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**THE NAFTA AND THE SOFTWOOD LUMBER DISPUTE:
WHAT KIND OF CANADA-US PARTNERSHIP?**

Gilbert Gagné

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Université du Québec à Montréal
C.P. 8888, succ. Centre-ville,
Montréal, H3C 3P8

GROUPE DE RECHERCHE SUR L'INTEGRATION CONTINENTALE

<http://www.unites.uqam.ca/gric>

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The notion of partnership has imposed itself within the past few years in international relations and international political economy. Although this is a rather ambiguous concept that may apply to a wide variety of relationships between different actors, it is often used to refer to existing relations between the three countries parties to the North American Free Trade Agreement (NAFTA). However, this has not entailed that relations between NAFTA partners have been devoid of conflicts or tensions. Among the conflicts that have characterized trade exchanges between Canada and the United States, the dispute over the Canadian exports of softwood lumber to the United States has proved the most important in terms of trade volumes, complexity, procedures, politicization, and duration. Superlatives abound when referring to the Softwood Lumber dispute, 'the largest trading dispute in the largest trading relationship in the world.' Now that in 2002 the Canadian-US Softwood Lumber dispute has never attracted so much attention, I wish to provide a concise summary of the essential of this long-running dispute, while drawing key conclusions on the basis and conditions for the Canadian-US partnership.

The Softwood Lumber dispute started in 1983 when US authorities first considered whether Canadian lumber exports were subsidized. The main issue at stake has been whether fees charged by provincial authorities to lumber firms to harvest trees on public land (stumpage rights) are artificially low and constitute countervailable subsidies. Canada has insisted that this is a matter of public policy that is in no way related to trade and subsidization. The conflict really began when US authorities concluded in 1986 that stumpage rights were 'specific' and insufficient, and, as a result, could be subject to countervailing duties (CVDs). For the Americans, it is essential to protect a major industry that is under direct competitive threat from unfairly subsidized imports. For the Canadians, the United States is unilaterally and arbitrarily deciding how provincial governments should tax and manage their resource industries.¹ The Softwood Lumber dispute has

¹ Subsidization generally refers to any government measure (e.g., grants, loans, tax concessions) that benefits firms. CVDs are based on an evaluation of the subsidy and aim to offset its effect. In addition to CVDs, the US trade remedy legislation includes anti-dumping (AD) measures, safeguard measures (Section 201), and measures to deal with 'unfair trade' under Section 301. Only recently, i.e., from 2001, have AD measures been used in the Softwood Lumber dispute. Dumping generally refers to a product imported at less than its normal value, notably if its price is lower than the one in the exporting country or when destined for a third country, or less than its cost of production. Despite successive multilateral and US provisions aimed at clarifying the notions of dumping and subsidy as well as the conditions for the imposition of trade remedies, we will see that these remain rather elusive and could lead to abuse. An alternative to the application of trade remedies is for the exporting firm(s) to raise prices (Price undertakings), or, in CVD cases, for the exporting country to eliminate or reduce the subsidy, or to take other measures, such as an export tax. We will see that this

gone through different periods, some highly conflictual, reaching peaks at times, followed by periods of relative calm after an ad hoc and temporary arrangement had been devised to prevent US retaliation. After 20 years, the dispute still goes on as no 'permanent' settlement acceptable to both parties appears to be in sight.

The main emphasis of this paper is not on the economic and legal aspects of the Softwood Lumber dispute, but on the political game surrounding the conflict.² Canada is highly dependent on the American market, and softwood lumber is one of the country's main exports. This is mainly what prompted Canada to negotiate a free trade agreement with the United States in order to secure provisions against retaliatory measures. These are contained in the 1988 Canada-United States Free Trade Agreement (CUSFTA) and now in the 1992 NAFTA. These rules, specified in Chapter 19 of the CUSFTA and NAFTA, have consisted mostly of binding reviews by binational panels of state final anti-dumping (AD) and CVD determinations, instead of domestic judicial review. Should such determinations be found not in accordance with national laws, state authorities must terminate the AD or CVD order and reimburse collected duties.³

solution has been resorted to in the Softwood Lumber dispute. As for Section 301, the most potent of US unfair trade law, it has also been used in the Softwood Lumber dispute. In all cases, imports are subject to remedies if it is found that the goods are tainted by unfairness and/or injury calling for either exclusion orders or offsetting penalties.

For a thorough analysis of US trade policy experience, see I.M. Destler, *American Trade Politics*, 3rd edn (Washington: Institute for International Economics, 1995); Anne O. Krueger, *American Trade Policy: A Tragedy in the Making* (Washington: The AEI Press, 1995). For a good summary of US trade remedy legislation and practice, as well as of the history and significance of US actions against Canadian exports, see Canada, Department of Foreign Affairs and International Trade, U.S. Trade Relations Division (UET), *U.S. Trade Remedy Law. A Ten Year Experience* (Ottawa, March 1993).

² For more thorough analyses of the Softwood Lumber dispute, particularly of its economic and legal aspects, see: Charles F. Doran, 'Trade dispute resolution 'on trial': softwood lumber,' *International Journal* 51 (autumn 1996), 710-33; T.M. Apsey and J.C. Thomas, *The Lessons of the Softwood Lumber Dispute: Politics, Protectionism, and the Panel Process*, Mimeo, April 1997; Benjamin Cashore, *Flights of the Phoenix: Explaining the Durability of the Canada-US Softwood Lumber Dispute*, *Canadian-American Public Policy* 32 (Orono: University of Maine, December 1997); Gilbert Gagné, 'The Canada-US softwood lumber dispute - an assessment after 15 years,' *Journal of World Trade* 33 (february 1999), 67-86.

³ Canada, External Affairs, *The Canada-U.S. Free Trade Agreement* (Ottawa, 1987); Canada, *North American Free Trade Agreement* (Minister of Supply and Services, 1992). The CUSFTA was agreed in October 1987 and came into force in January 1989. The NAFTA was concluded in August 1992 and became effective in January 1994. Signatories to the NAFTA are Canada, Mexico, and the United States. Unless specifically provided, CUSFTA provisions have been superseded by the NAFTA's.

Binational review panels are composed of five neutral experts. Both parties to a dispute appoint two members in consultation with the other and agree on the fifth member. In

Yet, the United States has proved willing to disregard internationally agreed rules when they did not coincide with American interests, and rather rely on whatever weight or leverage it has in its relations with Canada. In this respect, we will argue that the Softwood Lumber dispute represents a prominent and revealing case where power politics has prevailed over international trade rules. Major US economic and political interests have led to a disregard for CUSFTA/NAFTA provisions and left Canada negotiate whatever settlement may prove acceptable to the Americans. Complementing the multilateral trading regime, the CUSFTA and later the NAFTA were expected to be the cornerstone of Canadian-US economic integration. For Canada, this was to entail a partnership on a more secure and equal basis. In this respect, the Softwood Lumber dispute raises key questions concerning the effective basis of the Canada-US partnership.

As the late Susan Strange emphasized, conventional texts on international politics, when dealing with trade, often tend to start with the relevant international organizations. For Strange, this gives the false impression that it is the trade 'regime' - the rules and arrangements agreed between governments - that is a prime determinant of what actually happens. Instead, she claimed, 'rulebooks' are a rather peripheral influence, power and interests being almost always the prevailing factors,⁴ as has indeed proved to be the case with the Softwood Lumber dispute. Unlike national laws, international regimes do not set binding or enforceable legal liabilities in any strict or reliable sense. Rules of international regimes are also frequently bent or broken to meet the exigencies of the moment. However, rules may still make a difference, even if minimal in the Softwood Lumber case, as the United States may not like to be seen to contravene the provisions and principles of the international organizations and regimes to which it belongs. In this regard, laws and norms may exercise a compliance pull of their own, partly independent of US power and interests.

In reality, there is a constant and unstable balance between raw political behaviour and law-governed behaviour, the former being more likely in a regime such as the CUSFTA/NAFTA with minimal institutional arrangements. Hence, contrary to 'typical' cases of power politics, where states simply act as they please on the basis of their interests, in the Softwood Lumber conflict, while the US interprets obligations to its own

practice, the composition of panels has witnessed a rotation between a majority of US and Canadian panellists. For more on the CUSFTA and NAFTA provisions relating to trade remedies and dispute resolution, see William J. Davey, *Pine & Swine. Canada-United States trade dispute settlement: The FTA experience and NAFTA prospects* (Ottawa: Centre for Trade Policy and Law, 1996); Gilbert Gagné, 'North American free trade, Canada, and US trade remedies: an assessment after ten years,' *The World Economy* 23 (january 2000), 77-91.

⁴ Susan Strange, *States and Markets* (New York: Basil Blackwell, 1988), 161-2.

advantage, it is constrained by the need to justify its actions and practices in legal terms. Legal concepts and processes are actually used to achieve power ends. What is interesting, with the Softwood Lumber dispute, is that all actions are construed so as to give the impression of an 'apolitical' legal process in accordance with US and international trade provisions. Hence, although power and interests remain primary determinants of state conduct, as realists argue, states can less act as they please, being to varying degrees constrained by international rules and principles.⁵

The exchange of goods and services between Canada and the United States represents the most important trading relationship between two sovereign states. Each country is the other's main trading partner. The value of Canada-US trade amounted to more than C\$310 billion in 1993, and now more than C\$ 1 billion of merchandise cross the border every day.⁶ When we consider statistical figures on the magnitude of CVDs in Canada-US trade prior to the CUSFTA, the volume of bilateral exchanges subject to American CVD orders was about C\$ 200 million in 1986 if we exclude the Softwood Lumber case. In contrast, the Softwood Lumber dispute involved about C\$ 3 billion of Canadian exports in 1986, and that alone may explain why the Softwood Lumber case has attracted so much attention in Canada. When policy analyst Daniel Schwanen, then at the C.D. Howe Institute, conducted a detailed quantitative study of bilateral trade disputes, he found that the value of lumber trade had to be excluded 'because it would dwarf all the others.'⁷

Softwood lumber has constituted the second most important Canadian export sector after automotive products and one of Canada's largest industries. British Columbia and Quebec account respectively for about 60 and 20 per cent of Canadian lumber exports. In 1999, Canadian exports of softwood lumber to the United States amounted to C\$ 10.7 billion, accounting for 70 per cent of Canada's lumber production.⁸ Trade disputes in agricultural and commodity products, as is the case with softwood lumber, often take a further political dimension as they affect large numbers of citizens, often concentrated within regions, which make their votes count even more. In Canada, it has been estimated that more than 300,000 workers have been directly or indirectly affected by the conflict,

⁵ See Andrew Hurrell, 'International society and the study of regimes: a reflective approach,' in Volker Rittberger, ed, *Regime Theory and International Relations* (Oxford: Clarendon Press, 1993), 49-72; Marc A. Levy, Oran R. Young, and Michael Zürn, 'The study of international regimes,' *European Journal of International Relations* 1 (1995), 267-330.

⁶ Statistics Canada.

⁷ Daniel Schwanen, *Securing Market Access: Canada's trade agenda for the 1990s*, C.D. Howe Institute Commentary No. 32 (Toronto: C.D. Howe Institute, July 1991).

⁸ Statistics Canada.

and 350 communities have been dependent on the forest sector as their primary source of employment.⁹

Usually, four main phases are identified in the evolution of the Softwood Lumber dispute, referred to as Softwood Lumber I, II, III, and IV. I will observe these distinctions, although there is not much to say about Softwood Lumber I, which will be treated with Softwood Lumber II. Softwood Lumber III is to be analyzed with a specific section on the Softwood Lumber Agreement in place from 1996 to 2001. Softwood Lumber IV will finally be discussed before the concluding remarks.

Softwood Lumber I and II

The Canada-US dispute over softwood lumber raises crucial questions regarding how to define subsidies, and, more generally, involves serious policy issues of an economic, political, and legal nature.¹⁰ Canadian exports of softwood lumber to the United States were first subject to a CVD investigation by American authorities in 1982-83 during what is now known as Softwood Lumber I. At that time, the issue of US CVDs on Canadian softwood lumber exports appeared to have been resolved for good. The American authorities had found that Canada's policies regarding the pricing and allocation of timber harvest did not constitute a countervailable subsidy to the softwood lumber industry. Softwood timber from public land was found to be freely available on similar terms regardless of the industry or recipient and not provided at preferential rates to softwood lumber producers.¹¹

In May 1986, the same US interests grouped within the Coalition for Fair Lumber Imports (the Coalition) filed a new petition alleging that Canadian timber pricing and allocation policies conferred a countervailable subsidy and requested that a 27 per cent duty be imposed on Canada's softwood lumber imports. The evidence provided by the Coalition differed little in substance from the one during the 1982-83 phase

⁹ Statistics Canada; Government of Canada, *News Release No. 232*, 17 December 1993.

¹⁰ For a thorough discussion of the economic, political, and legal aspects of Softwood Lumber I and II, see Michael B. Percy and Christian Yoder, *The Softwood Lumber Dispute & Canada-U.S. Trade in Natural Resources* (Halifax: Institute for Research on Public Policy, 1987).

¹¹ US Department of Commerce (DOC), International Trade Administration (ITA), 'Final negative countervailing duty determination: certain softwood lumber products from Canada,' *Federal Register*, vol. 48, no. 105, 31 May 1983.

of the dispute. Nor had either the law or the facts of the case changed in the meantime. On the other hand, the Canadian share of US domestic consumption of softwood lumber had risen from 28.5 per cent in 1983 to 31.6 per cent in 1985.¹²

Another change, a fundamental one, was in the interpretation of the US CVD law by the Department of Commerce (DOC), which led to Softwood Lumber II. In October 1986, the DOC reversed its precedent decision and, in a preliminary determination, found Canada's timber pricing and allocation policies to constitute a countervailable subsidy. The US authorities found that governmental discretion was exercised so as to give the lumber industry (with the pulp and paper industry, both viewed as a single industry, as opposed to the furniture industry) a disproportionate share of the stumpage rights, which were then found to be specifically bestowed and, hence, countervailable. The DOC also found that stumpage programs were not based on commercial considerations, in that Canadian provincial governments were assuming a portion of the production cost of softwood products, and therefore such programs provided goods at preferential rates.¹³ A provisional duty of 15 per cent was set, i.e., half-way between the Coalition's alleged subsidy and the Canadian argument that there was no subsidy, which of course was less than coincidental. The US DOC's preliminary determination in October 1986 in Softwood Lumber II illustrated the extent to which legal and economic concepts can be stretched to achieve a desired political outcome.¹⁴

Expecting that the final determination was to uphold the preliminary finding and perhaps impose a higher duty, Canadian authorities then reluctantly agreed in late December 1986 to a 15 per cent export tax on softwood lumber destined for the United States. The settlement, under the form of a Memorandum of Understanding (MOU) between the Canadian and American governments, provided for the replacement of the export tax within five years by increased stumpage or other charges, at Canada's option, after consulting with the United States. The MOU provided as well for the monitoring of provincial and federal data regarding softwood and total harvest levels, federal and provincial revenues from timber production, export volumes to the US, and revenues collected under the export tax. Consultations between the Canadian and US governments, between Canada's federal and provincial authorities, and, in both countries, government-industry consultations were also a central element

¹² Percy and Yoder, *Softwood Lumber Dispute*, xxv-i.

¹³ US DOC, ITA, 'Preliminary affirmative countervailing duty determination: certain softwood lumber products from Canada,' *Federal Register*, vol. 51, no. 204, 22 October 1986. See Percy and Yoder, *Softwood Lumber Dispute*, xxx, 99-101.

¹⁴ Percy and Yoder, *Softwood Lumber Dispute*, xxix-xxx.

of what was a relatively innovative and ad hoc trade management device.¹⁵

For Canada, an export tax involved that the money paid by lumber producers remained in Canada instead of going to the US Treasury, as would have been the case with CVDs. The level of the tax was set to match the subsidy intensity calculated by the DOC in its preliminary determination. In return, CVD proceedings were terminated and the US domestic industry, namely the Coalition, made a commitment to the American government not to pursue trade remedy cases against softwood lumber imports from Canada.¹⁶ Concurrently, Canada had brought the matter before the Committee on Subsidies and Countervailing Measures within the General Agreement on Tariffs and Trade (GATT), but withdrew its complaint following the conclusion of the MOU.¹⁷

¹⁵ *Canada-United States Softwood Lumber Memorandum of Understanding*, 30 December 1986. For considerations on the MOU, see Percy and Yoder, *Softwood Lumber Dispute*, 101-3, 115-29.

¹⁶ *Federal Register*, vol. 52, no. 315.

¹⁷ General Agreement on Tariffs and Trade (GATT), *Basic Instruments and Selected Documents*, 34th Supplement (Geneva, 1987), 194-7.

Softwood Lumber III

The Softwood Lumber dispute entered its third phase in October 1991 when Canada terminated the MOU, which prompted US authorities to impose immediate retaliatory duties. This new phase in the dispute was to take place on the basis of the CUSFTA dispute settlement provisions in force for nearly three years.

The 1986 MOU, that had been grandfathered in the CUSFTA, provided for the elimination or reduction of the export tax on softwood lumber as a result of changes in provincial forest-management regimes, particularly increased stumpage rights, and other forest-management charges. Indeed, after successive amendments to the MOU, Atlantic Canada was exempted from the export tax, the same tax was removed for lumber exports from British Columbia, and it had gradually been reduced for Quebec's lumber exports to a rate of 3.1 per cent. On 3 September 1991, Canada informed the US government of its intention to terminate the MOU with effect from 4 October. Before taking this action, Canada used the US government's own Timber Sales Program Information Reporting System (TSPIRS) to compare government forestry costs and revenues in the four major timber-producing provinces. The analysis revealed that each province obtained revenues far in excess of its forestry costs. The Canadian government then concluded that circumstances had materially changed from 1986, that the US authorities would conclude that there was no longer any subsidy on Canadian softwood lumber production, and that the MOU no longer served any purpose.¹⁸

The amendments to the MOU following changes in Canadian provincial policies were the results of consultations with the United States. However, the decision to terminate the MOU was a unilateral move on the part of Canada as the United States responded by self-initiating a CVD investigation on 31 October 1991, its third CVD investigation on Canadian softwood lumber imports within a decade. The United States also imposed an interim bonding requirement on Canada's lumber imports under Section 301 of the US 1974 Trade Act. The Atlantic provinces were excluded from the interim bond and the CVD investigation. Such an episode was revealing of the politicization of US trade cases, and particularly a major one such as Softwood Lumber. After the termination by Canada of the MOU, a letter signed by 66 senators requested the President to take 'swift and strong action' on softwood lumber. This was

¹⁸ Canada, *News Release No. 232*.

soon accompanied by a rare self-initiation of a trade case by the DOC.¹⁹ On the Canadian side, two main factors seem to have played a key role. Provincial authorities did not appreciate having to discuss their policies with US authorities found to be intrusive and the government and forest company officials of British Columbia pressed the federal government to repeal the MOU.²⁰ Also, the economic recession of the early 1990s and the closure of many manufacturing plants had shed doubts in the public's mind about the virtue of free trade. By putting an end to the unpopular MOU, the federal government, and particularly the then minister of Finance Michael Wilson, wanted to boost the popularity of the CUSFTA and to show that the agreement worked for Canadians' interests.²¹

Canada challenged the imposition of the interim bonding requirement and the initiation of a CVD investigation before the GATT. A GATT Subsidies Code panel was established in December 1991 to determine whether US actions were consistent with international trade rules. The GATT panel concluded that the United States had violated its obligations when it imposed the Section 301 bonding requirement, but that it possessed sufficient evidence to launch a CVD investigation. On this last conclusion, Canada claimed that stumpage programs should have trade-distorting effects to be considered as subsidies, but the GATT Subsidies Code panel viewed the issue as an empirical one, requiring fuller investigation. The panel report was adopted by the GATT Subsidies Committee on 27 October 1993.²² However, by that time, Canada had resorted to the CUSFTA dispute mechanism to address the 'substantive' issues in the Softwood Lumber conflict.

With respect to the US CVD investigation, a preliminary determination of injury was made by the International Trade Commission (ITC) in December 1991.²³ For its part, the DOC initially limited its investigation to stumpage programs to later include, at the Coalition's request, British Columbia's log export control measures. In March 1992, the DOC came up with a preliminary determination that provincial stumpage programs and log export restrictions conferred subsidies at a national rate of 14.48 per cent, stumpage accounting for 6.25 per cent and log export measures for 8.23 per cent. In its final determination in May 1992, the DOC confirmed

¹⁹ Homer E. Moyer, Jr., 'How will the Uruguay Round change the practice of trade law in the United States? U.S. institutions, not the WTO, may hold the answer,' *Journal of World Trade* 30 (June 1996), 79-80.

²⁰ Apsey and Thomas, *Lessons of the Softwood Lumber Dispute*, 35-7; Cashore, *Flights of the Phoenix*, 18.

²¹ Confidential interview.

²² GATT, *Basic Instruments and Selected Documents*, 40th Supplement (Geneva, 1995), 358.

²³ US International Trade Commission (ITC), *Softwood Lumber from Canada*, Pub. no. 2468, December 1991.

its decision, although the country-wide subsidy rate was reduced to 6.51 per cent, with stumpage at 2.91 per cent and log export controls at 3.6 per cent.²⁴ Finally, in July, the ITC determined that subsidized imports of Canadian lumber materially injured US producers.²⁵

Canada referred both US final determinations to the CUSFTA binational panel review mechanism. The CUSFTA panel established to review the US subsidy determination (the subsidy panel) reported its findings on 6 May 1993, unanimously instructing the DOC to re-examine its determination on virtually all key issues in the case.²⁶ On 17 September 1993, the DOC reaffirmed its original finding, even concluding that the subsidy rate had increased from 6.51 per cent to a level of 11.54 per cent.²⁷ Then, on 17 December 1993, the subsidy panel ruled that, under US trade law, the DOC should not have found a countervailable subsidy on either stumpage programs or log export restrictions. However, on remand, the subsidy panel was not unanimous, the two US panelists dissenting on most issues.²⁸

On 26 July 1993, the injury panel remanded the ITC's determination for lack of sufficient evidence that the alleged subsidized imports of Canadian softwood lumber were causing injury to the US lumber industry.²⁹ In response to the panel remand, the ITC again found in October 1993 that the American lumber industry was injured by lumber imports from Canada.³⁰ In January 1994, the panel concluded that there

²⁴ US DOC, ITA, 'Preliminary affirmative countervailing duty determination: certain softwood lumber products from Canada,' *Federal Register*, March 1992; US DOC, ITA, *Certain Softwood Lumber Products from Canada*, May 1992.

²⁵ US ITC, *Softwood Lumber from Canada*, Pub. no. 2530, July 1992.

²⁶ CUSFTA, Article 1904 Binational Panel Review USA-92-1904-01, *Certain Softwood Lumber Products from Canada*, Decision of the panel, 6 May 1993.

²⁷ US DOC, ITA, *Certain Softwood Lumber Products from Canada Redetermination Pursuant to Binational Panel Remand*, 17 September 1993.

²⁸ CUSFTA, USA-92-1904-01, *Certain Softwood Lumber Products from Canada*, Decision of the panel on remand, 17 December 1993. For more on this, see George Hoberg and Paul Howe, 'Law, knowledge, and national interests in trade disputes: the case of softwood lumber,' *Journal of World Trade* 34 (march 2000), 109-30.

On the specificity test in US law, regulations, and practice, with numerous references to the Softwood Lumber case, and to other CUSFTA/NAFTA panel decisions, see John A. Ragosta and Howard M. Shanker, 'Specificity of subsidy benefits in U.S. Department of Commerce countervailing duty determinations,' *Law and Policy in International Business* 25 (1994), 639-83.

²⁹ CUSFTA, Binational Panel Review USA-92-1904-02, *Softwood Lumber from Canada*, Decision of the panel reviewing the final determination of the US International Trade Commission, 26 July 1993.

³⁰ US ITC, *Softwood Lumber from Canada*, First remand, Pub. no. 2689, October 1993.

was no basis for a material injury determination, although the panel provided the ITC with an opportunity to review one element of its decision.³¹ In its second determination on remand in March 1994, the ITC maintained its conclusion of material injury caused by Canadian lumber imports on the sole basis of the importance of these imports.³² In July 1994, the panel in its decision on a third remand again rejected the determination that there was injury to the US lumber industry.³³

The matter was still open when the injury panel review was terminated. Proceedings were initially stayed due to a constitutional challenge to the panel process from the Coalition before US courts, and later ended after Canada and the United States reached a settlement on lumber trade issues relating to this US CVD action. Let be mentioned that, unlike the subsidy panel, all the decisions from the injury panel were unanimous and there was a majority of US panelists.

In April 1994, the American government decided to resort to the extraordinary challenge procedure provided in the CUSFTA/NAFTA to have the decision of the subsidy panel revoked.³⁴ The appeal was rejected by the Extraordinary Challenge Committee (ECC) on the grounds that the US government's claims did not meet the conditions required to invoke the extraordinary challenge procedure. However, to add to an already conflictual situation, the three-member committee was not unanimous in its decision. While the two Canadian judges upheld the panel's decision, the US chair of the committee attacked the legitimacy of the CUSFTA/NAFTA binational review mechanism.³⁵ This led the US government and interests to denounce the binational subsidy panel and committee for failure to apply the appropriate standard of review and for

³¹ CUSFTA, USA-92-1904-02, *Softwood Lumber from Canada*, Decision of the panel on review of the remand determination of the US International Trade Commission, 28 January 1994.

³² US ITC, *Softwood Lumber from Canada*, Second remand, Pub. no. 2753, March 1994.

³³ CUSFTA, USA-92-1904-02, *Softwood Lumber from Canada*, Decision of the panel on review of the US International Trade Commission's second remand determination, 6 July 1994. For more on the legal issues over the US injury determinations and the panel remands, see Mary Y. Pierson, 'Recent developments in the U.S./Canada softwood lumber dispute,' *Law and Policy in International Business* 25 (1994), 1187-1203.

³⁴ Under the CUSFTA and the NAFTA, only in exceptional circumstances can a panel decision be challenged, namely, if a panellist is guilty of gross misconduct, bias or serious conflict of interest, or if the panel has seriously departed from a fundamental rule of procedure or manifestly exceeded its authority, *and* that one of these factors has significantly influenced the panel's decision and threatens the integrity of the binational review process. An Extraordinary Challenge Committee (ECC) composed of three judges is then established and renders its decision (CUSFTA/NAFTA, art 1904.13).

³⁵ CUSFTA, ECC USA-94-1904-01, *Certain Softwood Lumber Products from Canada*, Committee opinions of 3 August 1994.

voting along national lines.³⁶ More generally, this also resulted in fierce criticism of the panel review mechanism for being an unacceptable encroachment on US sovereignty and a threat for the integrity of its trade legislation.³⁷

Through the remands in the Softwood Lumber case, it was clear that the US agencies openly resisted complying with binding decisions from binational panels, or did so defiantly, disparaging panels' decisions. In addition, the resort by the United States to the extraordinary challenge procedure suggested that the US saw that procedure as an ordinary appeal channel.³⁸

The Softwood Lumber Agreement

After the United States 'lost' its legal case in Softwood Lumber III following the reject of its appeal by the ECC, the DOC reluctantly dropped its CVD order on Canada's softwood lumber. However, it threatened not to reimburse the duties collected since 1991. Among these were the duties perceived under the Section 301 interim bonding requirement, which a GATT panel found to contravene international trade rules. Yet, many saw this threat as a tactic to bring Canada to negotiate a settlement.

This episode in Softwood Lumber III took place at the time the US implementing legislation of the results of the Uruguay Round of multilateral trade negotiations, the Uruguay Round Agreements Act (URAA), was before Congress for ratification.³⁹ The American authorities seized this opportunity to modify the US legislation along positions which the US agencies advocated without success before binational panels during Softwood Lumber III. Despite Canadian objections, the US

³⁶ For a discussion of the extraordinary challenge procedure in the Softwood Lumber case, see William J. Davey, *Pine & Swine*, 232-44. Davey's book also includes an exhaustive treatment of the political and legal aspects of Softwood Lumber III.

³⁷ See, among others, Charles M. Gastle and Jean-G. Castel, 'Should the North American Free Trade Agreement dispute settlement mechanism in antidumping and countervailing duty cases be reformed in the light of softwood lumber III?,' *Law and Policy in International Business* 26 (spring 1995), 823-96. On the allegations of national bias and the CUSFTA/NAFTA panel mechanism, see Matthew Stevenson, 'Bias and the NAFTA dispute panels: controversies and counter-evidence,' *The American Review of Canadian Studies* 30 (spring 2000), 19-33.

³⁸ See Moyer, 'How will the Uruguay Round,' 67; Davey, *Pine & Swine*, 261-9.

³⁹ US, *Uruguay Round Agreements Act (URAA)*, 1994.

implementing provisions, notably through the way a subsidy is defined, the disregard for the effect of a subsidy, and the conditions for determining the specificity of a subsidy, sought to overturn the decisions of the lumber subsidy panel.⁴⁰ Indeed, the Clinton administration in its Statement of Administrative Action accompanying the URAA stressed that this was intended to correct the lumber panel's 'misinterpret(ation)' of US law.⁴¹ It must be pointed out that controversial legal matters are raised here, in fact subsequent NAFTA panels took issue with the conclusions of the lumber subsidy panel and its specificity analysis.⁴² Yet, it remains that such US provisions represent not only a unilateral interpretation but a disregard for multilateral and NAFTA provisions.

Once the political obstacle of the approval by Congress of the results of the Uruguay Round and the World Trade Organization (WTO) had successfully been lifted, the American authorities reimbursed the duties, which led to the refund of approximately C\$ 1 billion to the Canadian lumber industry. Then, it was announced in December 1994 that the Canadian and American governments agreed to establish a bilateral consultation process, known as the lumber dialogue.⁴³ The lumber dialogue took the form of government-to-government sessions that followed combined government-industry meetings.

The URAA and notably the provisions adopted to overcome the decisions of the subsidy panel in Softwood Lumber III may have led Canada to conclude that it was less than certain that a NAFTA panel could again find in favour of Canadian interests. Canada's primary objective through the lumber dialogue was to avoid further litigation, as all that was needed for another US investigation to take place was the submission of a new complaint. Indeed, the Coalition had made it clear that if the lumber dialogue did not lead to satisfactory results, it would file a CVD petition.

⁴⁰ Whereas the subsidy panel found that all factors in the DOC's regulations had to be considered to conclude to the specific (and hence countervailable) character of a subsidy measure, the URAA specifies that only one factor is dispositive. Also, whereas the subsidy panel found market distortion a condition for determining a countervailable subsidy, the URAA provides that the DOC is not required to consider the effects of a subsidy to find it countervailable.

See Moyer, 'How will the Uruguay Round,' 75-6. On the implications of the US interpretation and implementation of the Uruguay Round results, see Gary N. Horlick and Peggy A. Clarke, 'The 1994 WTO subsidies agreement,' *World Competition* 17 (June 1994), 41-54; Gilbert Gagné, *The WTO Subsidies Agreement: Implications for NAFTA*, Occasional Paper No. 45 (Ottawa: Centre for Trade Policy and Law, March 1998), 19-22.

⁴¹ *Uruguay Round Agreements Act, Statement of Administrative Action*, H.R. Doc. 316, 103d Cong., 2d Sess., 1994.

⁴² See Ragosta and Shanker, 'Specificity of subsidy benefits,' 654ff.

⁴³ *Inside U.S. Trade*, 16 December 1994, 1, 27-8.

By the end of 1995, British Columbia and Quebec, the two main lumber exporters, made offers to the American authorities. Whereas British Columbia proposed an export tax above a set quota, Quebec's offer corresponded to US demands for more market-oriented practices. Yet, the United States found Quebec's offer insufficient. Then, it became obvious that the United States was not really looking for changes in stumpage policies as for a direct reduction of exports. Indeed, the United States insisted that Quebec would either have to raise producers' costs enough to *guarantee a decrease* in exports to the United States, or else *reduce the quantity* of exports through a *direct* mechanism.⁴⁴

Finally, an agreement, known as the Softwood Lumber Agreement (SLA), was reached in May 1996,⁴⁵ whose main provision was an annual tariff-rate quota for softwood lumber exports to the United States from British Columbia, Quebec, Alberta, and Ontario. The SLA allowed 14.7 billion board feet (based on Canada's average exports over the period 1993-95) per year with no tax (tax-free quota). Above this ceiling, a US\$ 50 tax per thousand board feet applied on the next 650 million board feet, and beyond that a tax of US\$ 100 per thousand board feet. A license was required for all exports indicating, *inter alia*, the province of origin, and such licenses were allocated on a company-by-company basis. There was a trigger price at and above which additional free licenses (below quota) were to be allocated.

The Canadian government had prime responsibility to monitor the SLA and to provide all required data and information to the US side. A dispute settlement system was included whereby after an initial 35-day consultation period, all quota or tax issues could be settled by an auditor, while all other issues were to be referred to an arbitral panel. If it were established that Canada had materially breached the SLA, the United States could have taken unilateral action under Section 301 of its trade legislation.⁴⁶ The Canadian side also committed that neither the federal government nor the provinces were to directly or indirectly reduce the impact of the SLA by granting subsidies to the lumber industry or by modifying timber management or pricing systems in a way that would have reduced the cost of timber or its harvesting for the industry.⁴⁷

⁴⁴ *Inside U.S. Trade*, 22 December 1995, 1, 16-7; 2 February 1996, 1, 19-20; 23 February 1996, 3-4; 12 April 1996, 11-3.

⁴⁵ *Softwood Lumber Agreement between the Government of Canada and the Government of the United States of America* (Canada, Treaty series 1996/16). The SLA was formally signed in May 1996 with application retroactive to 1 April.

⁴⁶ *Inside U.S. Trade*, 14 June 1996, 7-8.

⁴⁷ For the details of the SLA, see *Inside U.S. Trade*, 5 April 1996, 3ff.

In simple terms, to buy five years of peace in trade terms, Canada agreed to limit the amount of wood it exported to the United States. In return for these commitments, the American government and the Coalition agreed not to pursue any new trade actions for five years. It was stipulated that the SLA could be renewed. Such an arrangement in favour of a 'managed market' contradicted the very idea of a free trade agreement. Moreover, by lifting the Softwood Lumber dispute out of the NAFTA provisions, it was a clear blow to the binational panel review mechanism. Yet, when comparing the terms of the 1986 MOU with the 1996 SLA, it appeared that Canada's bargaining position was strengthened as a result of its victories under the CUSFTA/NAFTA regime. Whereas the 1986 MOU entailed a tax on all exports, the 1996 SLA allowed a significant amount of lumber, in fact 90 per cent of Canada's 1995 records high share of softwood lumber exports to the US market, to be duty free.⁴⁸

By the end of 1997, issues arose in the implementation of the SLA when British Columbia proposed to lower stumpage fees after its timber industry was hit by the Asian economic crisis, and, for its part, the US industry sought the reclassification of certain wood products into a tariff category covered by the SLA. Both issues led to a renewed period of tension in the saga of the Softwood Lumber dispute.

The United States argued that British Columbia's plan to reduce stumpage fees violated the SLA by undercutting the effect of the export tax and reducing firms' costs. After British Columbia initially delayed the cut in stumpage fees to consult with the US, it announced that it was to cut stumpage fees by C\$ 600 million, or 16 per cent, over three years from 1 June 1998. Then the American government requested consultations with Canada and, in late July, formally requested arbitration under the SLA. By the end of 1998, the arbitral panel was formed. On 26 August 1999, the day before the panel report was to be announced, Canada and the United States reached a settlement. This first amendment to the SLA, pertaining only to British Columbia, stipulated that one-fourth of the province's quota shares subject to the US\$ 50 tax, i.e., 90 million board feet, were made subject to the US\$ 100 regime, limited then to 110 million board feet, while above this level a third export fee of US\$ 146.25 per thousand board feet applied.⁴⁹

The other litigious set of issues followed the decision by the US Customs Service in October 1997 to classify studs with pre-drilled holes as carpentry and joinery (category 4418) under the Harmonized Tariff System

⁴⁸ Gordon Ritchie, *Wrestling with the Elephant: The Inside Story of the Canada-U.S. Trade Wars* (Toronto: Macfarlane, Walter & Ross, 1997), 212.

⁴⁹ *Inside U.S. Trade*, 23 January 1998, 1, 21-3; 27 March 1998, 6; 29 May 1998, 1, 15-6; 26 June 1998, 3; 7 August 1999, 10-1; 27 August 1999, 1, 12-3; Canada, *News Release No. 191*, 30 August 1999.

and not as softwood lumber (category 4407). US lumber interests strongly objected to this decision and pressed for pre-drilled studs to be classified as lumber to make them subject to the restrictions of the SLA. For the Coalition, it was essential to plug a major loophole in the agreement. It claimed that following the US Customs' decision Canadian exports of 'drilled lumber' had risen significantly, resulting in a circumvention of the SLA. Political pressures brought the US Customs Service in April 1998 to revoke its October 1997 decision with effect from 1 July 1998. Canada stressed that this constituted a breach of the SLA by unilaterally placing pre-drilled studs within its scope.

In February 1999, the US Customs Service announced its intention to reclassify other Canadian products as softwood lumber under heading 4407, which was effective in June with regard to notched lumber and rougher headed lumber. Canada then sought arbitration over these US decisions. In May 2000, an arbitral panel was established. Concurrently, Canada referred the reclassification of these two products to the World Customs Organization (WCO), as it had done for pre-drilled studs. In all these cases, the WCO's instances gave reason to Canada. In October 2000, with respect to rougher headed lumber, it was announced that the annual SLA tax-free quota was expanded by 72.5 million board feet, reflecting Canadian historical shipments of rougher headed exports prior to the SLA. In return, Canada dropped the arbitration procedure over the reclassification of rougher headed lumber. In late March 2001, the arbitral panel ruled that the US violated the SLA by reclassifying drilled studs and notched lumber to make them subject to the terms of the SLA.⁵⁰

In 1999 began on both sides of the border the process of examining whether to renew or renegotiate the SLA, or allow it to expire on 31 March 2001. On the Canadian side, there was consensus that the SLA should not be renewed in its existing form, although provinces and their respective lumber industries have been split on the strategy to pursue vis-à-vis the United States. Reflecting traditional positions from the main Canadian parties in the Softwood Lumber dispute, most eastern firms from Quebec and Ontario, grouped within the Free Trade Lumber Council, have insisted on the end of the SLA and free trade in lumber, while most west coast firms, grouped within the British Columbia Lumber Trade Council, have sought a new deal to prevent further US legal attacks. Then, at a meeting of Canadian lumber interests in May 2000, a successor agreement to the SLA was ruled out, although discussions between government authorities and lumber interests from both sides of the border were encouraged.

⁵⁰ *Inside U.S. Trade*, 23 January 1998, 1, 21-3; 11 June 1999, 1-3; 13 October 2000, 8; *International Trade Reporter*, 22 June 2000, 980-1; 12 October 2000, 1565; 12 April 2001, 589; Canada, *News Release No. 40*, 30 March 2001.

In the US, consultations by the United States Trade Representative (USTR), as well as congressional lobbying and initiatives were under way while the administration indicated by 1999 that it did not seek the renewal of the SLA, but could conceive a new arrangement which would change Canadian forestry practices over time. The United States again told Canada to reform its forestry practices by adopting a market-based timber pricing system or it would face a new trade remedy action. A threat again reiterated by the Coalition, which fought for the renegotiation of the SLA and notably for a tighter definition of the covered products.

Both governments dragged their feet on the issue, apparently unwilling to continue regulating lumber trade. In February 2001, Canada proposed a panel of two eminent persons or special envoys, one appointed by each party, to develop non-binding recommendations on softwood lumber trade. The proposal remained in the air, floating for a few months. Shortly before the due date for the expiration of the SLA, the US warned Canada against a 'surge' of lumber shipments, and indicated as a solution an export tax, similar to the 1986 MOU. Almost sponsorless, the SLA finally expired on 31 March 2001.⁵¹

⁵¹ *Inside U.S. Trade*, 8 October 1999, 1, 17-8; 21 April 2000, 6-9; 2 June 2000, 17; 3 November 2000, 10-1; 2 March 2001, 1, 8-9, 21-4; *International Trade Reporter*, 20 April 2000, 642.

Softwood Lumber IV

As soon as the SLA expired, the Coalition filed a petition for a CVD and an AD investigation on Canada's lumber imports, as well as a 'critical circumstances' determination under which duties are imposed retroactively to the filing of a case. For the first time in the long-running Softwood Lumber dispute, an AD investigation was added to the anticipated CVD case, with a claim that Canadian lumber was sold in the US at less than fair market value. The Coalition targets provincial stumpage programs and log export restraints and alleges subsidies amounting to 40 per cent and dumping margins as high as 36 per cent.⁵² This has triggered the most acrimonious phase ever in this never-ending Softwood Lumber dispute. In fact, for the past 20 years, each successive conflictual phase has gained in acrimony. Throughout the US trade remedy process and investigation, Canada and the United States continued to look for a mutually acceptable solution to put an end to trade litigation. Concurrently, Canada has challenged US trade remedy laws and actions in both WTO and NAFTA instances.

The ITC provisionally determined in May 2001 that allegedly dumped and subsidized softwood lumber imports from Canada threatened to cause injury to US lumber producers.⁵³ In its preliminary CVD determination on 10 August 2001, the DOC found that Canada's softwood lumber exports were subsidized at a rate of 19.31 per cent. As in the case of a pre-determined outcome, the subsidy margin found by the DOC here again is half-way between the Coalition's allegations of a 40 per cent subsidy and the Canadian position of no subsidy. The DOC also concluded to 'critical circumstances' in that there was a 'massive surge' of Canadian softwood lumber imports in the first quarter after the expiration of the SLA. Although US regulations have historically considered a surge as an increase of imports beyond a 15 per cent threshold, the 'surge' was in the proportion of an 11.3 per cent increase when compared with the same quarter in 2000.⁵⁴

⁵² *Inside U.S. Trade*, 6 April 2001, 1, 17-9.

⁵³ US ITC, *Softwood Lumber from Canada*, Pub. no. 3426, May 2001; *Inside U.S. Trade*, 1 June 2001, 13.

⁵⁴ US DOC, ITA, 'Notice of preliminary affirmative countervailing duty determination, Preliminary affirmative critical circumstances determination, and Alignment of final countervailing duty determination with final antidumping duty determination: *certain softwood lumber products from Canada*,' 66 *Federal Register* 43186, 17 August 2001; Canada, *News Release No. 118*, 10 August 2001; *International Trade Reporter*, 16 August 2001, 1284-5; *Inside U.S. Trade*, 17 August 2001, 1, 12-3.

However, on 31 October 2001, when the DOC provisionally determined that Canada's softwood lumber exports were dumped in the US, it also affirmed that there was no evidence of surge. Six major companies were targeted, with dumping margins ranging from 5.94 to 19.24 per cent, while the average duty rate, i.e., for all other companies, was set at 12.58 per cent.⁵⁵ On 22 March 2002, the DOC announced both its final CVD and AD determinations, subsequently revised on 25 April. The subsidy margin remained almost the same at 18.79 per cent, while the dumping margins were reduced, ranging from 2.18 to 12.44 per cent, with an average margin of 8.43 per cent. The DOC's final ruling found no critical circumstances in either the subsidy or dumping case, which meant that no retroactive duties were applied. The four Atlantic provinces and 20 companies were excluded from the CVD action. Hence, the US final combined CVD and AD amount to a 27 per cent punitive duty on Canadian softwood lumber exports.⁵⁶

On 2 May 2002, the ITC's final determination, in a 4-0 vote, upheld its preliminary finding of a threat of injury to US producers resulting from subsidized and dumped softwood lumber imports from Canada. Under a decision of a 'threat of injury,' no provisional duties (prior to 16 May) were imposed, eliminating over US\$ 760 million in potential duties.⁵⁷

By September 2001 and until the completion of the US trade remedy investigations, bilateral government-to-government discussions deepened and centred less on process but on the root cause of the dispute, i.e., Canadian forestry practices, particularly stumpage fees, tenure policies, and laws mandating minimum cuts.⁵⁸ A Canadian-US 'working group'

⁵⁵ US DOC, ITA, 'Notice of preliminary determination of sales at less than fair value and postponement of final determination: *certain softwood lumber products from Canada*,' 66 *Federal Register* 56062, 6 November 2001; *International Trade Reporter*, 1 November 2001, 1749; *Inside U.S. Trade*, 2 November 2001, 4-5.

⁵⁶ US DOC, ITA, 'Notice of final affirmative countervailing duty determination and final negative critical circumstances determination: *certain softwood lumber products from Canada*,' 'Notice of final affirmative antidumping duty determination and final negative critical circumstances determination: *certain softwood lumber products from Canada*,' 67 *Federal Register* 15545, 2 April 2002; Canada, *News Release No. 28*, 22 March 2002; *Inside U.S. Trade*, 29 March 2002, 3-4.

⁵⁷ US ITC, *Softwood Lumber from Canada*, Pub. no. 3509, May 2002; Canada, *News Release No. 46*, 2 May 2002; *News Release No. 53*, 17 May 2002.

⁵⁸ Stumpage fees refer to the rights to Canadian companies to harvest timber on state-owned land. The US has argued that these are set by provincial governments at artificially low prices or below market value. Tenure policies cover the length of time Canadian companies are given exclusive cutting rights to an area. For example, in British Columbia, it is about 50 years. Mandatory minimum cut laws require producers to log and process a determined amount of timber and, as the US argues, regardless of market demand. For the US, all these practices result in unfair subsidies and/or dumping. For a discussion of the

ensued from these talks, and government-to-government meetings were often accompanied by industry and government-industry meetings. The US side suggested a 'bridging agreement' as a transitional step toward a long-term solution of the dispute. This was to be in the form of an export tax on Canadian lumber, to be collected by the Canadian government, and that was to be reduced as provinces made changes to their forest-management practices. In this respect, the US has long insisted on an auction-based system, as in the US, or something else that would bring timber prices more in line with the market. The issue of an enforcement mechanism was raised, to ensure that reforms led to true competitive conditions in the Canadian timber industry. Then, the US appointed former Montana governor Marc Racicot as special representative in bilateral lumber discussions.

Canadian-US talks stalled over the large gap between the percentage of timber provinces were willing to put up for auction, 13 per cent in the case of British Columbia compared with the current 6 per cent, and the percentage of 60-80 per cent demanded by the Coalition. Then, provincial authorities tabled further offers to the US. British Columbia offered to use the price from auction-bidding as a basis for calculating the administrative price for the remainder of provincial timber. For the US, this still fell short of a truly market-based system. Then, the USTR asked the Coalition to suggest a 'tipping point' of when enough provincial timber rights are competitively sold to lead to a fair administrative price. The Coalition had repeatedly emphasized that for a market-based regime more than 50 per cent of provincial timber had to be put for competitive bidding. Quebec also proposed that a limited amount of its timber be auctioned to set provincial timber prices. Ontario floated an idea that would use prices in neighboring US states as a basis for calculating the provincial price charged to lumber firms.⁵⁹

The Coalition in January 2002 stressed alternative combinations of potential forest reforms by Canadian provinces, notably that two-thirds of British Columbia's timber be auctioned, the Coalition's 'preferred solution.' The Coalition also called for reductions or elimination of long-term leases held by Canadian lumber firms allowing them to log timber (tenure policies), and demanded the lift of log export bans. In February 2002, the US government did not submit a counterproposal to Canada, but simply mentioned different proposals to package together various forest policy changes, possibly incorporating cross-referencing of softwood

multiple aspects of Canada's forestry practices, including US trade pressures, see Michael Howlett, ed, *Canadian Forest Policy: Adapting to Change* (Toronto: University of Toronto Press, 2001).

⁵⁹ *International Trade Reporter*, 13 September 2001, 1442-3; *Inside U.S. Trade*, 14 September 2001, 1, 22-3; 5 October 2001, 1, 23-4; 23 November 2001, 12-3; 14 December 2001, 1, 18-21; 4 January 2002, 1, 20.

lumber prices across the Canada-US border. The main US suggestion at that time was a possible agreement to suspend the DOC's final subsidy and dumping determinations through an export tax and a minimum price on softwood lumber shipments until such time as long-term systemic forest reforms were implemented.

During marathon negotiating sessions in March, three main dividing issues related to 1) the level of the export tax, the US suggesting 37 per cent and Canada 10 per cent or less; 2) the details of required provincial forest reforms (as outlined in the preceding paragraphs); and 3) the powers of a binational lumber council to oversee the implementation of the agreement, particularly the *binding* resolution of disputes in softwood lumber, which for Canada was essential to ensure secure access to the US market. The bilateral negotiations broke off in May. The American and Canadian partners apparently being unable to bridge their differences and the latter being unsatisfied by the US proposals, Canada then preferred to wait for the results of its challenges to US trade actions within both the WTO and the NAFTA.⁶⁰

If there were a distinctive feature to Softwood Lumber IV, it is certainly that there has been more emphasis from both sides of the border on a long-term, durable solution to the dispute. Yet, the recent and ongoing Canadian-US talks over softwood lumber trade bear much resemblance to those of the preceding phases of this long-lasting conflict. The same key elements and patterns that have characterized the dispute for now 20 years can still be observed. Although at the centre of the dispute, alleged timber subsidies continue to be the pretext for US lumber producers to defend what they consider a fair share of their domestic market, either through US trade remedies or bilateral trade-restrictive deals. This was clear when in 1991 log export controls were added to the CVD case and when in 2001 an AD investigation was conducted alongside the CVD action. It was also obvious during the SLA negotiations because if the United States really believed that Canadian lumber was subsidized, it would have refused to even discuss the possibility of such 'unfair' imports not being subject to remedy.

Recently, there have been cases of cross-border investments and mergers between timber companies, as in the case of the US-based Weyerhaeuser that bought Macmillan-Bloedel, the largest Canadian lumber firm. By creating joint interests, this may serve as a disincentive to US trade remedy actions and to restrict bilateral lumber trade. Indeed,

⁶⁰ *International Trade Reporter*, 21 February 2002, 298-300; 14 March 2002, 460-1; 21 March 2002, 504-5; 28 March 2002, 522-4; *Inside U.S. Trade*, 25 January 2002, 25-6; 22 February 2002, 1, 22-3; 15 March 2002, 7-8; 22 March 2002, 1, 25-7; 29 March 2002, 11-2; 10 May 2002, 3-5.

major US companies, such as Weyerhaeuser and Georgia-Pacific, have not anymore participated actively in the Coalition.⁶¹

Even before the expiration of the SLA, Canada turned to the WTO with a view to preventing the application of US trade remedy provisions against its softwood lumber exports. Since 2000, Canada has taken no less than six actions within the WTO against various elements of US trade laws, regulations, practices, and decisions. In May 2000, Canada took preemptive action to challenge US trade regulations explicitly allowing export restraints, such as raw log export controls, to be considered as countervailable subsidies. As the WTO Agreement on Subsidies and Countervailing Measures defines a subsidy explicitly as a 'financial contribution,' a WTO panel in June 2001 ruled that export restraints were in no manner a financial contribution and therefore not countervailable.⁶² In January 2001, Canada also challenged US trade provisions effectively preventing prompt elimination of AD and CVD orders when found to violate international trade rules. A WTO panel in June 2002 dismissed the case as premature, as this US legislation had not yet been applied against Canada.⁶³ With 10 other states including Mexico and the European Union, Canada objected to the so-called Byrd law under which final AD and CVDs are distributed to the petitioners, as this results in unfair subsidies, exceeds the remedies for unfair trade spelled out in the WTO, and creates a further incentive for US firms to seek trade remedies. A single panel was established in September 2001 and, in its interim decision in July 2002, found that the Byrd amendment violated international trade law.⁶⁴

On 21 August 2001, Canada requested accelerated WTO consultations with the United States regarding the DOC's preliminary determination of CVD and of critical circumstances, as well as the US denial of expedited reviews for company-specific duty rates. In December 2001, a dispute settlement panel was set up. In its report in September 2002 the panel found that US CVDs on Canadian softwood lumber violated international trade rules. However, it is not a complete victory for the Canadian position. The panel found that stumpage rights were a 'financial contribution', a point long held by American authorities, but that the United States failed to establish the existence and amount of 'benefit', the other condition for imposing trade remedies.⁶⁵ On 6 March 2002, Canada

⁶¹ *Inside U.S. Trade*, 23 March 2001, 17-8; 6 April 2001, 1, 17.

⁶² *Inside U.S. Trade*, 2 June 2000, 1, 17-8; 4 May 2001, 1, 22-4; *International Trade Reporter*, 25 May 2000, 816; 5 July 2001, 1045-6; WTO, *United States – Measures treating export restraints as subsidies, complaint by Canada*, Panel report, WT/DS194, 29 June 2001.

⁶³ *Inside U.S. Trade*, 26 January 2001, 1-2; *International Trade Reporter*, 13 June 2002, 1060-1.

⁶⁴ *Inside U.S. Trade*, 29 June 2001, 11-2; Canada, *News Release No. 81*, 17 July 2002.

⁶⁵ World Trade Organization, *United States – Preliminary Determinations with respect to Certain Softwood Lumber from Canada*, WT/DS236/R, 27 September 2002.

also requested consultations with the United States concerning its preliminary finding that Canadian softwood lumber was dumped into the American market.⁶⁶ In this regard, recent WTO dispute panels in other cases have already found the US methodology for calculating dumping to contravene the WTO Anti-dumping Agreement. On 3 May 2002, Canada requested consultations on final US CVDs.⁶⁷

Between February and May 2002, Canada requested panel reviews under NAFTA Chapter 19 of the US final CVD, AD, and injury determinations. Canadian lumber firms have also requested a NAFTA panel review on final US ADs.⁶⁸ The key WTO and NAFTA decisions are expected in 2003. In addition, as of September 2002, three Canadian lumber companies, Canfor Corp., Doman Industries, and Tembec, have sought arbitration under the NAFTA Chapter 11 investor-state provisions to challenge the US CVD and AD determinations on Canadian softwood lumber. Canfor seeks damages of US\$ 250 million, while Doman's claim reaches US\$ 513 million.⁶⁹

Although the stiff US penalties applied from May 2002 severely hit the Canadian lumber industry, Canada may have concluded that it has not much to lose from waiting for WTO and NAFTA rulings. The reforms requested by the United States are not only imposed on another sovereign partner, they are far-reaching. Why would Canada acquiesce to such extensive foreign pressure if there were another realistic avenue to address the problem of its lumber exports to the United States? In this respect, a referral to the WTO of the key outstanding issue of whether stumpage rights could be considered as subsidies would allow for an authoritative decision that could bring considerable benefits to Canada. This corresponds to the cornerstone of Canada's postwar foreign policy of relying on international organizations both to ensure a rules-based trading system and to limit the harmful exercise of power by its US partner. Depending on the overall outcome of the Canadian trade actions before the WTO, undesired public policy reforms could be avoided and Canada's standing could be strengthened in its dealings with the United States.⁷⁰

⁶⁶ Canada, *News Release No. 24*, 6 March 2002.

⁶⁷ *International Trade Reporter*, 9 May 2002, 853-4.

⁶⁸ See *International Trade Reporter*, 28 February 2002, 365-6; Canada, *News Release No. 28*, 22 March 2002.

⁶⁹ *International Trade Reporter*, 8 November 2001, 1803; www.naftalaw.org.

⁷⁰ See a recent backgrounder publication from the C.D. Howe Institute, authored by Lawrence L. Herman, *Softwood Lumber: The Next Phase*, 6 December 2001, that recommends that Canada press ahead on all available legal fronts with a view to ensuring an outcome to set a better precedent for trade disputes such as Softwood Lumber.

In the meantime, negotiations between Canada and the United States over softwood lumber trade may still resume to arrive at a mutually acceptable solution to the dispute, notably in view of the outcomes of some of Canada's WTO challenges. Indeed, a few days after the WTO panel's preliminary decision against US CVDs on Canadian softwood lumber in late July 2002, it was announced that the Canadian-US negotiations were to resume by late August 2002. On Canada's side, all provinces and their industries apparently favour the resumption of bilateral negotiations.⁷¹

Concluding Remarks

As to the essential problem for Canada of its exports to the United States being liable to retaliatory measures, it was clear by the mid-1980s that the definitions of 'dumping,' 'subsidy,' 'injury,' and 'industry' in US law and practice had become sufficiently flexible to accommodate virtually any petition for trade remedy. Despite the results of successive multilateral trade negotiations, such definitions remain sufficiently elusive to allow US authorities considerable leeway to impose retaliatory measures. Canadian industries should thus be aware that continued access to the American market depends critically on not exceeding some explicit or implicit market share. That market forces are responsible for shifts in market share does not appear to be a sustainable defense before US authorities, at least in politically visible cases such as Softwood Lumber.⁷²

In a major conflict such as the one involving softwood lumber, the United States has proved willing to assert its interests with a disregard for CUSFTA/NAFTA provisions to which it had itself agreed to resolve such issues. In fact, in the Softwood Lumber dispute, 'the world's largest bilateral trade dispute,' state interest as well as the respective leverage that each state enjoys vis-à-vis the other have proved determinant rather than any other factors such as international trade provisions. Such disregard has entailed that the search for ad hoc temporary settlements to suit American interests has continued to be on the agenda in the long-standing Canada-US conflict over softwood lumber.

One may argue that the CUSFTA/NAFTA provisions were (at least partly) observed in Softwood Lumber III as the bilateral review process was completed and the US agreed to return the collected duty amounts.

⁷¹ *Le Soleil*, 7 August 2002, C3.

⁷² Percy and Yoder, *Softwood Lumber Dispute*, xxiii.

Yet, such a view can hardly be sustained. The United States deliberately amended its trade legislation and regulations in order to overturn the Softwood Lumber subsidy panel's decision and facilitate the imposition of duties on Canadian lumber imports. Then, Canada and the US embarked on consultations that were to lead to a settlement outside the NAFTA.

It would be interesting to investigate to what extent a case such as the Canada-US Softwood Lumber dispute is unprecedented in international trade. This dispute is certainly unique in its elements and evolution. Yet, instances of long-running trade conflicts where major interests are involved and where compromises are devised outside the realm of international trade regimes are not uncommon. Canadian wheat exports have also been subject to long-lasting differences with the United States that have led to export constraints, the US complaining about the unfairness of the Canadian Wheat Board. Outside Canada-US trade, steel has long been the object of protracted negotiations between the United States and Europe marked by several instances of either bilateral deals or AD impositions. Here, it may be noted that in 2002 the exemption of Canada and Mexico from the US unilateral tariffs on steel imports could be attributable to membership, or partnership, in the NAFTA regime.

The high level of economic integration between Canada and the United States is striking. What is less certain and more controversial is the effective basis of such integration. International trade regimes, namely the GATT/WTO and the CUSFTA/NAFTA, do not appear to be primary determinants, but state power and interests, at least in a major dispute such as Softwood Lumber. This has led to a situation where the rules of the game have been periodically rearranged on an ad hoc basis to suit the short-term interests of the most powerful country, namely the United States. If this in no way leads to disintegration, it certainly corresponds to anarchical integration. The recent referrals by Canada to the WTO and the NAFTA of US trade provisions and actions against its softwood lumber exports is likely to further mitigate power politics, although the latter may well continue to prevail.

As an overt case of power politics, the Softwood Lumber dispute is again far from exceptional, although we saw that the United States has somehow been constrained by the need to justify its actions in legal terms and to make them appear compatible with international rules. The CUSFTA and later the NAFTA were expected to be the cornerstone of Canada-US trade relations. For Canada, this would have entailed a partnership on a more certain and equal basis. Yet, US attitude, as in the case of the Softwood Lumber dispute, has clearly not resulted in such a new partnership.