analysis with respect to sales of logs between unrelated harvesters/sawmills and sawmills.

IV. Conclusion

29. In conclusion, China is of the following views:

(i) Although the Review Determination may not be a measure taken to comply with the DSB recommendations and rulings at issue, it is closely linked to and may have an important effect on the existences of the purported "measure[] taken to comply" – the Section 129 determination; it is the mandate of this Panel to consider the Review Determination in these proceedings from the perspective of whether it invalidates the Section 129 Determination;

(ii) The five external factors identified and applied by the USDOC in the Section 129 Determination could not exempt the U.S. from conducting pass-through analysis as required by the rulings of the original panel and the Appellate Body with respect to sales of logs between unrelated harvesters/sawmills and sawmills.

ANNEX C-2

ORAL STATEMENT OF CHINA

21 April 2005

Introduction

1. Mr. Chairman, members of the Panel, it is our great honor to appear before you today to present the views of China as a third-party to these proceedings. As the Panel already has our written submission, we do not intend to restate all the comments contained in that document. Rather, we seek to offer the Panel a concise synopsis of the views of China in regards to the current dispute between Canada and the United States. In short, the issues we will focus on today pertain to (1) whether the administrative Review Determination of the US Department of Commerce is properly within the mandate of this Panel and (2) whether the five external factors identified by the US Department of Commerce exempt the US from conducting a pass through analysis as required by the original Panel and the Appellate Body in their rulings.

USDOC Administrative Review Determination

2. China is of the opinion that the mandate of an Article 21.5 panel is subject to two limitations. First, the mandate of a compliance panel shall be confined by the coverage of the measures referred to by the complaining party in its panel request. Second, as held by the Appellate Body in *Canada - Aircraft (Article 21.5 – Brazil*), "Article 21.5 proceedings are limited to those 'measures taken to comply with the recommendations and rulings of' the DSB."[1]

3. Applying the first limitation to this dispute, it seems indisputable that Canada specifically and explicitly refers to the DOC's Administrative Review Determination in its panel request and therefore, this measure passes the test of the first limitation. However, to reiterate what was said above, the mandate of this Panel shall be limited to those "measures taken to comply with the recommendations and rulings" of the DSB.

4. In this regard, given the facts of this dispute, China tends to agree with the US that the Review Determination may not be properly categorized as a "measure taken to comply". However, while China does not consider the Review Determination to be a "measure taken to comply," it also does not believe that a decisive answer has yet been reached in regards to whether the Review Determination is properly before this Panel. The underlying purpose of these proceedings is to review and to resolve this particular dispute as to "the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings" of the DSB. Although the words "existence" and "consistency" are of equal importance, in this particular dispute, China surmises that the correct interpretation of "existence" will be crucial to the resolution of whether the Review Determination is properly before the Panel.

5. The dispute of *Australia – Automotive Leather (21.5 – US*) offers pertinent insight concerning such interpretation and deserves the attention of this Panel. In a similar fact pattern to the current dispute, Australia, on the one hand, ordered the repayment of a grant, a move that was purported to withdraw the illegal subsidy; while on the other hand, it provided a non-commercial loan to the parent company of the subsidy recipient. The United States requested an Article 21.5 panel. That compliance panel stated that the loan in dispute was "inextricably linked to the steps taken by

[1] *Canada – Aircraft (Article 21.5 – Brazil)*, WT/DS70/AB/RW, para.36.

Australia in response to the DSB's ruling . . . in view of both its timing and its nature".[2] The panel determined that the "loan cannot be excluded from our consideration without severely limiting our ability of judge, on the basis of the United State's request, whether Australia has taken measures to comply with the DSB's ruling".[3] Consequently, believing there to be no presence of a compelling reason to act otherwise, the panel declined "to conclude that a measure specifically identified in the request for establishment . . ."[4] was not in the panel's terms of reference.

6. Consequently, in China's view, because Canada has submitted that a "measure taken to comply" has been invalidated by a subsequent measure, this Panel should at least be allowed to assess the relationship between the Section 129 Determination and the Review Determination. To exclude such an assessment would put this Panel at the risk of failing to make a comprehensive and well-founded judgment as to the "existence" of a measure taken to comply with the relevant DSB recommendations and rulings.

7. Looking at the particular facts of this dispute, the Review Determination was announced ten days after the Section 129 determination took effect which resulted in the establishment of a new rate for the cash deposit for Canadian goods and replaced the rate in the Section 129 determination. Such facts warrant further consideration on whether these changes rendered the non-existence of the Section 129 determination.

8. For all the reasons above, China believes that while the Review Determination itself may not be classified as a "measure taken to comply," it is inextricably linked to the steps taken by the US in response to the DSB's ruling in both its timing and its nature. Because excluding the Review Determination would severely limit the Panel's ability to judge, upon Canada's request, whether the US has taken measures to comply with the DSB's rulings and recommendations, China concludes the Review Determination to be within this Panel's mandate.

The Pass-Through Analysis

9. We now turn briefly to the second issue of the dispute, namely that of the pass-through analysis conducted by the US. Specifically, the issue revolves around the DOC imposing two conditions that in effect limited the number of log transactions that were subjected to a pass-through analysis.

10. The DOC effectively required that relevant log transactions (1) be conducted between unrelated parties; and (2) satisfy an "arm's length transaction" test before a pass-through analysis was necessitated. As a result, the question ultimately becomes whether the phrases "arm's length transaction" and "unrelated" are one and the same or rather distinctive terminology.

11. In its report, the Appellate Body seemed to be of the view that if subsidies are bestowed on an entity different from the producer of the subject product, then a pass-through of subsidies cannot be presumed. However, the Appellate Body did not intimate that the transactions between the two entities had to be free of interference by external factors. Neither did it base its analysis on such a premise.

12. Referring specifically to paragraph 167(e) of the Appellate Body Report, in which the Appellate Body affirms the original Panel's finding with respect to sales of logs by tenured harvesters/sawmills to sawmills, the phrases "arm's length sales" and "unrelated" are mentioned in parallel. However, looking at paragraph 7.99 of the original Panel Report, which the Appellate Body has purportedly affirmed, there is no mention of the phrase "arm's length transactions" or "arm's

[2] *Australia – Automotive Leather (21.5 – US)*, WT/DS126,RW, para.6.5.
[3] *Id.*
[4] *Id.*

length sales"; rather the only condition referenced is that the parties be unrelated. If the Appellate Body had intended to impose an extra condition, as the US actually did, it should have said so and partially reversed the original Panel's rulings. Therefore, China believes that the phrase "arm's length transactions" in the ruling of the Appellate Body should be construed to bear the same meaning as that of "unrelated".

13. Finally, China would like to present its own views on the five external factors identified by the US DOC. China believes that it is not necessary to satisfy this test of five external factors in order to require a pass-through analysis. China submits that an instance requiring a pass-through analysis is one where the direct recipient of the subsidies at issue is not the same entity as the producer of the countervailed subject product. Such an instance does not require the transactions to be free of influence by any external factors.

14. In addition, China believes that the five external factors may themselves be responsible for resulting in the pass-through of subsidies. However, to skip a pass-through analysis would presume that the subsidies are passed through in its entirety. Such an approach would most likely exaggerate the actual benefit indirectly bestowed on the subject product producers. China believes, by using an appropriate pass-through analysis, the effects of the five external factors can be fully accounted for without incorrectly calculating the actual amount of benefit on the subject product producers.

Conclusion

15. Mr. Chairman, that concludes the third-party statement of China. Thank you very much for the attention.

ANNEX C-3

THIRD PARTY SUBMISSION BY THE EUROPEAN COMMUNITIES

17 March 2005

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I. INTRODUCTION

1. The European Communities (EC) welcomes this opportunity to present its views in this DSU Article 21.5 proceeding. Canada claims that the United States has failed to implement the recommendations and rulings of the DSB in *United States –Lumber CVD Final*. The Appellate Body found that the countervailing duty imposed on softwood lumber was not based on a pass-through-analysis ensuring that the numerator is not artificially inflated through non-subsidised arm's length sales.[1]

2. The United States informed the DSB on 17 December that it had implemented its recommendations and rulings through a determination pursuant to Section 129(b) of the *Uruguay Round Agreements Act* ("Section 129 determination"). The Section 129 determination reduced the original rate of 18.79% to a rate of 18.62% (because of no pass-through in some cases) and was effective on 10 December 2004.[2] However, ten days later, the first administrative review[3] of the countervailing duty order kicked in, establishing a definitive countervailing duty rate for the period of review and replacing the amended Section 129 countervailing duty cash deposit rate with a new cash deposit rate (17.18%, not containing any reduction resulting from a lack of pass-through).[4]

3. Canada claims that the United States failed to implement the recommendations and rulings of the DSB because neither the Section 129 determination nor the administrative review carry out the pass-through analysis required by Articles VI:3 of the GATT 1994 and Articles 10 and 32.1 of the *SCM Agreement*.[5]

4. The United States has raised a preliminary objection contending that the administrative review is not a measure "taken to comply" within the meaning of Article 21.5 of the DSU and therefore not within the jurisdiction of this 21.5 Panel.[6] According to the United States, the administrative review is legally separate from the original investigation/ Section 129 determination and concerns new factual data.[7] The United States relies on *EC – Bed linen 21.5*, to argue that annual administrative review measures are entirely new determinations and therefore not a measure "taken to comply" within the scope of Article 21.5 proceeding.[8]

5. The EC considers that the US arguments are entirely misconceived. The US view (if accepted) would turn the US system of countervailing duty assessment into a moving target that escapes the WTO disciplines. Given that WTO jurisprudence is limited, the EC will confine this third party brief to this important jurisdictional question. As will be detailed below:

- Article 21.5 panels, in principle, have jurisdiction on all factual and legal matters relating to the resolution of the original dispute (as defined by that panel's terms of reference);

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[1] Appellate Body Report, *United States – Lumber CVD Final*, adopted on 17 February 2004.

[2] 19 U.S.C. § 3538(b). *Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*, 6 December 2004; *Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products From Canada*, 69 Fed. Reg. 75,305 (Dep't Commerce 16 December 2004).

[3] Referred to as the "assessment review" in the US First Written submission.

[4] *Notice of Final Results of Countervailing Duty Administrative Review and Rescission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce 20 December 2004); and *Issues and Decision Memorandum*: *Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*, December 13, 2004.

[5] panel Request (WTDS257/15), Canada's First Written Submission, para. 72.

[6] US First Written Submission, para. 12.

[7] US First Written Submission, paras. 21-24.

[8] US First Written Submission, paras. 15-16.

- The measure to be reviewed by this DSU Article 21.5 Panel is the continued application of a countervailing duty on the basis of the administrative review (superseding both the original determination and the Section 129 review).

6. This submission concludes that the Panel should dismiss the preliminary objection made by the United States. However, the EC wishes to clarify that it does not take a position on whether or not the administrative review complies with the recommendations and rulings of the DSB. The EC expects to provide its views on this substantive issue at the oral hearing (after having received the parties' rebuttal submissions).

II. THE SCOPE OF DSU ARTICLE 21.5 PROCEEDINGS

7. The scope of DSU Article 21.5 proceedings has several aspects that have not yet been fully clarified in WTO jurisprudence. Some jurisdictional issues relate to the claims that can be made in a DSU Article 21.5 proceeding. Here, the Appellate Body has already clarified that panels are to review the "totality" of claims relating to the consistency of that measure with the covered agreements[9] (continuing violations, new violations and consequential violations of the covered agreements). The precise issue before this Panel is whether the phrase "taken to comply" limits the 21.5 Panel's jurisdiction to reviewing only a measure explicitly taken to comply (here the Section 129 review) as opposed to an administrative review.

8. Article 21.5 of the DSU provides in relevant part:

> Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel. The panel shall circulate its report within 90 days after the date of referral of the matter to it. When the panel considers that it cannot provide its report within this time frame, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report.

9. Contrary to what the US argues, the phrase "taken to comply" cannot be read to limit the 21.5 proceeding to those measures that were explicitly taken to replace the measure at issue in the original proceedings. The phrase "taken to comply" must be read together with its immediate and broader context as well as the purpose of the DSU to reach a prompt solution of a dispute.

10. Most importantly, it is preceded by the term "existence" and followed by the expression "with the recommendations and rulings of the DSB". This suggests that the role of a 21.5 Panel is different from the task of an original Panel. While the original Panel is faced with a dispute relating to a precise measure, the 21.5 Panel is tasked to assess whether or not there is a failure to comply and whether or not the original dispute has been resolved.

11. Indeed, the broader purpose of Article 21.5 of the DSU is to secure the solution of a dispute between two WTO Members relating to the measures brought before the original Panel. This purpose is reflected in Article 3.3 of the DSU which reads;

> The prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective functioning of the

[9] Appellate Body Report, *United States – Shrimp (21.5*) , para. 87.

> WTO and the maintenance of a proper balance between the rights and obligations of Members.

12. Moreover, Article 3.7 of the DSU clarifies that Article 21.5 proceedings form part of the adjudication of an initial dispute by determining whether the defendant has withdrawn the measure or otherwise complied. Article 3.7 of the DSU reads:

> In the absence of a mutually agreed solution, the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the provisions of any of the covered agreements. The provision of compensation should be resorted to only if the immediate withdrawal of the measure is impracticable and as a temporary measure pending the withdrawal of the measure which is inconsistent with a covered agreement. The last resort which this Understanding provides to the Member invoking the dispute settlement procedures is the possibility of suspending the application of concessions or other obligations under the covered agreements on a discriminatory basis vis-à-vis the other Member, subject to authorization by the DSB of such measures.

13. This particular nature of the DSU Article 21.5 proceeding was explicitly recognised by the Panel in *Australia – Salmon (21.5)* which even considered a measure taken during the Article 21.5 proceeding on the basis of the following consideration:

> To do otherwise would, in our view, go against the principle of prompt settlement of disputes and could hamper implementation of both DSB recommendations in the original dispute and our findings in this case.[10]

14. Although the Appellate Body has not yet been faced with the precise point at issue here, it has already confirmed the above principle in *Canada – Aircraft 21.5*:

> In our view, the phrase "measures taken to comply" refers to measures which have been, or which should be, adopted by a Member to bring about compliance with the recommendations and rulings of the DSB. In principle, a measure which has been "taken to comply with the recommendations and rulings" of the DSB will *not* be the same measure as the measure which was the subject of the original dispute, so that, in principle, there would be two separate and distinct measures34: the original measure which *gave rise* to the recommendations and rulings of the DSB, and the "measures taken to comply" which are – or should be – adopted to *implement* those recommendations and rulings.[11]

15. Moreover, the Appellate Body clarified in the accompanying footnote 34:

> We recognize that, where it is alleged that there exist *no* "measures taken to comply", a panel may find that there is *no* new measure.

16. The Panel in *EC – Bed linen*, on which the United States relies, based itself explicitly on the *Australia – Salmon 21.5* case law and only discarded later review measures adopted by the EC as they were:

[10] Panel Report, *Australia – Salmon (21.5)*, para. 7.21.
[11] Appellate Body Report, *Canada – Aircraft 21.5*, para. 36 (footnote omitted).

> not so clearly connected to the panel and Appellate Body reports concerned, both in time and in respect of the subject-matter, that any impartial observer would consider them to be measures "taken to comply".[12]

17. It is important to note that the two measures in *EC – Bed linen* were not dismissed from the scope of that 21.5 proceeding because they were "review measures". They were dismissed because they did not relate to the original dispute between the EC and India.

18. The EC submits that the case-by-case test applied by the Panel in *EC – Bed linen* should be further interpreted in line with the above considerations. In particular, it is the EC's submission that the scope of the 21.5 proceeding is determined by all aspects of the measure giving rise to the initial dispute. The purpose of the 21.5 proceeding is to determine whether or not the defendant has complied by either withdrawing that measure or bringing it otherwise in full compliance with the covered agreements. Whether a measure is taken to comply must then be decided on a case-to-case basis having regard to the original dispute (as defined by the terms of reference of the Panel) and the particular obligations of the covered agreement at issue.

19. As already confirmed by the DSU Article 21.5 Panel in *EC – Bed linen*, it is for the Panel alone to determine which measures it reviews when determining whether or not there is compliance.[13] Moreover, the appropriate date for assessing the compliance of a Member with the recommendations of the DSB is the date of establishment of the Article 21.5 panel.[14]

III. IS THE ADMINISTRATIVE REVIEW WITHIN THE SCOPE OF THIS PROCEEDING?

20. Canada claims that the United States failed to comply with the rulings and recommendations of the DSB (pass-through analysis) because none of the measures taken by the United States carries out such pass-through analysis.

21. The United States defends itself legally by arguing that the administrative review is a separate measure from the (i) original determination and (ii) Section 129 determination and, hence, not before the Panel.

22. The US view is based on the assumption that the measures to be attacked in countervailing duty cases are the determinations made by the investigating authorities. This is false. As is clarified in Article 10 of the *SCM Agreement*, the measure of concern is the "imposition of a countervailing duty", defined as a "special duty levied" for the purpose of offsetting a subsidy. The WTO Member imposing the countervailing duty is under the obligation to demonstrate through an investigation and determination that such duty is not "in excess of the … subsidy" as required by Article VI:3 of the GATT 1994. Therefore, the accompanying determinations play a significant role in assessing whether the duty is in excess of a subsidy. However, it is the duty itself that interferes with trade and is the measure of concern. To the extent a countervailing duty is not imposed on the basis of a proper determination, it is incompatible with WTO law.[15]

23. The United States has a retrospective system of imposing countervailing duties. The administrative review at hand in this case is a hybrid instrument. It fixes the final duty rate for the assessment period with retrospective effect. It is similar to a retrospective assessment within the meaning of Article 9.3 of the *Anti-Dumping Agreement* and it certainly is not a fully-fledged review

[12] Panel Report, *EC – Bed linen 21.5*, para. 6.17.
[13] Panel Report, *EC – Bed linen 21.5*, para. 6.15.
[14] Panel Report, *United States – Shrimp 21.5*, paras. 5.12-5.13.
[15] See description of the measure in Appellate Body Report, *United States – Lumber CVD Final*, para. 2.

of both the subsidy and injury within the meaning of Article 21 of the *SCM Agreement*.[16] Significantly, the administrative review does not change the date of the expiry of the measure under Article 21.3. The administrative review happens to change the cash deposit rate provisionally for future imports, but only subject to a further annual review in the future.

24. While footnote 52 of the *SCM Agreement* recognises the existence of such annual reviews used in a retrospective system, it does not, as suggested by the United States[17], recognise that these types of administrative review are separate from the original determination (and or a Section 129 determination).

25. The United States has not disputed Canada's characterisation of the administrative review as superseding both the original countervailing duty determination and the Section 129 determination.[18] As explained by the United States, the Section 129 determination exclusively focused on the original investigation and partially redid it. However, that Section 129 determination was only in place for 10 days. It was then superseded by the administrative review which definitively fixed the duties for the relevant period. At the date of the establishment of the Panel (14 January 2005) only the administrative review was effectively in place.

26. According to WTO jurisprudence, a measure that essentially replaces an earlier measure remains within the terms of reference of an original Panel.[19] *A fortiori*, a 21.5 Panel must be in a position to assess whether an annual administrative review determination that confirms and supersedes the original determination relating to the same countervailing duty constitutes a "continuing violation".

27. Contrary to what the US attempts to argue, the Panel in *EC – Bed linen 21.5* does not stand for a general proposition that any review measure is outside the scope of a 21.5 proceeding. As noted already under point 17 above, the review measures at issue in that case were entirely different in nature. The EC applies a prospective system of assessing duties and therefore does not carry out such annual administrative reviews. The measures at hand in *EC – Bed linen* were either specific reviews of anti-dumping duties imposed on exporters from other Members (Egypt and Pakistan) or entirely new determinations in a review based on results of an event subsequent to the EC having adopted the implementing measure in *EC – Bed linen.*

28. Also the final US argument that it would not be possible to fully assess a new set of facts relating to an assessment review, based on a wholly new administrative record, within the 90 day period prescribed by Article 21.5 and that therefore administrative reviews must be subject to a different proceeding[20], is without merit. The Appellate Body already recognised that the examination of an Article 21.5 measure can require assessment of a new set of facts.[21] The 90 day period reflects the right of the complaining Member to a prompt resolution of the original dispute by determining whether or not compliance exist before he may resort to suspension of concessions.

29. Accepting the US view that the administrative review is not subject to a DSU 21.5 Panel review would turn the US system of duty assessment into a moving target that escapes from countervailing duty disciplines. Each administrative review would have to be subject to a new panel request, and by the time the panel, Appellate Body and implementation procedure was completed,

[16] Panel Report *US – Softwood Lumber (Preliminary)*, para 7.151.
[17] US First Written Submission, para. 21 and footnote 23.
[18] Canada's First Written Submission.
[19] See most recently, Panel Report *Dominican Republic – Cigarettes*, paras. 7.11-7.21
[20] US First Written Submission, para. 90.
[21] Appellate Body Report, *Canada – Aircraft 21.5*, para. 41. See also, Appellate Body Report, *United States – Shrimp 21.5*, para. 86.

another administrative review would have overtaken the results of any Section 129 determination. A new panel would have to be started against this review, creating a "Groundhog Day" situation.

IV. CONCLUSION

30. For the above reasons, the EC considers that the Panel has full jurisdiction over the administrative review measure in this case and that the US preliminary objection should therefore be dismissed.

ANNEX C-4

ORAL STATEMENT
BY THE EUROPEAN COMMUNITIES

21 April 2005

TABLE OF CONTENTS

I. INTRODUCTION

Mr. Chairman, Members of the Panel, good afternoon, and thank you for providing the European Communities (EC) with an opportunity to present its views before you today.

1. The EC intervenes in this proceeding because of its systemic interest in the correct interpretation of the *SCM Agreement*, the GATT 1994 and the DSU. This dispute raises two key issues:

- What is a "measure taken to comply" within the meaning of Article 21.5 of the DSU?
- What are the substantive and procedural requirements for ensuring a proper analysis of pass-through?

II. MEASURE TAKEN TO COMPLY

2. The US continues to argue in its rebuttal submission that the administrative review is not a measure taken to comply.[1] Indeed, the US does nothing to defend the administrative review, but only focuses on the determination under Section 129. The EC regrets that it has not received Canada's rebuttal submission on the due date (although this is a right of third parties under Article 10 of the DSU).[2] The EC obtained Canada's rebuttal submission only this Tuesday after close of business, and had, therefore, only one working day to consider it.

3. From a first reading of Canada's submission, the EC can confirm that overall, it fully supports Canada's request to dismiss the US objection. Yet, the EC notes that there are some differences in the legal concepts on how to determine the scope of a DSU Article 21.5 proceeding.

4. The EC refers to all its arguments made in its third party submission, which it will not repeat today. As detailed therein, the broad mandate of DSU Article 21.5 panels stems directly from the term

[1] US rebuttal submission, paras. 2 and 46.
[2] Appellate Body, *US – FSC 21.5*, para. 251.

"existence" of a measure taken to comply read in the light of the broader purpose of DSU Article 21.5 to secure a prompt solution of a dispute between WTO Members.[3] Canada also explicitly agreed with the EC's basic proposition that the jurisdiction of DSU Article 21.5 Panels must, therefore, be determined in a way that prevents implementation measures from becoming "moving targets".

5. There are different legal concepts on how to do this. Canada and China put much emphasis on the fact that the administrative review while not being the "measure taken to comply" undid the Section 129 determination and, therefore, falls (as a successor measure) under the Panel's purview.[4] While the EC agrees with this characterisation of the relationship between the administrative review and the Section 129 determination[5], it considers that this general procedural criterion (Panel's terms of reference also cover successor acts) is not exclusively determinative for the jurisdiction of this DSU 21.5 Panel.

6. Given the major systemic importance of this issue, in particular for the EC, the EC respectfully requests the Panel to give the third parties further opportunity to comment in detail on Canada's arguments on how to define the scope of an Article 21.5 proceeding through written questions.

7. Let me close today's observations on this point by noting that, ironically, the US, through its preliminary objection, brings itself into a catch-22 situation. If it rejects the consideration by the Panel of the administrative review as compliance measure, no measure taken to comply existed (because the Section 129 determination had expired before the establishment of the 21.5 Panel). The Panel's report could therefore be quite short.

III. PASS-THROUGH

8. Turning now to the key substantive issue in this dispute: pass-through. The US and Canada disagree whether the US investigating authorities have done enough in terms of procedure and substance to demonstrate that subsidies received by certain upstream producers were passed-through to the down-stream producer of lumber products.

9. The need to ensure a pass-through analysis is not written explicitly into the *SCM Agreement* but stems directly from the obligation of a WTO Member imposing a countervailing duty to comply with Article VI:3 of the GATT 1994, and Article 10 of the *SCM Agreement* which require that investigating authorities:

> before imposing countervailing duties, must ascertain the precise amount of a subsidy attributed to the imported products under investigation.[6]

10. There are different situations in which the need for a pass-through analysis may arise, e.g., whether a subsidy was extinguished following a transfer of ownership. This Panel is tasked to assess whether the US investigating authorities established that subsidies to input producers benefited the downstream producers of the processed product subject to the investigation.[7] The key question is whether the US investigating authorities established that benefits received by the input producers

[3] EC Third Party Submission, paras. 10-18.
[4] Canada's rebuttal submission, para. 4, China's Third Party submission, para 12.
[5] EC Third Party Submission, paras. 2.and 25.
[6] Appellate Body Report, US – Countervailing Measures on Certain EC Products, para. 139.
[7] Appellate Body Report, US – Lumber, para. 146.

> have been passed through, at least in part, from producers of logs to producers of softwood lumber (and remanufactured lumber) which are the products subject to the investigation.[8]

11. The US and Canada disagree on whether the approach taken by the US investigating authorities suffices to establish the correct amount of subsidisation.

12. The EC as a third party is not in a position to comment in detail on this fact-intensive issue before the Panel. However, it wishes to offer a few general comments:

13. As regards the test for pass-through, the main parties appear to disagree on the meaning of "arm's length", in particular, whether it refers exclusively to a "related person" test. The EC notes that neither of these two notions are set out anywhere in the *SCM Agreement*. The obligation of an investigating authority is to establish the precise amount of subsidisation benefiting the product on which a CVD is imposed in accordance with Article VI:3 of the GATT 1994.

14. The Appellate Body referred for contextual guidance to Article 19.3 of the *SCM Agreement* whereby countervailing duties "shall be levied, in the appropriate amounts in each case, on a non-discriminatory basis on imports of such product from all sources found to be subsidised and causing injury". The Appellate Body recognised that this provision gives investigating authorities broad discretion to choose between different means of demonstrating and calculating the amount of the subsidisation, in particular whether they resort to sampling, aggregate or company specific investigations.[9]

15. The precise methodological approach to determine pass-through (or better: the amount of benefit received by the producer of the target product) inevitably varies from case-to case. The pass-through is likely to be somewhere between 0 and 100% depending, amongst other things, on the relationship between the input supplier and the processor as well as the economic context. Where the producers of the input and the processed product form part of the same *economic entity*, it may be presumed that 100% of the subsidy passed through.[10] By contrast, where the input product was sold on a functioning market at arm's length and for fair market value, there is a presumption of 0% pass-through.[11]

16. The existence and amount of pass-through must be established on a case-by-case basis. While a number of different factors may be relevant, the EC considers that the price charged by the input supplier to the producers of the product (in comparison to some relevant benchmark) plays a key role in measuring to which extent (if at all) the subsidy benefited the producer of the processed product.

17. The discretion of investigating authorities on how to establish pass-through is (as always) limited by the general obligation of investigating authorities to carry out an objective and unbiased examination, and the need to ensure that the countervailing duties are imposed in "appropriate" amounts "in each case" and on a "non-discriminatory basis" from "all sources found to be subsidised".

18. Procedurally, the investigating authority must do its best to facilitate the pass-through examination, e.g., by preparing a questionnaire and offering a company-specific approach unless the number of respondents is too high to allow a meaningful individual examination to take place. In such cases sampling or similar techniques may be required.

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[8] Ibid., para. 147.
[9] Appellate Body Report, US – Lumber, paras. 152-153.
[10] Ibid. para. 142.
[11] Appellate Body Report, US – CVD on Certain EC Products, WT/DS212, para. 126.

19. The investigating authority must then provide an adequate and reasoned explanation why, on the basis of the information received, the amount of pass-through calculated in the individual case is appropriate and that its assessment of the facts on the record is objective and unbiased.

IV. CONCLUSION

20. Mr. Chairman, Members of the Panel, this concludes our oral statement. I thank you for your attention and stand ready to respond to any questions you may have.

ANNEX D

Request for Establishment of a Panel

ANNEX D-1

REQUEST FOR ESTABLISHMENT OF A PANEL

WORLD TRADE ORGANIZATION

WT/DS257/15
4 January 2005

(05-0008)

Original: English

UNITED STATES – FINAL COUNTERVAILING DUTY DETERMINATION WITH RESPECT TO CERTAIN SOFTWOOD LUMBER FROM CANADA

Recourse to Article 21.5 of the DSU by Canada

Request for the Establishment of a Panel

The following communication, dated 30 December 2004, from the delegation of Canada to the Chairperson of the Dispute Settlement Body, is circulated pursuant to Article 21.5 of the DSU.

On 17 February 2004, the Dispute Settlement Body (DSB) adopted the Panel and Appellate Body reports in *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*.[1] The Panel and Appellate Body found that the US Department of Commerce (Commerce) was required to conduct a "pass-through" analysis in respect of arm's length sales of logs by tenured harvesters/sawmills[2] and independent harvesters to unrelated sawmills pursuant to the *General Agreement on Tariffs and Trade, 1994* (*GATT 1994*) and the *Agreement on Subsidies and Countervailing Measures* (*SCM Agreement*).

On 28 April 2004, Canada and the United States reached an agreement on a "reasonable period of time" pursuant to Article 21.3(b) of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (*DSU*).[3] The United States confirmed in this agreement that it would complete implementation no later than 17 December 2004.

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[1] Dispute Settlement Body, *Minutes of Meeting (17 February and 19 March, 2004)*, WT/DSB/M/165, 30 March 2004, at para. 49. Also See *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, Report of the Appellate Body, WT/DS257/AB/R, adopted 17 February 2004 ["Appellate Body Report"]; and *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, Report of the Panel, WT/DS257/R, adopted 17 February 2004.

[2] The Appellate Body used the term "tenured harvester/sawmill" to refer to an enterprise holding a stumpage contract that fells trees and produces logs, and also processes logs into softwood lumber. See Appellate Body Report, at fn. 150.

[3] *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada, Agreement under Article 21.3(b) of the DSU*, WT/DS257/13, 30 April 2004.

Shortly after adoption of the Panel and Appellate Body reports, the United States commenced implementation proceedings pursuant to section 129(b) of the *Uruguay Round Agreements Act* (*URAA*).[4] On 6 December 2004, Commerce released a countervailing duty determination pursuant to section 129 that announced results of its purported "pass-through" analysis. On 10 December 2004, in accordance with an instruction of that date from the US Trade Representative to implement the determination, Commerce issued a notice of implementation of its section 129 determination, in which it announced that the countervailing duty cash deposit rate would be reduced, effective 10 December 2004, by 0.17 (*i.e.*, from 18.79 per cent to 18.62 per cent).[5] On 20 December 2004, with the publication of the final results of the first administrative review of the countervailing duty order, Commerce established a definitive countervailing duty rate for the period of review and replaced the amended section 129 countervailing duty cash deposit rate with a new cash deposit rate without any "pass-through" analysis.[6] At the DSB meeting of 17 December 2004, the United States informed the DSB that it had complied with its rulings and recommendations.

Canada considers that the United States has failed to comply with the DSB's recommendations and rulings by incorrectly:

– limiting the category of transactions reviewed in the "pass-through" analysis to sales of logs by independent harvesters to unrelated sawmills, excluding transactions between harvesters/sawmills and unrelated sawmills, contrary to the DSB's recommendations and rulings;

– presuming, without an appropriate "pass-through" analysis, that certain transactions between independent harvesters and unrelated sawmills were not at arm's-length and that a "pass-through" of the alleged benefit occurred;

– applying the results of the "pass-through" analysis to a countervailing duty cash deposit rate invalidated as a result of judicial review proceedings conducted in accordance with US law, and failing to apply the results to a valid rate;[7] and

- failing to conduct a "pass-through" analysis in the final results of the first administrative review.[8]

Canada considers that the following measures allegedly taken by the United States to comply with the DSB's recommendations and rulings were inconsistent with US obligations under Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the *GATT 1994*:

– *Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products from*

[4] 19 U.S.C. § 3538(b).

[5] *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*, 6 December 2004; *Notice of Implementation Under Section 129 of the Uruguay Round Agreements Act; Countervailing Measures Concerning Certain Softwood Lumber Products From Canada*, 69 Fed. Reg. 75,305 (Dep't Commerce 16 December 2004).

[6] *Notice of Final Results of Countervailing Duty Administrative Review and Rescission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*, 69 Fed. Reg. 75,917 (Dep't Commerce 20 December 2004); and *Issues and Decision Memorandum*: *Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*, December 13, 2004.

[7] *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*, 6 December 2004, Comment 6, at 11.

[8] See e.g., *Issues and Decision Memorandum*: *Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*, 13 December 2004, at 43-48.

Canada,[9] and *Section 129 Determination: Final Countervailing Duty Determination, Certain Softwood Lumber from Canada*;[10]

– *Notice of Amended Final Affirmative Countervailing Duty Determination and Notice of Countervailing Duty Order: Certain Softwood Lumber Products from Canada*;[11] and

– *Notice of Final Results of Countervailing Duty Administrative Review and Rescission of Certain Company-Specific Reviews: Certain Softwood Lumber Products from Canada*,[12] and *Issues and Decision Memorandum*: *Final Results of Administrative Review: Certain Softwood Lumber Products from Canada*.[13]

Accordingly, as there is a disagreement as to the existence or consistency with a covered agreement of the measures taken to comply with the rulings and recommendations of the DSB, Canada seeks recourse to Article 21.5 of the DSU in this matter. Accordingly, Canada requests that a special meeting of the DSB be held on 14 January 2005 to consider the following agenda item:

United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada

Recourse by Canada to Article 21.5 of the Understanding on Rules and Procedures Governing the Settlement of Disputes.

Canada requests that the DSB refer the matter to the original panel, if possible, pursuant to Article 21.5 of the DSU.

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[9] 69 Fed. Reg. 75,305 (Dep't Commerce December 16, 2004)
[10] 6 December 2004.
[11] 67 Fed. Reg. 36,070 (Dep't Commerce 22 May 2002).
[12] 69 Fed. Reg. 75,917 (Dep't Commerce 20 December 2004).
[13] 13 December 2004.