

INTERNATIONAL TRADE
SOFTWOOD LUMBER, CONSTRUCTION AND BUILDING PRODUCTS COMPANIES IN LIMBO AS U.S. AND CANADA ATTEMPT TO RESOLVE NEW SOFTWOOD LUMBER DISPUTE

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Softwood lumber producers, remanufacturers, construction, building products companies, importers and shippers are waiting to see whether the United States and Canada can work towards heading off another softwood lumber trade dispute. The dispute revolves around the expiration of the Canada-U.S. Softwood Lumber Agreement (Agreement) on October 12, 2015, which began a one-year truce during which the countries can try to agree to a new deal. President Barack Obama and Prime Minister Justin Trudeau met yesterday and agreed to intensively explore all options and report back within one hundred days on the key features that would address this issue.

The expired Agreement ended a lengthy trade dispute between the two countries during which the U.S. collected approximately \$5 billion in anti-dumping and countervailing duties from Canadian producers. If a new deal cannot be reached before October 12, 2016, the U.S. Lumber Coalition (Coalition) is free to initiate another round of costly litigation against Canadian producers.

The scope of products to be affected in any outcome is far-reaching. Companies on either side of the border, who are involved in softwood lumber, the building product sector, and construction, including producers, importers, exporters, distributors, retailers and consumers of softwood lumber products and remanufactured products (including studs, flooring, trusses, joists, decking, fencing, railing, lattice, siding, trim, molding, pallets, packaging), engineered wood products, oriented strand board, laminated veneer lumber, pressure treated lumber as well as home lumber products contained in single family home packages, should be monitoring developments now and taking those measures necessary to promote and protect their interests in what will either be renewed litigation or a negotiated settlement.

Since the Agreement expired, shipments of Canadian softwood lumber products may have increased, which could have adverse impacts in any new deal or litigation. Companies would be well-advised to carefully consider their production, shipping and purchasing strategies throughout the supply chain during this interim period.

Dickinson Wright has considerable expertise in this area and is available to assist companies in mitigating the effect on their business of any new agreement or litigation.

The Core Issue: Subsidization

For more than four decades, Canadian softwood product exports to the U.S. have been the subject of a trade war, with four other major tussles between the countries since 1982. Canada is a major exporter

of softwood lumber products to the U.S., and timberlands in all provinces except the Atlantic region are almost exclusively owned by the provincial government as opposed to private landowners, a stark contrast to the U.S., where the majority of lumber comes from privately owned land. Canadian lumber companies pay stumpage fees to provincial governments for the right to cut timber on provincially owned land. Stumpage fees are not determined exclusively by market forces. U.S. lumber producers maintain that the provincial governments set stumpage fees that are too low, and that imports of softwood lumber products from Canada are "subsidized" and cause injury to U.S. producers.

Last Round of Litigation

The softwood lumber dispute focuses on the application of U.S. trade remedies against Canadian softwood lumber imports. International law permits the U.S. to take retaliatory action against two trading practices considered to be unfair.

The first is dumping, which is selling goods to the U.S. for less than the price in Canada; or for less than cost plus a reasonable profit. If dumping is causing or threatening to cause material injury to domestic producers, the U.S. may offset the dumping by imposing an anti-dumping (AD) duty equal to the difference.

The second unfair practice is subsidization. If imports of subsidized softwood lumber are causing or threatening injury to domestic producers, the U.S. may impose a countervailing (CVD) duty to offset the subsidy. In the U.S., dumping and subsidy determinations are made by the Department of Commerce (DOC) and material injury determinations by the International Trade Commission (ITC).

During the last lumber trade dispute between 2001 and 2006, the DOC slapped combined AD and CVD duties of up to 27.22 percent on imports of softwood lumber products from Canada, resulting in numerous appeals and re-determinations of the ITC's injury decisions and DOC's determinations of dumping and subsidy to the U.S. courts, NAFTA Panels and the WTO Appellate Body. Some Canadian companies (British Columbia's Canfor Corp., Terminal Forest Products Ltd. and Montreal-based Tembec Inc.) launched claims against the U.S. government under Chapter 11 of NAFTA, claiming that the government's actions violated its obligations to ensure that investors such as themselves "are treated in accordance with international law, are treated fairly and equitably, and are treated no less favorably than their United States competitors"—that is, the Coalition.

By the time the Softwood Lumber Agreement was signed on September 12, 2006, approximately \$5 billion in unliquidated AD and CVD duties had been collected by DOC.

2006 Agreement

On September 12, 2006, the US and Canada signed the Agreement to

end the litigation. After two amendments, it expired on October 12, 2015, starting a one-year litigation moratorium. In other words, new U.S. unfair trade cases may not be brought by the Coalition against Canadian lumber before October 12, 2016.

The product coverage of the Agreement matched the product coverage of the countervailing and antidumping duties (softwood lumber products and a broad remanufactured wood products and home builder kits). Indeed the scope of the Agreement expanded as Commerce determined an increasingly number of softwood lumber products to be covered by the Agreement.

Canada, through the Canada Revenue Agency, imposed, administered and collected export measures on a broad range of softwood lumber products from Canada. Exports from BC were subject to Option A, which imposed higher taxes on softwood lumber product exports. Mills in Quebec, Ontario, Manitoba, and Saskatchewan choose Option B, which combined export taxes ranging from 5 to 15 percent and quotas depending on the level of lumber prices. These measures became more restrictive when the price of lumber fell, with no tax and no quota where prices were above US\$355 per mbf.

Lumber that was remanufactured by impending remanufacturers was taxed at the lower value of the production input, whereas integrated remanufacturers were taxed at the price of the finished products.

Lumber produced from logs harvested in the Maritime provinces, the Yukon, the Northwest Territories or Nunavut is excluded from the border measures, as is lumber produced by certain Canadian companies, primarily along the Quebec/U.S. border, that were excluded from the countervailing duty.

Disbursement of the \$5 Billion

The Agreement spelt out in detail how the nearly \$5 billion in AD and CVD duties collected since 2002 would be allocated upon termination of the litigation. Of those duties, \$1 billion stayed in the U.S., \$450 million was set aside to a fund for "meritorious initiatives," \$500 million was distributed to the Coalition members who brought the trade case, and the remaining \$50 million went a binational industry council. The remaining deposits of approximately \$4 billion were returned to U.S. importers, who were generally affiliated with Canadian mills.

Issues Going Forward

Canada and U.S. officials will face obstacles as they work on a new softwood lumber agreement because of disagreements between their respective lumber industries, as well as among Canada's provinces, on the type of export measures that should be applied to Canadian shipments. The U.S. lumber industry has signaled a preference for a hard quota on Canadian exports, while the Canadian government wants to ensure that any agreement includes more than one type of export measure, leaving it up to provinces to choose the option they

prefer. As the largest lumber supplier to the United States, British Columbia is shipping in large volumes, thus, will generally oppose a quota system. Quebec is demanding that its exports be excluded altogether under any new deal because it believes that its timber pricing system is market-based.

Also, some Coalition members may favour litigation, considering they received \$500 million under the last Agreement. The changed economics further complicate matters, as it is not certain that Canada would prevail in any new litigation in a similar way that it did in the last round.

For all of these reasons a prudent course of action for all affected companies on both sides of the border is to monitor and advocate where necessary to ensure that their interests are protected and promoted in any new deal or ensuing litigation. Those efforts include closely monitoring the developments over the next year and interjecting where necessary; undertaking the necessary efforts to make sure that the products that will be subject to any new litigation or deal are not adverse to their interest; advocating for particular export measures in any negotiated settlement; advocating for product and company exclusions or inclusions according to their interests; and understanding how any new AD or CVD duties or export measures, whether in the form of quotas or taxes, will be applied, paid and collected throughout the supply chain

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