

THE CANADA – UNITED STATES SOFTWOOD LUMBER DISPUTE:
A LOOK AT THE STATE OF CERTAIN ECONOMIC AND POLITICAL
INDICATORS AND THEIR RELATIONSHIP TO THE OUTCOME OF DISPUTES

by

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THESIS SUBMITTED IN PARTIAL FULFILLMENT OF
THE REQUIREMENTS FOR THE DEGREE OF
MASTER OF ARTS
in
INTERNATIONAL STUDIES

THE UNIVERSITY OF NORTHERN BRITISH COLUMBIA

December 2004

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ISBN: 0-494-04649-X

Our file Notre référence

ISBN: 0-494-04649-X

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Abstract

This thesis argues that softwood lumber disputes are highly politicized and that certain economic and political indicators may help to explain the outcome of disputes. The indicators are important considerations for Ottawa and Washington, in helping them make strategic decisions concerning softwood lumber.

The interests of Canadian softwood lumber exporters were best served when Commerce found no subsidies in the first countervailing duty case (CVD 1). This is the case, given that Canadian softwood producers were not subject to any restrictions, taxes or duties. With countervailing duty 2 (CVD 2), Canada and the U.S. negotiated a Memorandum of Understanding (MOU) which resulted in a 15% export tax on Canadian softwood lumber exports. Certainly, this was less advantageous to Canadian softwood producers than the outcome of CVD 1. In theory, the relative ad/disadvantageousness of countervailing duty 3 (CVD 3) was on par with that of CVD 2. That is, Canadian lumber was subject to conditional access to the U.S. market. Given that countervailing duty 4 (CVD 4) is ongoing, it is impossible to compare the outcome in terms of relative benefit to Canadian softwood exporters.

This analysis discerns how the conditions at the launch of CVD 1 differed from those when each of the other disputes was launched. One fixed set of indicators is used to analyze how certain political and economic indicators relate to the outcome of disputes: Market Share, State of U.S. Economy, Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade and Level of Protectionist Sentiment in U.S.

The analysis has shown that, contrary to the initial hypothesis, the indicators do not necessarily contribute a logical explanation for predicting the outcome of disputes.

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Acknowledgement

I would like to thank all who took the time to share their expertise on a personal level. This research would not have been possible without your participation.

Special thanks to my beautiful bride, family and dear friends for your support in getting me through this process — you have helped me overcome some difficult obstacles and this has meant so much to me.

Chapter One: Introduction

The softwood lumber dispute is a two-decade-old trade battle between softwood lumber producers in Canada and the United States, over the U.S. softwood lumber market. U.S. producers argue that they simply cannot compete with Canadian producers in their own marketplace because the Canadian Provinces subsidize domestic production.¹ These producers, and the trade associations that represent them, continue to lobby for the reform of provincial forest management into a market-based system. Canadian softwood producers, the provinces and Ottawa concede that the management of Crown forests is different in Canada than that found on state or federal forests in the U.S., but generally oppose allegations that the provinces subsidize production. They argue that it is impossible to compare the U.S. and Canadian forest management regimes, and that provincial forest management policies are no different than the policies that govern all other natural resource sectors in Canada.

U.S. softwood producers have been unable to resolve the softwood issue solely through diplomatic channels and have thus made it a point to use strong U.S. trade law remedies to help advance their interests. For the most part, the U.S. softwood lumber industry has done so by repeatedly requesting that the Department of Commerce (hereafter “Commerce”) impose countervailing duties² (CVD) on Canadian softwood lumber imports upon finding that the provinces do subsidize production. Only the third CVD challenge was triggered by Canada, when it pulled out of the Understanding it had with the U.S. to resolve the second CVD challenge.

It has thus far been the case that when Commerce finds affirmatively in its subsidy and/or anti-dumping investigations, Canada and the U.S. subsequently come to an (interim) compromise

¹ Subsidies are various forms of funding and programs used by governments to support domestic industries.

² The U.S. Department of Commerce can impose countervailing duties on an imported good, when it finds that the good has been subsidized, and the subsidies are injuring U.S. competitors.

to terminate the respective petition(s).³ The North American Free Trade Agreement (NAFTA) and World Trade Organization (WTO) dispute settlement mechanisms were designed to achieve this result — to encourage parties to resolve their differences through diplomacy, before resorting to arbitration. However, in the fourth case, diplomacy has thus far failed. The U.S. industry won support for its petition in the U.S. system and Canadian softwood lumber exports is currently subject to countervailing and antidumping duties. Ottawa is now challenging the legality of these duties through both the NAFTA and WTO dispute settlement mechanisms, while engaging in discussions with the U.S.

Canada and the U.S. may also have different views about whether it makes sense to enter into agreements like the (former) Softwood Lumber Agreement (SLA), given the apparent inconsistency between such agreements and the spirit of free trade under the North American Free Trade Agreement (NAFTA).

According to John Ragosta, of U.S. law firm Dewey-Ballantine,⁴ the SLA does not contradict the objectives of the NAFTA because “U.S., Canadian and WTO laws recognize that cases can be settled through bilateral suspension or termination agreements” such as the Canada–U.S. SLA.⁵ He also argues that without provisions in the NAFTA that affirmed the rights of parties to respond to unfair trade practices, there would have been insufficient political support for the Agreement. Ragosta also draws attention to the fact that Chapter 19 of NAFTA

³ In the first CVD case, Commerce found no subsidies. Therefore, Canada had no reason to talk with the U.S. When Commerce found affirmatively in its preliminary determination in the second CVD case, Canada and the U.S. negotiated a Memorandum of Understanding (MOU); with Canada agreeing to impose a tax on its softwood exports. An affirmative subsidy finding in the third CVD case led to the negotiation of the Softwood Lumber Agreement (SLA). In the fourth subsidy case, the U.S. imposed CVD and AD (anti-dumping) duties on Canadian softwood lumber exports. This case is presently ongoing - Canada and the U.S. continue to make modest attempts at reaching some form of compromise.

⁴ Dewey-Ballantine is one of the top trade law firms in the U.S. and is counsel for U.S. industry on softwood lumber.

⁵ It is important to note that because the SLA was negotiated after NAFTA, it is not directly referred to in the Agreement.

“expressly recognizes” the right of Parties to continue to impose duties on dumped or subsidized imports which injure or threaten to injure domestic producers.⁶

Gordon Morrison, the former Deputy Director of the Softwood Policy Division in the former Canadian Department of Foreign Affairs and International Trade (DFAIT),⁷ indicated that it is difficult to determine conclusively whether the SLA is consistent with NAFTA, because there has yet to be a challenge on the issue (Morrison, 2000). It is possible that Canada and the U.S. recognize the potential conflict between the agreements but do not want to undermine support for NAFTA, nor the potential to extend NAFTA to create a Free Trade Area of the Americas (FTAA). The Canadian Government, itself, has yet to pass judgement on the question.

This chapter explains the analytical model employed in this thesis by explaining the value of adopting one fixed-set of indicators and what the indicators contribute to understanding the outcomes of softwood disputes. The reader is versed on the main issues of contention between Canada and the U.S. on the matter of softwood lumber and is exposed to a small sample of the existing works. The intent is to provide the reader with a basic understanding of the main issues relevant to softwood lumber and to clearly map out the main objectives of this analysis.

This thesis argues that softwood lumber disputes are highly politicized and that certain economic and political indicators may help to explain the outcome of disputes. The indicators are important considerations for Ottawa and Washington, in helping them make strategic decisions concerning softwood lumber which, in turn, shape the outcome of these bilateral disputes. In particular, the indicators help Canada and the U.S. determine whether or not it is in their best interests to negotiate a compromise resolution to CVD and/or AD cases. Canadian softwood lumber exports were unaffected when Commerce found no subsidies in CVD 1; exports were not subject to any restrictions, taxes or duties. The opposite was true of the

⁶ Dumping occurs when a producer in one country sells their product in a foreign market at a price below their own production costs. This is done in order to drive competitors out of the marketplace.

⁷ DFAIT the “Department of International Trade” as of January 2004.

outcomes of CVD 2 and CVD 3, and CVD-AD 4 is ongoing. The analysis will discern how the conditions that existed at the launch of CVD 1 differed from those that existed when each of the other disputes was launched. It was unclear at the outset of this research what was different about CVD 1, that it has thus far been the only dispute to conclude without any restrictions on Canadian softwood lumber exports. The hypothesis was that there were likely a number of political and economic indicators that would help explain the varying outcomes. The indicators include: (a) Market Share: share of U.S. softwood lumber market that Canadian producers hold; (b) State of U.S. Economy: Gross Domestic Product (GDP), overall unemployment, unemployment in the lumber and lumber products sector; (c) Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade: were there any looming trade negotiations, or other outstanding disputes between Canada and the U.S. to which the U.S. held significant stakes at the time when each dispute was launched; (d) Level of Protectionist Sentiment in U.S.: number of countervailing duty (CVD) and anti-dumping (AD) cases launched by the U.S. against all countries in the year that each dispute was launched and the number of WTO cases launched against the U.S. in that same year. These particular indicators were selected, given that the information was readily accessible and/or measurable for the purpose of analyzing a relationship with the outcome of each dispute. For example, the latter indicator may be used to determine whether a (relatively) high-level of U.S. protectionist sentiment had any discernible influence on Canadian and U.S. strategic positions and subsequently the outcome of that dispute.

There are other indicators that could have been examined in this thesis, but have been excluded because, in relative terms, they appear to be less significant considerations for Ottawa and Washington in helping them reach strategic directions on softwood lumber. For example, “trade balance” could have been used as a measure of the ability of Canada to retaliate against the U.S. when it imposes punitive duties, because when Canada is running a large trade surplus, there are often more sectors that would lose than gain from such a policy. However, given the

dependency of Canadian goods exporters on the U.S. market, retaliation is rarely a pragmatic option. Another option was to compare the mean value of softwood lumber exports from Canada to the U.S. before the launch of each CVD case, with the mean value of exports after the treatment. This indicator would examine whether the U.S. price of softwood lumber tended to rise significantly following the launch of a CVD and/or AD cases. If this trend was evident, the U.S. might be inclined to launch investigations more liberally. This would certainly have implications both for Canadian and U.S. strategy. Similarly, the “volume of softwood lumber exports from Canada to the U.S.” could have been used as an indicator. The logic here is that the U.S. is more inclined to negotiate a resolution with Canada at a time when it is importing a relatively lesser volume of lumber from Canada. However, neither the mean value, nor volume of softwood lumber exports, are as informative to Canada and the U.S. as is market share. This is the case because market share provides a good measure of how well Canadian softwood lumber exporters are faring in U.S. markets. The value and volume indicators do not themselves provide any significant insight regarding Canadian exporters’ presence in the U.S. softwood lumber market. For example, a relatively high value of softwood exports from Canada could simply reflect high U.S. demand for lumber (and consumption) in a given period. Similarly, a high volume of softwood lumber exports does not necessarily mean Canadian producers are injuring U.S. softwood lumber producers.

The outcome of a dispute is the point when Commerce reaches a negative determination in its subsidy and/or dumping investigations, or when Canada and the U.S. reach some form of compromise. For the first dispute (CVD 1), the outcome came in May 1983, when the U.S. issued its final negative determination of subsidies. For the second dispute (CVD 2), the outcome came in December 1986, when Canada and the U.S. agreed on terms of the Memorandum of Understanding (MOU). The outcome of the third dispute came in April 1996,

when Canada and the U.S. agreed to the terms of the Softwood Lumber Agreement (SLA). The fourth dispute (CVD-AD 4) is ongoing.

Each dispute is put into context with a discussion that identifies who the policy actors were at the time and how these actors mobilized their resources throughout the policy-making process. In doing so, the discussion provides a step-by-step account of the policy process by which the network addressed the softwood issue at the time.

Several important facts remain about the softwood lumber dispute, each of which deserves greater attention. The following section presents the main areas of debate between the U.S. and Canada and touches upon the question of whether Canadian lumber firms benefit from lower production costs.

Background: Canadian and U.S. softwood lumber producers compete for the U.S. market and have different views on how Canadian forestry should operate

At the hub of the Canada-U.S. softwood lumber dispute are differences in forest management policies and practices between the two countries. In the United States, 71% of timberland is privately owned. Of these private forests, 58% is non-industrial private (some of which is used for forestry), and 13% forest industry private (Smith, et. al, 2001, p.8).

U.S. firms secure rights to standing timber on public forests for 1-3 year terms and on private forests for 1-2 year terms. On both public and private forests, firms pay fixed harvesting costs arrived at through competitive bids such as sealed bids, oral auctions, sealed bid followed by oral auction and negotiated price (B.C. Ministry of Forests, 2001. p. E1; H&W Saunders & Rickard, 2001, p. 33). The starting bids are calculated by adding the estimated costs of building access roads to the appraised value of the resource. Companies are not obligated to harvest all the timber on the land they lease. However, those harvesting from government-owned forests are encouraged to do so, in order to cover contractual obligations such as reforestation.

In Canada, the provinces own and manage 71% of all forests. The Federal Government owns 23% of Canada's forests and given that most of these are located in the territories, Ottawa has devolved management authority to the territorial governments. The remaining 6% is privately owned by forest firms, communities and families and is located mainly in the Maritime Provinces (Natural Resources Canada, not dated, On-Line A).

Approximately 73% of all production is under long-term harvesting leases of 15-25 years (B.C. Ministry of Forests, 2001, p. E1). The majority of these leases are 15-year terms and allow license holders and the provincial government to negotiate new contracts every five years.⁸ Short-term leases with the provinces last from 1-5 years and represent about 17% of provincial output.⁹ The remaining 10% is produced from private forests. Access is secured through competitive bidding (similar to the U.S. system) and there are no leases and few restrictions on harvest.

All of the provinces revise stumpage rates, during each calendar quarter, based on the average price their producers receive for their lumber in Canadian dollars, as published by Statistics Canada (B.C. Ministry of Forests, 1998).¹⁰ This means that if the market price of lumber falls over one quarter, the provinces lower stumpage fees for the next quarter. Many firms with major logging licenses are required to cut 50% or more of their Annual Allowable Cut (AAC) in order to maintain their provincial leases (Leyton-Brown, 1985, p. 44). B.C. used to employ a "cut control" system that penalized major license holders who failed to harvest plus or minus 10% of their AAC in each year of a 5-year period. The idea was to provide greater employment stability in B.C., but was eliminated as part of the government Forestry

⁸ In the province of B.C., there are both replaceable and non-replaceable forest licenses. Non-replaceable licenses last up to 20 years.

⁹ The above figures are approximate as they reflect B.C. softwood lumber production.

¹⁰ The provinces collect stumpage fees on standing timber removed from government-leased forests. In Canada, stumpage rates reflect end-product prices. This means that current timber prices are entered into the calculation of stumpage rates. Producers do not have to worry about being bound to harvesting costs that cannot be recovered from revenues.

Revitalization Plan (FRP). The FRP involves several changes to B.C. forestry and environmental legislation, transfers management responsibilities to license holders for their own timber supply areas and reallocates and subjects a higher share of coastal forests into competitive bids (Continuing Legal Education Society of British Columbia, November 2003, online). The B.C. Liberal government has stated that it intend to use competitive bid prices as the guidelines for crown stumpage rates once Forest Practices Code (FPC) has been fully phased out on Jan 1, 2006 (British Columbia Liberals, January 2004, online).

It is a strategic decision of the U.S. softwood lumber producers to downplay imperfections with the U.S. forest management system. Instead, U.S. producers allege that the real source of its economic difficulties is subsidized lumber — which makes it impossible for U.S. producers to compete in their own market (Jadrzyk, 1998). The argument is that as owners of public forests, the provinces ought to absorb a larger proportion of forestry revenues through stumpage.¹¹

One International Trade Commission (ITC)¹² report entitled “Conditions Relating to the Importation of Softwood Lumber into the United States” noted that average stumpage rates in Canada were 10.3% of stumpage fees on public lands in the U.S. West in 1984 (Percy & Yoder 1987, p. 62). This is strictly a stumpage comparison, which avoids the fact that Canadian producers face other significant costs, such as environmental costs more frequently tied to longer-term agreements. Further, cost comparison analyses have become more complex since the first dispute in the 1980s, so much so that a basic cross-border comparison of stumpage no

¹¹ Forest companies pay the provinces stumpage fees for harvesting trees. Until 1987, the provincial government in B.C. was responsible for collecting whatever was left over, after allowing for operating costs and profit (Residual/Modified Rothery System). Under the residual system, the province would collect less stumpage when profits were down, and more when profits were up. The stumpage system changed in 1987, when “comparative value pricing” (CVP) kicked in. Instead of stumpage being tied to industry profits, it would be adjusted based on the price of lumber on the Statistics Canada softwood lumber price index. For example, if the price of lumber went up 10%, stumpage would increase by the same margin. In 1994, a “super stumpage” system was introduced. This system retained the same underlying principles as CVP, but higher fees would kick in once market prices climbed above set levels (\$250 and \$400/cubic metre) (as cited in Cashore, Hoberg, Howlett, Rayner, & Wilson, 2001).

holds merit. Nevertheless, the comparison does raise an important question: Do the provinces “subsidize” or bestow some benefit to producers by deliberately setting stumpage lower than the rate that might be arrived at in a non-administered system? Interestingly, prior to the release of the ITC report back in the 1980s, the U.S. Department of Commerce stated:

We believe that a comparison of Canadian stumpage prices with the U.S. prices would be *arbitrary and capricious* in view of: (1) the wide differences between species composition; size, quality and density of timber terrain and accessibility of the standing timber throughout the United States and Canada; (2) the additional payments which are required in many provinces in Canada, but not generally in the United States; (3) the fact that in recent years, prices in national forests in the United States have been bid anywhere between two to five years in advance of cut, without taking into account the fluctuations in demand for lumber; and (4) the fact that in recent years the U.S. Forest Service has restricted the supply of timber in certain national forests due to budgetary and environmental constraints (Percy and Yoder, 1987; U.S. Federal Register 24168).

The above conclusion is troublesome for two reasons. First, while the ITC clearly identified problems with the U.S. forest management system in 1987, there has been no significant changes to the U.S. bidding system since then. Therefore, it is difficult to understand how the U.S. Government could possibly feel justified in criticizing provincial forest management policies, including the setting of stumpage fees. Second, the U.S. Government itself stated, on the record, that it would make no sense to compare stumpage fees in Canada to those in the U.S. This position was subsequently abandoned when the ITC determined that subsidies were causing material injury to U.S. producers (June 1986), but nevertheless challenges the validity of U.S. studies that show provincial stumpage fees as a fraction of U.S. stumpage.

Canadian softwood producers disagree with the argument that the provinces are subsidizing producers because stumpage rates are lower in Canada than in the U.S. They insist that there is no sense in conducting cross-border comparisons of stumpage because there are significant differences in the forest management practices of Canada and the U.S.

¹² The ITC is an independent, quasi-judicial federal agency that investigates the impact of imports on U.S. industries.

Given the magnitude of differences between these two forest management regime it is indeed difficult to compare Canadian and U.S. softwood lumber producers' costs. U.S. softwood lumber production is predominantly from logging rights obtained through competitive bids, while Canadian lumber production occurs mainly from longer-term leases between producers and the provinces. Arguably, a cross-border comparison can, however, be used to provide some indication of whether production costs differ significantly between Canada and the U.S.

Comparing Costs

Do the provinces deliberately set low stumpage fees in order to give domestic softwood producers a competitive advantage in the U.S. marketplace, or is lower stumpage in Canada needed to offset additional or higher costs that Canadian softwood lumber producers face?

First, Canadian producers face additional costs under long-term agreements. For example, only Canadian producers are obligated to pay average stumpage fees on the removal of stumps, which are removed for matters related to forest health and longevity (Percy & Yoder, 1987, p. 71). There is rarely a market for these stumps and therefore no revenue to help cover these fees.

Producers in the interior of B.C. face additional costs as a result of a greater tree species mix. The Province's diverse forest base is more expensive to harvest than less diverse forest stands in the U.S. (Percy & Yoder, 1987, p. 63).

According to the U.S. Forest Service, costs for harvesting softwood on private and public lands in the U.S. is essentially the same because "environmental standards for logging operations are very similar on private and public lands... and cost difference is more a product of logging method than ownership" (U.S. Forest Service, January 2001).¹³ On occasion, public agencies do require that more expensive operations, such as helicopter logging, be used in order to protect

¹³ No U.S. agency collects information to compare harvesting costs in the U.S. because private companies consider such information proprietary. It is therefore impossible to compare costs today, to say, harvesting costs in the early 1980s.

public and private lands identified as ecologically sensitive (ibid.). However, owners of private forests primarily employ this type of higher-cost logging operation when it is the most economically efficient harvesting method available.¹⁴

Some evidence suggests that Canadian softwood lumber producers face high environmental compliance costs. For example, B.C. producers must adhere to the Forest Practices Code standards for soil conservation and “green-up limits,” which restrict logging in areas where tree height is low. The Code also prescribes smaller cut blocks so as to minimize environmental damage and aesthetic damage to landscape (Clarke, 1997). At the same time, it is evident that Canadian softwood lumber producers have not faced environmental compliance costs associated with endangered species protection, until recently, when the *Species At Risk Act* (SARA) was proclaimed (June 2003). This may have provided a comparative advantage to producers with operations in the U.S. (Scott, et. al, 2001). Some evidence of reform is emerging in B.C. where, under the new FRPA, the Forest Practices Board (FPB) conducts periodic third party audits of government and forest companies to determine whether they are upholding the requirements of forest practices legislation. The intent is a shift away from traditional environmental enforcement, toward a system that also considers government or non-action in the event of non-compliance.

The Forest Practices Code has also generated additional road costs for B.C. producers in recent years, because smaller cut blocks means that more roads are needed to maintain the same level of production. For example, in B.C., road costs ballooned nearly 300%, from \$263 million in 1992 to \$761 million in 1997 (Council of Forest Industries-COFI, 1998).

Canadian softwood lumber industries are generally more technologically advanced inside the mill than are U.S. producers. These technologies have significantly lowered their production

¹⁴ A full comparison of environmental compliance costs would be quite extensive and is therefore outside the scope of this thesis.

costs, increased the profitability of the industry and given Canadian firms a comparative advantage over U.S. firms, who frequently use outdated, more costly operations (Canada, Department of Foreign Affairs and International Trade, 2001, Reference A).

Taking into consideration the preceding factors, Canadian softwood lumber producers do face some additional costs exporting to the U.S. These include costs associated with long-term tenure agreements, greater species mix and other provincial requirements. Canadian producers are also more efficient than their U.S. competitors, which offsets some of the additional costs described above. This draws one to consider how Canadian producers' costs might compare to U.S. producers, should the latter achieve more efficient production.

If it were the case that Canadian and U.S. softwood was produced under similar conditions, one could argue that higher production costs in Canada are somewhat offset by the country's lower stumpage rates. However, the reality is that there are several significant differences and far fewer similarities between forest management in Canada and the U.S. This makes a comparison of Canadian and U.S. softwood lumber production costs an extremely onerous task.

What Does All This Mean For Canada? Canada's Stakes in the Softwood Lumber Dispute

The softwood lumber sector is a critical component of the Canadian economy. Canadian industries export C\$10.3 billion worth of softwood lumber to U.S. markets each year (Canadian Council of Forest Ministers, On-line). There are approximately 300 Canadian communities dependent on forestry as the primary source of employment (DFAIT, not dated, On-Line A). In 1997, there were more than 365,000 Canadians directly employed in logging, lumber and pulp & paper industries, and another 465,000 employed in indirectly related jobs. Together, these jobs accounted for 1 out of every 17 Canadian jobs (Natural Resources Canada, not dated, On-Line A).

B.C.'s vast expanse of forest coverage has made softwood lumber the staple of the provincial economy. In 1996, B.C. was responsible for 57.6% of Canada's total softwood exports and 30% of total world exports (COFI, 1998). Aside from the direct benefits of employment in this sector, others are required to service the industry and transport products to their respective markets (Jones, 1987, p. 115). Some estimate that the indirect benefits are at least two times greater than the direct benefits in the form of wages (ibid.; PLC Reed & Associates, 1973).

The interests of Canadian softwood producers are not all homogeneous. Naturally, all Canadian producers that export softwood to the U.S. wish to do so without restrictions, do business without the threat of countervailing or anti-dumping (AD)¹⁵ duties being imposed on their exports and maintain their existing forest management regimes. The Atlantic Provinces were exempt from the SLA and the U.S. has assured them that they will again be free from subsidy challenges in the post-SLA period.¹⁶ The Atlantic Provinces also recognize that without a renewed SLA, or new duties imposed, they would potentially be subject to greater competition from Canadian producers previously subject to the terms of the SLA.

British Columbia, Alberta, Ontario and Quebec, together, have been subject to several U.S. CVD challenges over the past 21 years and face unlimited future challenges if they fail to reach some compromise in the post-SLA period.

It is no simple task to define the interests of the Canadian Government in the softwood lumber dispute. This is because while Canada has the constitutional jurisdiction over trade and foreign policy matters, the provinces have jurisdiction over their own natural resources. Ottawa is generally careful to show each of the provinces that their interests are being represented fairly when entering into negotiations. For simple economic reasons, Ottawa must also advance a

¹⁵ The U.S. Department of Commerce can impose antidumping duties on imports when it finds that an imported good is being sold in the U.S. at a price lower than cost. This is to prevent foreign competitors from "dumping" goods at a price that is so low that it forces domestic competitors in the U.S. out of business.

position that will serve the greater interests of the Canadian softwood lumber export industry. Ottawa could make it a priority to advance the interests of B.C. exports which represent more than 50% of Canadian softwood exports to the U.S. (the bulk of which are from the interior region of the province). Forestry generates tremendous tax revenues, not only for B.C., but also for Ottawa. At the same time, as with most major policy decisions, Ottawa must weigh this interest with those of its own political party. With almost two-thirds of the Canadian voting population residing in Ontario and Quebec, Ottawa has significant stake in asserting a stance that seems reasonable to these interests of Ontario and Quebec.

The following provides a small sample of the analysis that has been circulated among the academic and business communities on the matter of softwood lumber.

Gagne (1999) tracks the history of the softwood dispute from the initiation of the first CVD case through about mid-term of the Softwood Lumber Agreement. He argues that while the Canada-U.S. Free Trade Agreement (FTA) and subsequently the North American Free Trade Agreement (NAFTA) were “expected to be the cornerstone of Canada-U.S. trade relations,” the U.S. has shown disregard for the provisions it helped to create for resolving trade conflicts; including those that concern alleged subsidies such as softwood lumber (Gagne, 1999, p. 85). Gagne argues that despite the presence of international trade rules, it is not uncommon for compromises to be reached outside of these regimes, as was the case with the SLA. The U.S. is portrayed as having bullied Canada into accepting conditions that were clearly in conflict with basic principles of free trade.

Cashore (1997) sees the co-existence of the (U.S.) Administration’s strong economic liberalization policies and an increase in “administered protection” as paradoxical. He presents four possible ways of resolving the long-standing dispute: (1) the U.S. could change domestic trade laws that are tipped to favour affirmative subsidy determinations; (2) B.C. could adopt a

¹⁶ Softwood lumber exports from the Atlantic Provinces have been subject to smaller anti-dumping duties.

competitive bidding system for forestry; (3) Canada and the U.S. could agree to allow free trade in raw logs between the two countries; (4) Canada and the U.S. could reach a “broad-based” understanding or mutual recognition agreement (MRA) about forest management pricing systems and regulations, or a more narrow MRA on issues of contention from earlier rounds of the dispute (Cashore, 1997, pp. 32-4).

Apsey and Thomas (1997) produced what may be the most comprehensive analysis of the softwood lumber dispute available, by providing a detailed account of the events that transpired since the first CVD investigation in 1982, up until the SLA. In doing so, the authors have taken great care to explain the function of NAFTA and WTO dispute settlement and appeals mechanisms, which is critical to understanding a complex web of legal issues involved in the softwood lumber dispute.

The discussion has thus far identified the purpose of this thesis, explained the main issues of contention between Canada and the U.S. regarding softwood lumber and reviewed a small sample of existing works. The following section defines the structure of the analysis and explains what each of the indicators contributes to the analysis.

The following chapter establishes a conceptual framework for the analysis by identifying the public, business/economic, government interests in the softwood lumber dispute, and explaining how policy and trade policy is developed in Canada and the U.S.

The substantive analysis begins in Chapter Three, at which point each of the disputes is examined on a chapter-by-chapter basis. Each chapter consists of two sections.

The first section details “What Happened” in the dispute by providing a chronological account of the events that transpired. Given that it is the U.S. mounting CVD and AD cases against Canada, the discussion focuses upon what was happening in the U.S. policy-making process during each dispute and how Canada responded to each challenge.

The second section of each chapter reports on a fixed set of indicators that provide concrete information about the U.S. political and economic climate at the time when each dispute was launched. The information will be used in the final chapter, to collectively analyze the relative influence of these indicators on dispute outcomes favourable to Canadian producers.

Below is a more detailed look at what each of the indicators will examine:

(a) Market Share

Canadian, U.S., Other Countries' relative share of the U.S. softwood lumber market. This indicator is used to examine the relationship between Canadian producers' market share and the outcome of disputes. When Canadian market share is higher at the time that a dispute is launched, than at the outcome of the previous dispute, is this inevitably followed with an affirmative subsidy/dumping finding in the U.S.? Is U.S. producers' share of the U.S. softwood lumber market more important? Are there other noticeable trends?

(b) State of U.S. Economy

This indicator examines Gross Domestic Product (GDP), overall unemployment and unemployment in the lumber and lumber products sector. The indicator is used to analyze whether any relationship exists between the state of the U.S. economy, at the time when a dispute is launched, and the outcome of the dispute. For example, is the U.S. more likely to produce an affirmative subsidy determination, and subsequently draw Canada into a negotiated settlement, if the U.S. economy is ailing when that dispute was launched?

(c) Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade

The U.S. is often able to dictate the conditions when addressing bilateral disputes with Canada, but may be more likely to bend when other stakes such as national defence, energy, or fresh water are brought into the equation. This indicator looks at whether there were looming trade negotiations, tensions, or other outstanding bilateral disputes in which the U.S. held significant stakes, at the time when each dispute was launched. The objective is to determine

whether there has been any discernible relationship between trade uncertainty and the outcome of disputes. Is the U.S. more likely to budge when it has other significant trade interests on the line?

(d) Level of Protectionist Sentiment

This indicator looks at the level of protectionist sentiment in the U.S. in the year when each softwood lumber dispute was initiated. The objective is to determine whether the level of U.S. protectionist sentiment is at all related to the outcome of disputes. Specifically, if U.S. protectionist sentiment is relatively strong in the year when a softwood lumber dispute is initiated, are U.S. softwood lumber producers more likely to achieve uncompromised relief against Canadian softwood lumber imports? Despite U.S. leadership in promoting economic liberalization and integration globally, the U.S. is notorious for habitually-investigating whether foreign competition is subsidized and/or materially-damaging U.S. industries. This is in large part because U.S. laws and trade policies encourage these routine investigations.¹⁷ More importantly, "the absence of penalties for frivolous complaints means that a plaintiff often incurs only small costs" from these investigations (Bhagwati, 1988, p. 48). Further, the laws and institutions for investigating the appropriateness of trade remedies are far from "models of impartiality and fairness" (Ibid.). According to Lenway (1985), it is all about industries "insulating the U.S. market from foreign imports to save American jobs." In other words, if duties are imposed on imports, domestic industries may benefit from increased sales, and in turn, may be able to save U.S. jobs.¹⁸ It is also evident that "countervailing-duty and anti-dumping actions can be utilized as tactical devices to soften up one's foreign rivals and propel them and their governments into negotiating voluntary restrictions on exports" (Bhagwati, 1988, pp. 52-3).

¹⁷This point will be illustrated further in the paper, in a discussion of the Byrd Amendment, an act passed by U.S. Congress in 2000, to channel duties collected from such trade complaints back to the affected petitioners.

¹⁸ On a similar note, several countries, including Canada, are presently challenging the U.S. Byrd Amendment; a U.S. law that requires U.S. Customs to channel collected duties to the U.S. industries affected. The plaintiffs argue that the Amendment violates the WTO Subsidies and Countervailing Measures (SCM) Agreement.

There were a number of possible methods for measuring the level protectionist sentiment in the U.S in the year when each dispute was initiated. For example, one could examine year-to-year “trade-weighted average tariffs” in the U.S. as a relative measure of U.S. interest in engaging in free trade with other countries.¹⁹ One significant problem with trade-weighted average tariffs, and other average tariff measures, is that they alone are an insufficient measure of protectionism. Other factors, such as quotas, import licenses, and domestic regulations also often have a significant impact on trade flows (Suranovic, 2003, on-line). Another problem with this measure is that while highly developed countries (e.g. the U.S.) are fully phasing-out tariffs, this alone provides no assurance that a country is necessarily becoming less-protectionist. In other words, the presence of fewer or less significant tariffs provides no guarantee that fewer trade complaints or disputes will be initiated.

One theoretical method for examining the level of protectionist sentiment in the U.S. in the year when a softwood lumber dispute is launched is to measure the extent that U.S. domestic and trade policies affect goods and services flow between itself and the rest of the world. The level of U.S. protectionism would equal the sum of all exports and imports under the U.S. domestic policy regime in the year a dispute is initiated, divided by the sum of all exports and imports given a U.S. domestic policy regime that has no impact on U.S. trade. The protectionism indicator would range from “0” (when government policies do not permit any form of trade) to “1” (when government policies impose no restrictions once-so-ever on trade). This measure makes some sense in theory but would impossible to put into application (Suranovic, 2003, on-line).

It soon became clear that it would be extremely difficult, if not impossible, to find a flawless and widely-accepted methodology for measuring protectionist sentiment in this thesis. At this point, it made the most sense to adopt a measure(s) that could make use of relevant,

¹⁹ This measure is calculated by dividing total U.S. tariff revenue by the total value of U.S. imports.

readily available data as the basis for measuring the level/strength of U.S. protectionist sentiment in the year when a softwood lumber dispute was initiated. Two measures were selected and given equal weight toward calculation of relative values for the annual level of protectionist sentiment from 1972-2002.²⁰ The first is the total number of CVD and AD cases initiated by the U.S. against all other countries in each year that a softwood lumber dispute was initiated. The rationale for this first measure is that this would provide considerable information about the relative year-to-year level of protectionist sentiment within the U.S. The second measure is the number of GATT/WTO cases initiated against the U.S. by all other GATT/WTO member countries in each year a softwood lumber dispute was initiated. This measure would provide some indication of the relative external frustration that U.S. trade partners were experiencing from U.S. trade policy each year a softwood dispute was initiated. Equal weighting of the 2 measures would produce a balanced, quantitative birds-eye view of domestic trade politics in the U.S. and the extent that other GATT/WTO Members challenged the U.S. in instances where they believed the U.S. had violated U.S. trade commitments.

A scale was developed for this thesis so as to generate qualitative and relative labels for the number of CVD & AD and GATT-WTO disputes initiated each year a softwood lumber dispute was initiated: CVD 1 (1982), CVD 2 (1986), CVD 3 (1991) and CVD-AD 4 (2001). Each scale contains seven intervals: Extremely Low (> -1.5 standard deviations or “sds”), Very Low (-1.1 to -1.5 sds), Low (-0.5 to -1.0 sds), Average (-0.4 to $+0.4$ sds), High ($+0.5$ to $+1.0$ sds), Very High ($+1.1$ to $+1.5$) and Extremely High ($> +1.5$ sds). The average number of CVD and AD cases initiated by the U.S. annually from 1972-2002 was 52 (Reinhardt, forthcoming; WTO On-Line) and the average number of GATT/WTO cases against the U.S. was 5.5. As an example of how the scale is applied, consider how the level of U.S. protectionist sentiment is

²⁰ Data goes back to 1972 as this is 10 years prior to the first CVD case launched by the U.S. on softwood lumber. Doing so makes it possible to have some sense of the level of protectionist sentiment in the U.S. in the years preceding this first case.

calculated for the first CVD case (CVD 1). In 1982, the U.S. initiated 95 CVD and AD cases against all other countries. Given that the average number of CVD & AD cases initiated annually from 1972-2002 is 52, we calculate $95 \text{ CVD \& AD cases} - 52 \text{ (the average)} = 43$ and know immediately that there was an above average number of cases launched by the U.S. across all sectors, including softwood lumber in 1982. By dividing 43 by the standard deviation for this data set CVD & AD cases, 28.7, it is evident that U.S. protectionist sentiment, according to this first indicator is 1.5 standard deviations above the mean, or “extremely high”. In that same year, 1982, 6 GATT cases were launched against the U.S. by all other GATT countries. Given that the average number of cases launched against the U.S. annually from 1972-2002 is 5.5, we calculate $6 \text{ GATT cases} - 5.5 \text{ (the average)} = 0.5$ and know immediately that there was an above average number of cases launched by all GATT-Member countries against the U.S. in 1982. By dividing 0.5 by the standard deviation for this second data set, 4.5, U.S. protectionist sentiment is 0.1 standard deviations above the mean, but falls within the “average” interval. When equally weighted, the “extremely high” CVD & AD and “average” GATT-WTO measures yield a “high-very high” level of U.S. protectionist sentiment; a calculated, relative measure of the level of protectionist sentiment in the U.S. in the year CVD 1 was initiated. Standard deviation data is also provided for the Market Share indicator however, this was not possible with the other two variables – State of the U.S. Economy and Uncertainty in Trade for the U.S.

Table 1. Measuring the Level of U.S. Protectionist Sentiment in Each Year that a Softwood Lumber Dispute was Initiated: The Number of U.S. Initiated CVD & AD Cases and the Total Number of GATT (WTO) Cases Launched Against the U.S. that Year.

SCALE (in standard deviations:	CVD 1	CVD 2	CVD 3	CVD-AD 4	AVERAGE NUMBER CASES INITIATED ANNUALLY 1972-2002	STANDARD DEVIATION OF DATA SET
EXTREMELY LOW > -1.5	1982	1986	1991	2001		
VERY LOW -1.1 to -1.5						
LOW -0.5 to -1.0						
AVERAGE -0.4 to +0.4						
HIGH +0.5 to +1.0						
VERY HIGH +1.1 to +1.5						
EXTREMELY HIGH > +1.5						
(A) Number of U.S. Initiated CVD and AD cases launched against foreign interests in year case launched	95	109	77	95	52	28.7
Range (+0.9 - +2.0)	1.5	2.0	0.9	1.5		
Qualitative Value	VERY HIGH	EXTREMELY HIGH	HIGH	VERY HIGH		
(B) Number of GATT/WTO cases launched against U.S. in year case launched	6	10	9	8	5.5	4.5
Range (+0.2 - +1.0)	0.1	1.0	0.9	0.7		
Qualitative Value	AVERAGE	HIGH	HIGH	HIGH		
AVERAGE OF QUALITATIVE VALUES A+B =						
LEVEL OF U.S. PROTECTIONIST SENTIMENT	HIGH	VERY HIGH	HIGH	HIGH- VERY HIGH		

The analysis addresses the fundamental hypothesis of this thesis, that softwood lumber disputes are highly politicized and certain economic and political indicators may help to explain why certain disputes conclude bearing no immediate impact on Canadian softwood lumber exporters, others conclude in negotiated settlements and potentially duties or taxes. Which of the indicators were most closely related to disputes that culminated in outcomes favourable to Canadian softwood exporters?

Summary

The softwood lumber dispute is a longstanding dispute driven by U.S. lumber firms seeking better conditions to compete with Canadian softwood lumber imports. U.S. firms complain that the provinces subsidize production, which provides Canadian softwood exporters with an unfair advantage over firms that must compete in the U.S. for logging rights. Canadian softwood producers have generally resisted U.S. pressure for forestry reform in the provinces and dismiss U.S. allegations of subsidization. Some literature suggests that U.S. policies towards Canadian softwood lumber imports are protectionist, and are contrary to principles of free trade.

The next chapter establishes the theoretical underpinnings for the case-by-case analysis, by identifying those parties which hold stakes in the softwood lumber dispute, and explaining how Canada and the U.S. generate policy decisions on softwood lumber trade matters.

Chapter Two: Theoretical Background to Canadian, U.S. Policy and Trade Policy-Making

The primary objective of the softwood lumber sector in Canada and the U.S. is maximizing corporate profits — this does not change. The strategies that policy actors employ to achieve their respective objectives do change, and this is often to reflect changes in the political and economic climate in Canada and the U.S.

Policy Actors and Interests in the Softwood Lumber Dispute

a) Public Interests

The first group of policy actors can be categorized as public interests. These are individuals or groups that do not represent productive interests and act outside of the state. Public interests are often unorganized and passive, but are able to engage in policy-making when they so desire (Hessing & Howlett, 1997, p. 78).

Some of the larger public interest groups involved in the softwood lumber dispute include U.S.- based environmental non-governmental organizations (ENGOS) such as the Sierra Club, the National Wildlife Federation (NWF), Centre for International Environmental Law (CIEL), Natural Resources Defence Council (NRDC), Defenders of Wildlife and the Northwest Ecosystem Alliance (NWF, 2000). These actors educate their members and try to influence public opinion about the environmental repercussions that result from what they consider to be mismanagement of provincial forests. In the most recent chapter of the softwood lumber dispute, Canadian and U.S. environmental groups joined forces with the U.S. softwood lumber industry and, together, advocate for an overhaul of provincial forest management policies and practices (ibid.). For example, NRDC, Defenders of Wildlife, Northwest Ecosystem Alliance and Sierra Club (Canada and the U.S.) submitted an amicus (“friend of the court”) brief to a NAFTA dispute panel reviewing the final affirmative subsidy determination of Commerce (Northwest Ecosystem Alliance, 2002a). Several of these groups also asked the NAFTA environmental

body, the Commission for Environmental Cooperation (CEC), to issue an objective assessment of the environmental implications of the softwood lumber industry (ibid., 2002b). These groups argue that “subsidies to logging wherever they occur in North America are bad for the environment”...and that “inadequate environmental protection is tantamount to a subsidy and requires investigation” (Northwest Ecosystem Alliance, 2002b).

b) Business/Economic Actors

Business/economic interests theoretically operate from outside the state, but their general interest in profit maximization guides government policy-making (Hessing & Howlett, 1997, p. 83). These actors are the producers of raw spruce, pine and fir (hereafter “SPF”), and value-added service industries.

In Canada, there are a number of trade bodies that represent the commercial interests of the softwood lumber sector. The positions of the groups on how best to proceed with this latest chapter of the dispute are not all consistent.

The British Columbia Lumber Trade Council (BCLTC), representing more than 100 lumber companies in B.C. and over 95% of total lumber production in the province, has been open to forestry reform as a possible tool for reaching long-term free trade in softwood lumber between Canada and the U.S (B.C. Lumber Trade Council, 2002). The BCLTC represents the trade interests of the Council of Forestry Industries (COFI), a large business association that is the public voice for many B.C. lumber producers on a range of issues including Aboriginal Affairs, Energy and Environment, Forestry, Markets/Trade, Occupational Health and Safety, Taxation and Transportation (COFI, 2002).²¹

The Quebec Lumber Manufacturers’ Association (QLMA) represents 125 lumber producers in the Province who generate 90% of softwood lumber produced in Quebec (QLMA,

²¹ COFI Member Associations include the Northern Forest Products Association, Interior Lumber Manufacturers’ Association, Coast Forest & Lumber Association, Cariboo Lumber Manufacturers’ Association, Canadian Plywood Association, and B.C. Pulp and Paper Association.

2002). The Association has advocated for a long-term solution to the softwood lumber dispute, and has stressed that resolution must be reached on a provincial basis with the approval of both Quebec and the Canadian Government.

The Ontario Lumber Manufacturers' Association (OLMA) is a trade association that represents independent sawmills in Ontario. The OLMA has a standing committee on softwood lumber that represents the commercial interests of its members by meeting regularly with the Ministry of Natural Resources (OLMA 2002). The Ontario Forest Industries Association (OFIA) represents the bulk of forest industries in the Province, and operates in the same manner as OLMA (OFIA 2002a). In fact, the OLMA and OFIA have been working together as hardliners on the softwood dispute, preferring to allow WTO and NAFTA disputes between Canada and the U.S. to play their course (OFIA, 2002b).

The Alberta Forests Products Association (AFPA) is a non-profit organization that represents 60 Alberta lumber companies and secondary manufacturers. The AFPA advocates for free trade in softwood lumber between Canada and the U.S. and favours a unified approach to take on Commerce and the U.S. lumber coalition (AFPA, 2003).

The Free Trade Lumber Council (FTLC) is an advocacy group established in 1998 to represent the interests of forest product companies and industry associations from Ontario, Quebec, Alberta and B.C. (FTLC, not dated, On-Line). The Council is opposed to any negotiated settlement with the U.S. and believes that the dispute settlement mechanisms in the NAFTA and the WTO are "adequate to deal with any potential problems associated with Canada's softwood exports" (ibid.). The FTLC has made it a top priority to build consensus in the Canadian softwood lumber sector, in order to create a unified front against U.S. pressures for Canadian forestry reform which would put domestic industries in the best position to fight any U.S. trade actions. The Council supports provincial government reviews of stumpage

calculations and raw log export restraints, and advocates the benefits of free trade in lumber to government, U.S. consumers, and other stakeholders (ibid.).

The Canadian Lumber Trade Alliance (CLTA) is comprised of CEOs from forestry firms operating in the provinces of B.C., Alberta, Ontario and Quebec (B.C. Lumber Trade Council, 2002). The Alliance is a lobbying body formed in 2001 by the British Columbia Lumber Trade Council (BCLTC), the Quebec Lumber Manufacturers' Association (QLMA), the Alberta Forest Products Association (AFPA), the Ontario Lumber Manufacturers Association (OLMA), the Ontario Forest Industries Association (OFIA) and the Free Trade Lumber Council (FTLC). The group was established in anticipation of legal challenges that would be launched when the SLA expired, in order to fight for unfettered access to U.S. markets for the softwood lumber of their clients (ibid.).

The Canadian Lumber Re-manufacturers Alliance represents about 300 small firms who produce value-added products from raw softwood lumber. The Alliance is involved in the dispute because their products are also presently subject to U.S. duties. These secondary manufacturers contend that the producers of the raw product should be the sole target and are advocating for the exclusion of this sector from the U.S. trade action (Thomson, Ahern & Co., not dated, On-Line).

The Forest Products Association of Canada (FPAC) consists of the CEOs of the major North American forest product companies including, but not limited to, Canfor Corporation, Louisiana-Pacific (Canada), and Weyerhaeuser. The Association is mainly involved in a major communications effort to obtain the support of U.S. consumers, homebuilders, homeowners, lumber retailers and others in the U.S. that support free trade in softwood lumber. FPAC advocates for a long-term solution to the dispute that would allow their members to trade softwood lumber freely from Canada to the U.S. (FPAC, 2002a).

The U.S.-Canada Partnership for Growth is a grassroots campaign established by a federation of individuals and organizations from Canada and the U.S. to raise awareness as to how U.S. duties could damage the U.S. economy, and strain Canada-U.S. relations. The Partnership, established November 2002, is chaired by former senator (R-TN)/former United States Trade Representative (USTR) William Brock, and James Blanchard, former governor (D-MI)/former U.S. Ambassador to Canada (U.S.-Canada Partnership for Growth, 2002). The Partnership believes that the U.S. duties do not protect U.S. jobs, and has promoted Congressional action against the duties by supporting various bills in the U.S. House of Representatives and Senate. FPAC contributes funding to the Partnership (*ibid.*, document b).

In the U.S., the Coalition for Fair Lumber Imports (CFLI) is an alliance of large and independent saw mills, hundreds of thousands of mill employees, tens of thousands of woodland owners. The CFLI opposes provincial forest management policies and practices that allegedly “subsidize” softwood lumber production, and advocates for free competition for lumber (Coalition Fair Lumber Imports, 2002). The Coalition has supported each trade action against Canadian softwood lumber and initiated all legal actions against Canadian softwood lumber imports, except the third case, which was initiated by Commerce itself. Weyerhaeuser and Louisiana-Pacific, two of the biggest U.S. forest corporations, had for years been members of the CFLI. Interestingly enough, in recent years both firms withdrew from the coalition because they now harvest more softwood lumber in Canada than they do in the U.S. (Warnock, 2001, p. 36). Theoretically, these corporate retreats could have threatened the legitimacy of the CFLI, if not had the impact of restricting the Coalition’s ability to mobilize U.S. support in its most recent case. However, given the affirmative findings in the most recent case, the CFLI has been successful in averting this potential problem.

It should be clear from the discussion that there are significant divisions between the forestry trade associations on how best to represent their members into the future. While the

BCLTC appears open to the possibility of some forestry reform, the QLMA seems to be looking for province-specific deals approved by Ottawa. Ontario and Alberta oppose reforms and negotiated settlements altogether and favour NAFTA and WTO dispute settlement.

However, through the CLTA, many of these associations (and their member constituents) advocate for a unified, hard-line approach, which downplays the option of a negotiated settlement. This inconsistency is likely the product of anxiety amongst domestic producers — all want unfettered access to the U.S., but will otherwise entertain an option that best suits their membership. FPAC is advocating the same position as the CLTA in the present dispute, but because of its history wants to distance itself from the CLTA politically.

In the U.S., most softwood lumber producers are represented by the CFLI, which has indicated it will continue to fight an overhaul of provincial forestry practices.

c) Government Actors

All levels of Government in Canada and the U.S. hold significant stakes in facilitating a positive economic climate in their jurisdictions. This is the case for two main reasons:

First, a productive sector generally brings greater revenue to government coffers (Hessing & Howlett, 1997, p. 83). In Canada, the provinces, as landowners, collect economic rents for the extraction of softwood resources including spruce, pine and fir (SPF). In the U.S., state and federal governments generate revenue from the auctioning off of their forests, although the majority of production is from private plots. Municipalities in which production is located also stand to gain from corporate and personal tax revenues. Governments use these revenues to support things like infrastructure and social programs, and most attempt to maintain fiscal responsibility in the process.

Second, governments act to ensure the socio-economic interests of the electoral base are met. When governments are unable to foster sufficient opportunities for work, or are perceived to have failed in this respect, they risk losing voter support. This is particularly the case in many

small British Columbian towns where softwood lumber and affiliated industries support the local economy.

At this point in the discussion, it is still unclear how trade policies are made in Canada and the U.S. The following section identifies those institutions responsible for trade-policy development in Canada and the U.S., examines the process by which trade policy decisions are made and documents the laws upon which trade policy decisions are based. In addressing these considerations, each country analysis explains how trade policies are made concerning softwood lumber.

Trade Policy-Making in Canada

In Canada, the Department of Foreign Affairs and International Trade (DFAIT) is responsible for crafting policies concerning international trade and policy matters. The Minister advances Canada's trade policy positions with its trading partners and is often assisted by Ambassadors or other high-level officials on issues where the political and/or economic stakes are high. These representatives are appointed by a Cabinet comprised of members of the political party in power.

Despite the democratic nature of the domestic political system, "much of the serious conflict and hard bargaining over public policy issues in Canada is hidden from public view" (Stanbury, 1993, p. 63). Indeed, the debate over major policy issues generally occurs within the executive and between various government departments and agencies. Stakeholders have some opportunity to influence policy decisions of the bureaucracy, yet this is generally limited to the initial period when Cabinet considers a proposed policy (ibid., 1993, p. 64). This is because Cabinet is generally concerned that backing off approved policies may make parliament second-guess subsequent policy decisions. The process by which stakeholders attempt to influence Cabinet policy-making is further complicated by the fact that decision-making authority lies at

the Ministerial and Cabinet levels. The government tends to hold closed meetings in order to minimize opportunities for the political opposition (Stanbury, 1993, p. 63).

Cabinet policies are formulated on a number of levels. New policy initiatives are discussed at a fairly senior level between the departments and agencies that hold stakes in the initiative (ibid., p. 64). These consultations provide an opportunity for the various departments to present the interests of their respective clients; discuss whether the initiative is in line with existing government policies; debate about roles, policy responsibilities, how their financial resources will be allocated; and to coordinate efforts on the initiative (Stanbury, 1993, p. 65).

Major policy initiatives also go through a cabinet “subject matter” committee where ministers themselves debate over similar issues including jurisdiction and resource allocation (ibid.). For each subject matter committee created, a parallel committee is created for the deputy ministers of the respective departments and agencies. This committee meets before the subject matter committee and serves as an opportunity for the deputies to brief their ministers and assess the political climate and issues surrounding the policy initiative (ibid.). The subject matter committee will then approve of the initiative or send it back to deputies and their staff for redrafting. Once approved, the policy moves to the Cabinet Committee on Priorities and Planning (P&P) which has the final say on how the policy will be dealt with (ibid.).

On another level, the department that is seeking to take the lead on a particular policy initiative will generally have intra-departmental consultations among those civil servants with expertise on the subject matter (ibid.).

Canadian antidumping and countervailing duty legislation and procedures are embedded in the Special Import Measures Act (SIMA) (Fox, 1991, p. 30). The revised Act, which came into force April 15, 2000, allocates to the Commissioner of the Canada Customs and Revenue Agency (CCRA) the responsibility for receiving and reviewing initial requests for the imposition of CV or AD duties to protect domestic industries (Department of Justice, On-Line). If the

Commissioner finds merit to the claim in its initial review, the Canadian International Trade Tribunal (CITT) opens its own investigation. The CITT completes its review only after the Commissioner has issued its final determination (ibid., p. 31). This means that if the Commissioner does not issue a final affirmative determination on the merits of a claim, the CITT does not issue a final determination, and no trade remedies may be imposed. In order to find affirmatively, the CITT must find that the import under investigation has caused, is causing, or threatens to cause material injury to domestic producers or is slowing the establishment of domestic industries, or that the alleged dumping or subsidization would have injured or slowed the establishment of domestic industries (Fox, 1991, p. 31). In Canada, there is little evidence that suggests that the CCRA-CITT process is at all politically motivated. This argument is partly supported by the fact that politicians are not entitled to participate as witnesses in these reviews (Skogstad, 1988, p. 560; Fox, 1991, p. 31).

Canadian Actors and Softwood Lumber Trade Policy

Despite the fact that there are such significant economic and political stakes in the softwood lumber dispute, Canada's trade policy-making process is informed by a fairly small number of actors.

DFAIT meets with major industrial interests who hold the greatest stakes in the softwood lumber dispute – mainly the associations that represent the commercial interests of softwood lumber industries in B.C., Quebec, Ontario and Alberta. The Department focuses on these interests because of the magnitude of their economic stakes, primarily because what is good for commercial interests is generally considered good politics (Mayer, 1998, p. 147). There is no evidence that suggests that certain trade associations enjoy greater access to or exert a higher degree of influence over DFAIT trade policy. Given that the provinces have assumed a significant involvement in the dispute, DFAIT has lessened its domestic-level interactions by looking to the provinces for direction.

The provinces provide support to their commercial softwood interests through regular consultations with Ottawa (DFAIT reference c). B.C., Alberta, Ontario and Quebec have also met separately with the U.S. at various points in the dispute. However, given that trade negotiations fall under federal jurisdiction in Canada, there are arguably some limits to what these consultations can achieve. Provincial direction to DFAIT has, in large part, been informed by the provincial lumber trade associations identified earlier. This has worked fairly well for the provinces; in absence of such strong representation, they would have to devote more significant resources to protect the industry.

Canadian softwood lumber producers and their representatives have been wise enough not to restrict themselves to federal and provincial consultations in the disputes. Acknowledging that there are limits to what Ottawa or the provinces might ever be able to achieve in securing access to the U.S. market, the domestic softwood lumber industry also lobbies south of the border. This is because Canadian producers recognize that the best way of changing U.S. trade policy may actually be from within. This will, at times, involve testifying before Congress, the ITC or Commerce when requested to do so (Fox, 1991b, p. 32).

To date, there have been a small number of Canadian environmental non-governmental organizations (ENGOS) involved in the softwood lumber dispute. These groups have had marginal opportunity to feed ongoing provincial and federal level trade policy and have bolstered their effectiveness by concerting efforts with U.S. groups who have access to greater resources. It is difficult to assess the relative importance of ENGOS as actors in the softwood lumber dispute. However, given that Ottawa is still apprehensive about the possibility of forestry reform, the main policy objective of these groups has not yet been met.²²

²² Then again, it does not appear as if this chapter of the dispute has come to an end – punitive damages caused by the U.S. duties could still lead to reform.

Trade Policy-Making in the U.S.

There are three types of institutions involved in U.S. trade policy-making: the U.S. Trade Representative (USTR), Congress, Commerce (i.e. the International Trade Administration-ITA), and the International Trade Commission (ITC).

The United States Trade Representative (USTR) is the lead agency responsible for orchestrating the trade-related political and foreign policy needs of the Administration. The USTR performs these complicated and sensitive tasks through consultations with other government agencies, congressional committees, official trade advisors, lobbyists and sectoral advisory groups.²³ The overall goal of this complex consultative process is to advance one government position on a given trade policy matter (Castillio & Vega-Cánovas, 1995, p. 27). Importantly, the USTR is also responsible for representing the commercial interests of U.S. industry internationally. As a result, the USTR often advocates trade policy matters that are in consistent with major corporate interests.

The House of Representatives (hereafter the “House”), and the Senate, are the two main legislative divisions of the U.S. Congress. Each retains numerous committees and sub-committees which specialize in a range of disciplines. On trade matters, it is primarily the House Ways and Means Sub-Committee on Trade, and the Senate Finance Committee that are involved. Business and public interest groups request, or are invited to participate in hearings, where they attempt to persuade Congress to adopt their policy positions.

There are two main U.S. trade bodies whose investigative reviews determine whether certain imports will be subject to trade remedies such as countervailing and anti-dumping duties. The ITA, headed by the Under Secretary for International Trade, protects domestic firms from dumped or subsidized imports by enforcing U.S. trade laws, and helps domestic industries

²³ The USTR invites select corporate interests to participate in sectoral advisory groups to help inform its position. Private interests may otherwise transmit their positions through sectoral representatives posted at the USTR (Castillio & Vega-Cánovas 1995: 26).

develop their markets abroad (U.S. ITA, not dated, On-Line). The ITC is a non-partisan federal agency that determines whether imports are causing, or threaten to cause material injury to U.S. (competing) industries. The Commission is comprised of six individuals who are appointed by the President, may contain no more than three individuals from the same political party, and must operate independently of Congress and the President (Fox, 1991, p. 18). Most appointees to the ITC have had work experience with Congress or are from the private sector (Baldwin, 1985, p. 113; Fox, 1991, p. 22).

In the case of softwood lumber, the ITA and ITC have conducted their investigations with respect to U.S. subsidy and antidumping laws (Fox, 1991, pp. 19, 26). These laws are amended, as necessary, to conform to new commitments reached in GATT-WTO or other trade negotiations.²⁴

U.S. subsidy investigations have been conducted since the enactment of the first U.S. CVD law in 1897. In 1979, the U.S. passed the Trade Agreements Act (TAA) to bring U.S. law in compliance with the Tokyo Round GATT negotiations. One of the main accomplishments of these negotiations was this additional, binding, commitment among Members to prove that “subsidized” imports were also injuring domestic industries in trade disputes such as that concerning softwood lumber (*ibid.*, IV-6). Under the GATT-WTO 1994 Uruguay Round Act, all WTO members are now subject to the aforementioned rules, which are contained in the Subsidies Code. The U.S. law implementing the Uruguay Round negotiations, the Uruguay Round Agreements Act (1995), introduced mandatory “sunset reviews” that determine whether a CVD order should be removed after five years (*ibid.*, IV-7).

²⁴ U.S. laws also permit safeguard/escape clause actions that protect U.S. industry by imposing import constraints if it is found that actual/relative imports in a given sector are causing or threaten cause serious injury to U.S. competitors. Safeguard actions are used less frequently than CVD and AD actions because (1) the President can strike down/lessen relief recommended by the ITC, but cannot do so with CVD or AD actions, and (2) they can only be imposed temporarily, whereas CVD and AD duties can be imposed for up to five years.

U.S. dumping legislation has its roots in the Antidumping Act of 1916 (*ibid.*, IV-3). This Act was amended in 1921 and became the statutory basis for the investigations of the Department of the Treasury until 1979. The principles contained in the Antidumping Act also became the model for GATT Article VI antidumping laws, which established the GATT Antidumping Code in 1967. The Tokyo Round subsequently refined Article VI so it would conform with the new Agreement Relating to Subsidies and Countervailing Measures (*ibid.*, IV-3). In implementing the Tokyo Round negotiations, the U.S. Trade Agreements Act of 1979 repealed the Tariff Act of 1921 and transferred the authority for antidumping investigations from the Treasury to Commerce (i.e. ITA). Uruguay Round negotiations bound all Members to the terms of earlier GATT agreements, and to an agreement to implement Article VI of GATT 1994 (*ibid.*, IV-4). The U.S. Uruguay Round Agreements Act broadened the scope of material injury findings to include the “threat” of injury in trade disputes. The Act also requires sunset reviews for antidumping orders (*ibid.*, IV-5).

Commerce directs U.S. Customs to collect duties on imported goods/services when: (1) the ITA finds that imports have been subsidized or dumped in U.S. markets below production cost, and (2) the International Trade Commission (ITC) finds that those imports are causing, or threaten to materially injure domestic industries.²⁵ The ITA and ITC both produce preliminary and final determinations in the cases they investigate, unless petitions are in the process dropped. Their decisions do not have to be released in any particular order.

The U.S. trade remedy system benefits industry and the Administration for three main reasons. First, the preliminary affirmative findings can be used to pressure foreign governments to negotiate a settlement to a dispute prior to a final determination. In cases where foreign industries feel that they may lose the final determination, they may seek a negotiated settlement,

²⁵ Since 1982, there have been three rounds of CVD investigations, plus the current combined round which involves both CVD and AD investigations.

rather than paying potentially higher costs from an affirmative determination. At the same time, negotiations often result in some protection for domestic industries. Negotiations also help the U.S. appear less protectionist than would be the case if the dispute was settled solely by ITA and the ITC. Second, under certain circumstances, preliminary affirmative determinations allow Commerce to impose interim trade remedies while a more thorough investigation takes place. For example, if the ITA preliminarily finds subsidies, U.S. competitors may receive immediate protection from imports through the imposition of import taxes, levies, or other bonding requirements. Third, the U.S. system imposes no limitations on the number of investigations that may be directed at any given import and presently channels duties collected to affected U.S. industries. The latter is the product of a recent initiative by Senator Robert Byrd (D-W.Va) that led to the passage of the (U.S.) Continued Dumping and Subsidy Offset Act of 2000 (DFAIT, not dated, On-Line d). The law, known as the “Byrd Amendment”, was challenged recently by 11 WTO Members, who argued that it is inconsistent with the WTO Antidumping Agreement, and the Subsidies and Countervailing Measures (SCM) Agreement. In July 2002, the WTO upheld the challenge by finding the Byrd Amendment in violation of both WTO Agreements. The Panel was also clear in its conviction the only way that the U.S. could conform to its decision would be to repeal the relevant measure/amendments from its domestic Continued Dumping and Subsidy Offset Act. The WTO is generally quite reluctant to issue such strong determinations, so as not to infringe upon the sovereign right of states to regulate (ibid.).

The ITA and ITC begin their work on matters including, but certainly not limited to softwood lumber, when directed to do so by USTR. USTR receives requests for alleged unfair trading practice investigations from individual Members of Congress, who have been approached by their constituents and/or from the Senate Finance Committee and the House Ways and Means Committee.

The full House and Senate pass their own legislation to adopt major policy initiatives such as trade agreements. Together they must subsequently work out any legislative differences that exist, through a process called “Conference” before for the initiative becomes law.

U.S. Actors and Softwood Lumber Trade Policy

The USTR has fostered a more open process for advising its trade policy position on softwood lumber than has been the case with DFAIT. This has involved regular consultations with its sector advisors, ongoing inter-departmental and inter-agency discussions, and invitation of public comments through Federal Registers.²⁶

Congress is ultimately responsible for shaping U.S. trade policy because the Constitution requires it to approve of any trade deals that the USTR strikes (Fox & Uhler, 1991, p. 9). The USTR also recognizes that there is little sense in advancing a particular policy in talks with Canada if there is insufficient appetite for that policy in Congress. For this reason, U.S. softwood producers invest significant resources lobbying Members of Congress. These efforts help set the Congressional agenda, which, in turn, influences trade-policy. Public interest groups employ similar tactics.

Summary

This chapter established the context in which this analysis will take place, by identifying those parties which hold stakes in the softwood lumber dispute and explaining how Canada and the U.S. generate policy decisions on softwood lumber trade matters.

The discussion has identified three groups that are, in theory, capable of engaging in trade policy-making: public interests, business/economic interests and government. This thesis will now document what happened in each of the disputes and report on the state of the fixed set of indicators.

²⁶ Federal Registers are open requests for comments on policy matters. All comments are filed together and available to the public.

Chapter Three: The First Countervailing Duty Case (CVD 1)

Part I: What Happened

Competition over Forest Service timber in the U.S. Pacific Northwest in 1977 resulted in intense bidding between timber companies. This significantly drove up timber prices in the region (Doran, 1987, p. 3). In October of 1979, the United States Federal Reserve Board implemented a “restrictive monetary policy” in order to curb inflation (Apsey & Thomas, 1997, p. 5). This monetary policy brought on considerable interest rate hikes, which caused a slowdown in the U.S. housing industry. For example, domestic U.S. consumption of softwood lumber dropped from 38.9 billion board feet in 1979, to 29.8 billion board feet in 1981 (ITC, 1982, p. 6; Jansen, 1984, p.10). The slowdown generated significant financial difficulties for timber companies that had entered into fixed harvesting contracts that imposed sizeable penalties for non-compliance.

In 1982, a group of lumber mills in the U.S. Pacific Northwest organized as the Northwest Independent Forest Manufacturers (NIFM) and claimed that, aside from the decline in demand for lumber from the residential construction slowdown, Canadian softwood imports were the greatest source of unemployment in the Pacific Northwest (Apsey & Thomas, 1997, p. 5). At the same time, NIFM noted that depreciation in the value of the Canadian dollar was giving Canadian exports a significant advantage in the U.S. marketplace (U.S., 1981; Thomas & Apsey, 1997, p. 6). NIFM sought to advance a trade policy that would enable U.S. softwood lumber producers to better compete with imports from Canada, and began to present its case to Congress.

Senator Robert Packwood of Oregon then took action by requesting that the Senate Finance Committee investigate the competitive conditions of the trade based on s.332 of the *United*

States Tariff Act of 1930 (Apsey & Thomas, 1997, p. 6). These particular investigations are requested on behalf of industry, to gather evidence on a trade dispute, at the expense of government.

In response to this request, the Senate Finance Committee instructed the ITC to prepare a report on the competitive conditions of the bilateral softwood trade. The product was an ITC research report that helped NIFM and its allies in Congress, research, evaluate and rank policy options.

NIFM viewed the Committee's report as providing sufficient evidence for justifying an official trade complaint against softwood lumber (Gastle & Castle, 1996, 839; U.S. Senate, 1993, p. 35-36). On the other hand, Cashore (1998) argues that the report "fell short of claiming Canadian provinces subsidized their timber industry."

NIFM then strengthened its member support base by joining with business interests outside of the Pacific Northwest. The product of this initiative was the establishment of the United States Coalition for Fair Canadian Lumber Imports (CFCLI). The Coalition encouraged members of Congress, particularly those from states that had stakes in the softwood lumber trade, to promote trade action against Canada (Cashore, 1997, p. 11).

On October 7, 1982, the Coalition filed a CVD petition with Commerce on the grounds that the provinces were subsidizing Canadian softwood production by setting stumpage fees too low. In other words, Commerce was given the mandate to determine whether or not Canadian softwood lumber imports were subsidized.

In May of 1983, the ITA determined that the provinces were not "subsidizing" softwood exports (Cashore, 1997, p. 11) and that stumpage programs in the Canadian forest sector were

comparable to stumpage-type programs across all natural resource sectors in Canada. The ITA also noted that stumpage rates applied to the inter-provincial trade in softwood lumber were the same as those for exports (Thomas & Apsey, 1997, 10).

The investigation revealed that it is difficult, if not impossible, to compare Canadian stumpage programs to those in the U.S. The ITA explained that while there may be a “unified” market for softwood lumber in North America, there is no unified system for calculating stumpage. The ITA continued that stumpage must be calculated based on a number of factors including composition of species, density, quality, size, age, accessibility, terrain and climate (ibid., p. 11; U.S. ITA, 1983). The ITA added that “even if one believes that there is a rational basis for comparing U.S. and Canadian stumpage prices...Canadian prices for standing timber do not vary significantly from U.S. prices” (Apsey & Thomas, 1997, p. 10; U.S. Federal Register, 1983).

Failure of the U.S. softwood coalition to secure an affirmative subsidy finding meant it was business as usual for Canadian softwood lumber exporters. The U.S. Government, itself, ruled that it could not fulfil the request of U.S. firms to impose duties on softwood lumber imports from Canada. The negative determination fuelled the determination of U.S. softwood lumber producers to continue their fight against stiff competition from Canada. Congress redefined the problem that remained for U.S. softwood lumber producers, and given the earlier no-subsidies finding, opted to shift its focus towards consideration of the prohibitive contractual obligations that U.S. firms faced.

Congress implemented its desired course of action by passing the *Federal Timber Contract Payment Modification Act* (1984), in order “to allow contract purchasers of Federal Timber to be

relieved of the obligation to purchase up to 55% of the volume of timber for which they contracted before January 1, 1982, if they still held the contract.”²⁷ Without such legislation, “many small and medium-sized firms would be forced in bankruptcy...workers will lose their jobs...all to prove an abstract principle that a contract is a contract.”²⁸ In other words, Congress argued that in absence of this Act, there would be significant economic consequences for several firms and their workers, only to prove the importance of upholding contractual commitments.

Congress was reluctant to admit that the *Federal Timber Contract Payment Modification Act* was passed for the purpose of bailing-out some producers in the Pacific Northwest from a financial crisis that may have led them to declare bankruptcy. The Senate argued that,

This is not a timber bailout. The mills will pay a buy-out charge...The Federal Government gets the timber back and it can be resold at a later date.²⁹

The Senate did not publicly question whether the U.S. bidding system might have in some part been responsible for the financial predicament that U.S. producers were facing at the time. This would detract from the interests of their constituents, who were trying to make the case that Canadian imports were the source of their problems. At the same time, these Members of Congress must have questioned the logic behind a forest management system that could drive U.S. softwood lumber producers into such a predicament.

²⁷ Each contract purchaser was allowed to be relieved of a maximum of 200 million board feet of timber that they would otherwise be responsible for purchasing from government.

²⁸ Congressional discussion leading to the passage of the *Federal Timber Contract Payment Modification Act* (1984). Available at: <http://www.senate.gov>

²⁹ Senate Record Vote No. 252 Analysis. Available in text of *Federal Timber Contract Payment Modification Act*.

Part II: The Political and Economic Conditions for the Period of CVD 1 — The Indicators

(a) Market Share

Given that this was the first formal CVD case, there are no other disputes to use as the baseline for comparing Canadian softwood lumber producers' share of the U.S. market in the year CVD 1 was launched (1982). Market Share data is further limited, given that data is only available from 1979 forward. The available data does, however, provide some sense of how Canadian firms were performing in the U.S. when the dispute was launched. Canadian producers held 27% of the U.S. market in 1979, and 29% in 1982 (B.C. Ministry of Forests, 2001). In other words, when CVD 1 was launched, Canadian softwood lumber producers held a slightly larger share of the U.S. market than was the case a few years earlier. This was a large relative gain for Canadian softwood exporters over a short period, but -0.8 deviations from mean Canadian market share when looking at the full period of this thesis (1972-2002). U.S. softwood lumber producers held 71% of the U.S. market in 1982. Data on U.S. producers' share of the U.S. softwood market is incomplete prior to this date.

(b) State of U.S. Economy

The first countervailing duty investigation (CVD 1) was launched at the beginning of one of the worst recessions ever to hit the U.S. and Canadian economies.³⁰ In an economic downturn, industries are typically producing less, and fewer inputs (e.g. softwood lumber) are generally required. This, of course, is a general rule of thumb, because not all sectors face the same fluctuations in economic activity during a recession.

³⁰ Canada and the U.S. were not the only countries hard hit, but because the world's economies were not nearly as integrated in the early 1980s as they are today, economic downturns in one area did not necessarily have a significant impact on all other economies.

In 1982, U.S. Gross Domestic Product (GDP) was \$4.92 trillion — a slight contraction from \$5.02 trillion in the previous year.³¹ This was the only year-to-year GDP contraction in GDP in the U.S. in the 1980s.

Unemployment in the U.S. “lumber and wood products” sector was 17.2% in the year that the U.S. initiated CVD 1 in 1982 (BLS, 2003).³² This was more than double the average 8.1% annual unemployment rate in this sector from 1976-2002.³³ Overall unemployment in the U.S. civilian workforce was 9.7% when the U.S. launched CVD 1 (BLS, 2001). This was significantly higher than the 6.4% average rate of unemployment from 1976-2002.

The data has shown that when CVD 1 was launched in 1982, GDP had contracted since the previous year, unemployment in the lumber sector was extremely high, and overall unemployment in the civilian workforce was also high.

(c) Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade to Which the U.S. Had Significant Stakes

The U.S. was not involved in any major trade negotiations at the time when CVD 1 was launched. The Canada-U.S. Free Trade Agreement (FTA) may have been an incubating idea at the time, but this would not have had any significant influence on the outcome of this CVD case. The U.S. did have significant concerns about Prime Minister Trudeau’s National Energy Plan (hereafter “NEP”), which was proposed in 1980 — around the time of the first CVD case. The NEP would nationalize the Canadian energy sector by reversing foreign ownership in Canada’s oil and gas industries. However, this threat was eliminated when Ottawa dropped the NEP in

³¹ All figures in chained 1996 US dollars in order to adjust the figures to reflect inflation rates.

³² Includes manufacturing of durable lumber & wood products (excluding furniture) including: logging; sawmills, planing mills, & millwork; wood buildings and mobile homes; miscellaneous wood products. U.S. Bureau of Labor Statistics Data (BLS) on percentage of unemployed wage & salary workers, self-employed workers, family-owned workers (work 15+ unpaid hours – there are very few of these) by detailed industry.

³³ 1976 is the earliest date on record at the U.S. Department of Labor for “Unemployment in the lumber & wood products sector”. For this reason, the same period (1976-2002) is used to examine overall unemployment in the civilian workforce.

1982, in response to a sharp drop in world oil prices that made the plan unprofitable (Bothwell, 1992, p. 132).

(d) Level of Protectionist Sentiment in the U.S.

In 1982, the U.S. initiated a total of 95 CVD and AD cases (60 CVD, 35 AD), which is 43 cases more than the average 52 cases initiated annually from 1972-2002. Given a standard deviation of 28.7 for this first data set, this equates to +1.5 standard deviations, or “very high” in the qualitative scale employed in this thesis. Given that the U.S. economy was enduring its worst recession since the 1950s, it should come as no surprise that the U.S. initiated so many CVD and AD cases that year (ibid.). Congress and the Reagan Administration were under tremendous pressure from powerful U.S. lobby groups, to better protect U.S. industries against foreign competition (Apsey & Thomas, 1997, p. 6).

In that same year, 6 GATT cases were initiated against the U.S. This is slightly higher than the mean 5.5 cases launched from 1972-2002. Given a standard deviation of 4.5 for this second data set, this is +0.1 deviations from the mean and an “average” number of GATT cases initiated against the U.S.

Equally weighted, the CVD-AD and GATT/WTO quantitative measures yield a “high” level of protectionist sentiment in the U.S. at the time when CVD 1 was initiated.

Summary

In 1982, Commerce conducted its first formal CVD investigation on whether softwood lumber from Canada was subsidized. To the consternation of U.S. softwood lumber producers, the outcome was a “no subsidies” determination. This prompted Congress to bring ailing U.S. softwood lumbers an alternate form of economic relief through passage of the *Timber Contract Payment Modification Act*.

The assertiveness of the Coalition in this first dispute built a significant degree of influence in U.S. softwood lumber politics. This made it highly unlikely that the U.S. would, in

the future, make any significant policy decisions on softwood lumber, without first engaging in extensive consultations with the Coalition. This empowered the Coalition to direct U.S. policy-making on softwood lumber into the future.

The indicators have shown that when CVD 1 was launched, Canadian softwood lumber producers held a larger share of the U.S. market than in 1979 (the earliest date for which data is available). The U.S. economy was experiencing significant difficulties, as evident from the fact that GDP had contracted from the previous year, unemployment in the lumber sector was sky-high, and overall unemployment in the civilian workforce was also high. There were no major trade negotiations looming at the time when CVD 1 was launched. The U.S. did have concerns about the Canadian NEP. However, Canada dropped the NEP around the time that CVD 1 was launched. The U.S. initiated a “very high” number of CVD and AD cases against other GATT countries that year. An “average” number of GATT cases were launched against the U.S. Taken together, these two measures indicate that there was a “high” level of protectionist sentiment in the U.S. in 1982.

Chapter Four: Hopes for Free Trade, Fast-Track Authority, and the Second CVD Case

Part I: What Happened

The fight against Canadian softwood lumber, by producers in the Pacific Northwest, did not end with Commerce's initial finding of no subsidies in the first CVD investigation (CVD 1), nor with passage of the *Federal Timber Contract Payment Modification Act* (1984). The U.S. Coalition recognized that it had the option of dropping its case against Canadian softwood lumber imports, or continuing to seek protection from these imports. The Act had provided some contractual relief for several U.S. producers in 1984, but no action had been taken to help U.S. producers better compete with Canadian softwood lumber imports in the future. The initial effort of the Coalition and Congress (CVD 1) failed to achieve this objective and the Coalition knew it had the right under U.S. law to pursue a new CVD case.

The Coalition opted to draw "fast-track" negotiating authority for pending Canada-U.S. Free Trade Agreement (FTA) negotiations into the equation; a strategy it hoped would create renewed support for its case against provincial forestry practices, and its adverse effect on U.S. competitive conditions.

Fast-track (recently termed "Trade Promotional Authority") provides the U.S. Administration with the authority to negotiate trade agreements and deliberately restricts Congressional involvement in negotiations, by asking Congress to either approve or reject deals negotiated by the Executive Branch. Without fast-track authority, countries are often reluctant to enter into serious trade negotiations with the U.S. This is because they know that even if they are able to reach agreement with U.S. negotiators, U.S. Congress may otherwise place conditions on, or veto the deal.³⁴

³⁴ When a trade agreement comes to Congress, it is the House Ways and Means Committee and Senate Finance Committee that decide whether to "mark-up" proposed legislation and send it to the full House and Senate floors, or to send it down to the subcommittee level for further discussions and mark-up. If the full House and Senate pass an identical bill, the bill becomes law. However, if the text of a bill which passes the House is different from that

Fast-track was an issue in the mid-late 1980s because Congress was considering whether or not to grant the Administration negotiating authority for free trade negotiations with Canada. U.S. softwood lumber producers used this opportunity to put significant pressure on the Administration to resolve outstanding matters. If Congress were to reject the Administration's request for fast-track authority, this could have slowed or blocked negotiations of the FTA.

Opinions are divided on whether the outstanding softwood lumber dispute had an impact on Congress' decision to grant the Administration fast-track authority for free trade negotiations with Canada. According to Michael Hart (1999), "the looming softwood lumber issue did not have a significant influence on fast-track approval. In fact, the Senate Finance Committee realized later on that they hadn't thought this decision through very well." Hart suggests that while the Committee could have used its authority to grant fast-track authorization to pressure the Administration to take action on behalf of U.S. softwood producers, it never took advantage of this opportunity.

Yet, the U.S. Administration must have come under some pressure from Congress to settle the softwood lumber dispute before entering into serious talks regarding the Canada-U.S. Free Trade Agreement. According to Cashore (1997), the USTR, Clayton Yeutter, felt this weight from the Senate Finance Committee and other Members of Congress who believed that the alleged use of subsidies in the Canadian forestry sector would not provide a good standard for free trade. Cashore (1997) backs this claim by referring to a letter written to by 10 (unnamed) Members of the Senate Finance Committee, October 1, 1985, to the attention of Clayton Yeutter:

Any free trade agreement must be built on a foundation of mutually advantageous trade practices. Therefore, we believe the Administration should seek an early resolution of the softwood lumber trade issues. This would facilitate Finance Committee consideration of any Administrative proposals relating to the negotiation of a free trade agreement with Canada (Cashore, 1997, p. 12).

which passes the Senate, the two acts go to "Conference" where representatives from each house try and work out a mutually acceptable piece of legislation. Both the Senate and House must then approve of this compromise.

Technically, the Senate Finance Committee could have obstructed free trade talks by using its authority to reject fast-track authorization. It was therefore in Yeutter's best interest to resolve the softwood issue, in order to ensure that he received the negotiating authority the Administration required for negotiations.

Senate Finance Member, David Pryor, received a hand-written letter from Yeutter on April 17, 1986, urging him to vote for fast-track. Yeutter promised, "We'll get timber fixed."³⁵ Shortly after receiving this assurance, on April 23, 1986, the Senate Finance Committee granted fast-track approval for the Canada-U.S. free trade negotiations (Thomas & Apsey, 1997, p. 17). This move implemented the Coalition's decision to condition Congressional support for fast-track on USTR support for a new case against Canadian softwood lumber.

Whether or not the Senate Finance Committee would actually have rejected fast-track authorization without a promise from the USTR to fix the softwood issue is difficult to determine in hindsight. The U.S. still had significant economic interests in securing a Canada-U.S. Free Trade Agreement.

A couple of weeks after fast-track negotiating authority was issued, the Coalition for Fair Canadian Lumber Imports (CFCLI) dropped its anti-Canadian image by changing its name to the Coalition for Fair Lumber Imports (CFLI). The CFLI then requested a new CVD investigation on May 19, 1986 (Apsey & Thomas, 1997, p. 19). The Coalition was confident that changes made to U.S. trade laws would favour an affirmative determination in any new softwood investigation.

³⁵ This letter was made available to Counsel for the Canadian industry through a U.S. Freedom of Information Act (FOIA) request.

Congress had amended the *Tariff Act of 1930* in 1984 to include “upstream” or “input product” subsidies as countervailable where “the input product bestows a competitive benefit on those goods by affecting significantly the cost of production” (Cashore, 1997, p. 10).

The new law extended the definition of subsidies so that low stumpage rates would not be the only measure upon which Commerce could base its investigation. For example, Commerce could also find affirmatively if it found that the cost of processing raw logs into softwood lumber was subsidized. The Coalition believed that this amendment would help it win any successive subsidy investigations (Cashore, 1997, p. 10).

Canada requested consultations under the General Agreement on Tariffs and Trade (GATT) on June 17, 1986, in order to protest the initiation of the second CVD investigation. It argued that nothing had changed from the final negative determination in the first CVD investigation and that bringing up the case again was clear trade harassment. When initial mandatory consultations between Canada and the U.S. failed to resolve the matter, Canada requested the appointment of a review panel, as permitted under the 1979 GATT Subsidies Code (Apsey & Thomas, 1997, p. 20). Shortly thereafter, on June 27, 1986, the ITC issued its preliminary determination that subsidies were causing “material injury” to U.S. producers (Cashore, 1997, p. 11; Ragosta, 2000).

Canada’s position may have deteriorated when then B.C. Premier, Bill Vander Zalm, and his Minister of Forests, Jack Kempf, indicated that they would have to address the problem of stumpage rates being too low (Apsey & Thomas, 1999, p. 21). Vander Zalm’s behaviour can be explained by the fact that the B.C. forest industry was booming in 1986, while the Province faced a \$1 billion deficit (Cashore, 1997, p. 14). With higher stumpage rates, the Premier would be able to channel a greater portion of softwood revenues into B.C. provincial coffers. Kempf’s

comment that “we’re not getting a good return from the industry” was subsequently repudiated, yet the statement would nevertheless weaken Canada’s case that a second CVD case was unwarranted (ibid., p. 21). Canadian Trade Minister Pat Carney recognized this and at the urging of B.C. and Quebec, tabled a non-negotiable offer to the U.S. September 30, 1986. Major exporting provinces would voluntarily increase the stumpage they charged softwood producers by 10%, which would help U.S. softwood producers better compete in their own market (ibid.). The U.S. Executive Branch rejected the Canadian offer after Congress expressed its opposition.

The ITA released its preliminary finding for CVD 2 on October 16, 1986. Commerce reversed its (final) determination from CVD 1 and found that provincial stumpage rates benefited pulp and paper, wood products and logging industries. The level of subsidization was estimated at 15%.

It does seem odd that the ITA completely reversed its determination to a preliminary affirmative determination of subsidies in CVD 2. This is the case given that the same investigative authority flat-out rejected the subsidy allegations only a few years earlier in May of 1983.

It is entirely possible that the ITA was unable to conduct this subsidy investigation objectively, because it was under direct or indirect pressure from the CFLI and/or Members of Congress to produce an affirmative determination. The possibility also exists that the ITA simply erred in its initial subsidy investigations — U.S. trade laws do permit repeated CVD investigations, even if the grounds for the request have not changed. The fact that the initial determination was reversed proves how elastic determinations can be. However, Congress deliberately crafted trade remedies in a manner that would allow domestic industries to fight foreign competition by requesting new investigations, when the ITA and/or ITC produce

negative determinations. This is not to say that U.S. industries automatically lobby for a new investigation after losing a case. However, in this case, the Coalition felt that the stakes of U.S. producers warranted pursuit of a second CVD investigation, and that amendments to U.S. CVD laws would work in its favour.

The Administration was obviously interested in gaining fast-track authority in order to enter into free trade negotiations with Canada and was not willing to run the risk of losing fast-track authorization from failing to act on softwood. There is no other logical way of explaining how the same U.S. institution, the ITA, could completely reverse its determination on the same softwood issues only a few years after finding negatively in CVD 1.

a) The Memorandum of Understanding (MOU)

A preliminary finding of subsidization does not mean that Canadian exports are automatically subject to interim duties. However, the preliminary determination of subsidies did concern the provinces. A duty could potentially have a significant adverse impact on softwood exports, should the ITA and ITC both find affirmatively in their final determinations.

Ottawa, too, was concerned that a final subsidy determination could result in Canadian industries losing billions of dollars in duties to the U.S. and therefore opted to enter into negotiations with the U.S.

Before the ITA could produce a final determination in the second CVD case, on December 30, 1986, Ottawa and Washington signed the *Memorandum of Understanding between the Governments of Canada and the United States of America concerning trade in certain softwood lumber products* (hereafter the "MOU").³⁶ Ottawa withdrew the harassment petition it had filed under GATT, and the U.S. terminated its CVD case against softwood lumber from Canada. By entering into the MOU, Ottawa agreed to impose a 15% tax on softwood lumber exports to the U.S. and open its records to prove to the U.S. that it was actually collecting

the tax. The export tax revenues would then be redistributed back to the general provincial coffers.³⁷

In evaluating the MOU, the CFLI was content that the export tax would raise the price of softwood lumber imports from Canada and potentially slow their entrance into U.S. markets. This would have the effect of decreasing the supply of softwood lumber in the U.S., and potentially generate higher prices. The statistics suggest that the MOU did have the effect of increasing the price of softwood lumber in the U.S. market: the composite price of framing lumber rose from a monthly average of \$212/thousand board feet (U.S.) in December 1986, to \$226/thousand board feet (U.S.) in January 1987, an increase of 7% in the first month of the MOU (Random Lengths, On-Line a).³⁸ One year after the MOU, the composite price of framing lumber had risen to an average monthly cost of \$244/thousand board feet (U.S.), 15% higher than pre-MOU prices.³⁹

The MOU was potentially less punitive than duties might have otherwise been (without such a compromise) and the MOU brought long-sought results for the Coalition.

However, Canadian softwood lumber producers were not at all pleased with Ottawa's negotiation of the MOU. First, a 15% export tax would be applied to its U.S.-bound softwood exports. Second, softwood industries felt that signing the MOU sent the CFLI a message that Canada was willing to compromise on disputes concerning the lumber. In fact, the MOU may have weakened Canada's bargaining position for SLA negotiations in future years (Jadryk, 1999). To Ottawa, the MOU was a much better option than having the U.S. collect a 15% duty, and potentially billions of dollars, on softwood lumber imports from Canada.

³⁶ The MOU was not published.

³⁷ None of the export taxes that Ottawa collected were to be channelled back to lumber companies or loggers.

³⁸ The framing lumber composite is that of U.S. – based Random Lengths – a firm that gathers forest industry data as a broad measure of price movement in the lumber market. This price is a weighted average of 15 key framing lumber prices “Useful data – monthly composite prices”.

³⁹ Data on the historical composite price of structural panel was unavailable.

b) Controversial “Replacement Measures” and the Termination of the MOU

On October 1, 1987, B.C. instituted “replacement measures” that would replace the MOU export tax. Canada was required under the MOU to consult with the U.S. before implementing replacement measures, but the U.S. refused to engage in consultations (Random Lengths, On-Line b). The replacement measures included a change in timber pricing policies and legislative amendments to the B.C. Forest Act to transfer the cost of forest renewal to the holders of major leases (Sampson, 2000). The B.C. Government at the time, an New Democratic Party (NDP) government, also sought higher stumpage revenues and was willing to test whether the province could withdraw from the MOU without facing significant retaliation from the U.S. (Anonymous Interview, June 1999). The Province argued publicly that increasing stumpage rates would provide the same effect as the export tax collected in Ottawa. In other words, the replacement measures would increase the price of softwood lumber on the U.S. market by the same margin as the existing export tax. Some softwood-exporting producers may have been indifferent to the replacement measures, but non-exporting producers were angry that they would be forced to incur new costs.

On April 1, 1988, Quebec announced that its producers would no longer pay Ottawa the full 15% export tax it had agreed to under the MOU. Quebec explained that because its Forest Act (1986) resulted in higher net stumpage, silviculture and forest management costs, Quebec softwood lumber producers would begin to pay Ottawa only 8% in tax in order to offset these higher costs (ibid.). The tax was adjusted a number of times after this initial drop, in order to account for various alleged cost increases including stumpage and insect and disease control (ibid.).⁴⁰

⁴⁰ On November 1, 1990, the export fees were adjusted to 6.2%. On November 1, 1991, the export fees were adjusted to 3.1%. On November 1, 1992, the province announced that it was again revising Ottawa’s levy, on Quebec’s softwood exports to the U.S., down to 3.0% through October 31, 1994.

In 1991, Alberta began implementing replacement measures. Ottawa then acted on the wishes of the provinces by announcing to the U.S., September 3, 1991, that it would terminate the MOU on October 4, 1991 (ibid.). Termination of the MOU also meant that Canada would no longer be required to prove to the U.S. that it was collecting tax on U.S.-bound softwood lumber — this would reduce the administrative burden for Canada. The Canadian records never exposed to the U.S. how much each individual producer was exporting south. Canada ensured that this was the case, because the U.S. could have otherwise used this information to gain a competitive advantage.

Although Ottawa negotiated the MOU, natural resource management falls within provincial jurisdiction in Canada. Therefore, there was little Ottawa could have done, even if it wanted to, to force the provinces to pay the 15% tax it had earlier agreed to with the U.S. Domestic producers were also confident that if the U.S. initiated another countervailing action, the “replacement measures” would be sufficient to generate a negative subsidy determination.

Part II: The Indicators

(a) Market Share

When the U.S. launched its second CVD case (CVD 2) in 1986, Canadian producers held 29.7% of the U.S. softwood lumber market. Canadian market share peaked at 32.7% in the previous year (1985), so had cooled in the year CVD 2 was launched. Indeed, Canadian exporters had gained only 0.7% of the U.S. market since launch of the previous case (CVD 1). After this moderate gain, Canadian producers’ 29.7% share of the U.S. softwood lumber market was -0.6 deviations from the mean Canadian market share from 1972-2002. At the same time, there were signs that Canadian producers were slowly absorbing a more significant piece of the U.S. softwood pie. Other countries such as Chile, China and Mexico had also begun to tap into the U.S. market. These countries together supplied 0.3% of softwood lumber consumed in the

U.S. but nonetheless represented an added threat. Further, U.S. softwood producers' share of the U.S. market had fallen 1% to 70% since the U.S. launched its previous dispute. This was a -0.2 deviation from the 71% mean market share U.S. producers held of the U.S. softwood lumber market from 1972-2002.

(b) State of U.S. Economy

The U.S. launched CVD 2 near the end of the 1980s recession, at a time when economic activity was beginning to pick up in the U.S. However, given the intensity of economic hardship that Canadian and U.S. firms weathered during the recession, few were flush with cash. The Federal Timber Payment Modification Act provided some assistance to producers in the Pacific Northwest.

In the year that the U.S. launched CVD 2, 1986, U.S. GDP was \$5.91 trillion. This was considerably higher than the \$5.13 trillion GDP recorded three years back, when CVD 1 came to a close (1983).

The rate of unemployment in the U.S. lumber and wood products sector had fallen to 10.3% by the time the U.S. launched CVD 2 in 1986. This was an improvement to the 15.0% rate of unemployment in the sector at the outcome of CVD 1, but significantly higher than the average 8.1% rate of unemployment in this sector from 1976-2002 (U.S. Bureau of Labour Statistics, 2003) .

Overall unemployment in the U.S. civilian workforce was 7.0% when the U.S. launched CVD 2. This was a much healthier level than the 9.6% unemployment rate that existed at the outcome of CVD 1, but still slightly higher than the 6.4% average rate of unemployment rate from 1976-2002 (U.S. Bureau of Labour Statistics, 2001) .

(c) Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade to Which the U.S. Had Significant Stakes

Earlier, there was a discussion about whether pending fast-track authority might have influenced the outcome of CVD 2. When the U.S. launched this dispute, in 1986, the U.S. Administration had a significant interest in securing Congressional fast-track authority to bring Canada into serious negotiations regarding the proposed FTA. Canada also had significant interests in negotiating the Agreement; it too stood to gain significant economic benefits from this vast liberalization initiative.

(d) Level of Protectionist Sentiment in the U.S.

In 1986, the U.S. initiated a total of 109 CVD and AD cases (26 CVD, 80 AD), which is 57 cases more than the average 52 cases initiated annually by the U.S. from 1972-2002. Given a standard deviation of 28.7 for this first data set, this number of cases is +2.1 deviations from the mean, or “extremely high”. The fact that such a large number of cases were launched should, however, come as no surprise. When FTA talks loomed in the mid-late 1980s, “there were interests in the United States, mostly in the natural resources sector, hostile to expanding trade with Canada, and there were irritants that might at any point explode” (Bothwell, 1992, p. 145). Indeed, it was quite evident at the time that the FTA would open up all U.S. natural resource industries to major competition from Canada. Canadian firms had access to vast amounts of natural resources, and U.S. firms recognized that a FTA would significantly impact their ability to compete. Further, the U.S. populous was becoming increasingly concerned about vast trade deficits and accumulating debt in the U.S. The Reagan Administration was unable to slow this trend, which became fuel for U.S. protectionist fire (ibid.).

In that same year, 10 GATT cases were initiated against the U.S., which is 4.5 cases higher than the average 5.5 cases initiated annually from 1972-2002. Given a standard deviation

of 4.5 for this second measure, this number is +1.0, or one full deviation from the mean. One possible explanation (for this deviation) is that this was federal-level retaliation to the excessive number of CVD and AD cases the U.S. initiated against its trading partners around this period. Taken together, there was a “very high” level of protectionist sentiment in the U.S. when CVD 2 was initiated.

Summary

Following the “no subsidies” finding in the first CVD case, the CFCLI became the CFLI, and took renewed action against Canada by drawing “fast-track” authority (for the FTA negotiations) into discussions regarding the ongoing softwood dispute. Once fast-track had been secured, the Coalition requested a new CVD investigation. Before the ITA could produce a final determination, Canada and the U.S. signed the MOU. The CFLI was content with the MOU, which increased the price of softwood lumber in the U.S. Ottawa later took action on behalf of the provinces, and terminated the MOU in October 1991. Canadian producers were confident that if the U.S. initiated another countervailing action, provincial “replacement measures” adopted would be sufficient to generate a negative subsidy determination.

The indicators have shown that Canadian producers enjoyed a larger portion of the U.S. in 1986 than they did when the previous dispute was launched. There were also signs that Canadian producers could be gaining an even larger share in the future. U.S. GDP was considerably higher at the launch of CVD 2, than it was when CVD 1 came to a close; unemployment in the lumber sector had fallen significantly, but was still high relative to the average rate of unemployment from 1976-2002; and unemployment in the U.S. civilian workforce was at a much healthier level than at the outcome of CVD 1, but remained slightly higher than the average rate from 1976-2002. The U.S. Administration had a significant interest in securing fast-track negotiating authority for the purpose of entering into FTA negotiations with Canada. Canada also had significant interests in negotiating the Agreement. The U.S.

launched an “extremely high” number of CVD and AD cases and a “high” number of GATT cases were launched against it that same year. Taken together, these two data sets indicate that there was a “very high” level of protectionist sentiment in the U.S. when CVD 2 was initiated.

Chapter Five: The Third Countervailing Duty Case

Part I: What Happened

On the same day that the MOU was terminated, October 4, 1991, the DOC immediately applied interim bonding requirements on all Canadian softwood lumber exports with respect to Section 302 of its 1974 Trade Act (Apsey & Thomas, 1997, p. 40).⁴¹ The bonding requirements were applied in retaliation to Canada's abrogation of its obligations under the MOU, which Commerce argued Canada terminated illegally. At the same time, Commerce announced its intention to self-initiate a third CVD investigation against softwood lumber exports from Canada (ibid. p. 37). The U.S. knew that Canada could potentially withdraw from the MOU and the immediacy of the bonding requirements suggests that these two undertakings were part of a U.S. back-up plan.

On October 8, 1991, Canada requested consultations with the U.S. in order to put an end to what it alleged were illegal bonding requirements. Having achieved no significant progress, on November 1, 1991, Canada brought the matter before the GATT Committee on Subsidies and Countervailing Measures (SCM). The SCM recognized that consultations had failed to achieve any progress and thus appointed a dispute settlement panel one month later (ibid. p. 40).

Commerce self-initiated the third CVD case (CVD 3) on October 23, 1991. It argued that B.C. log export restraints (LERs), which make it illegal to export raw logs, increase the provincial supply of logs and artificially suppress the domestic price. Commerce argued that LERs “represented a subsidy to B.C. lumber producers and other firms using unprocessed logs as an input to manufacturing processes” (Hoberg and Howe 1999: 24). The LER platform represented an innovative arm for the U.S. case, which would complement its conventional

⁴¹ Interim bonding requirements enabled Commerce to immediately increase Canadian producers’ costs for exporting softwood to the U.S., while waiting for the results of its CVD investigation.

argument that provinces subsidize softwood production. The main objective of the U.S. softwood lumber industry remained unchanged, that is, the industry still sought to level the competitive conditions in the U.S. lumber market, through provincial forest management reforms and/or duties.⁴²

B.C. accepted the fact that LERs were in place, but argued that “B.C.’s LERs were superfluous” (ibid.). This was a rather weak response because the export restraints were obviously designed to have some effect on softwood production in B.C. (ibid.). “Export restraints ensure that goods which might otherwise be sold abroad remain within a country for domestic sale. This artificially increases the domestic supply of those goods, putting downward pressure on domestic prices” in Canada (ibid., p. 24).⁴³ In all likelihood, B.C. has used LERs in order to maintain and perhaps attract processing jobs to the Province.

B.C. also argued that LERs were an attempt to balance market distortions elsewhere in the global softwood lumber market. The Province explained that because Japanese tariffs on processed wood were so high, this artificially inflated the demand for B.C. raw logs. Therefore, B.C. claimed that LERs were necessary to offset the distorted demand for unprocessed logs (ibid. p. 27). Finally, B.C. argued that if LERs were removed, other nations would process more raw logs. In turn, this would decrease the demand for processed wood from the province, reduce domestic demand for B.C. raw logs and result in an overall loss of jobs from B.C. (ibid.).

The truth of the matter concerning LERs is that neither U.S. nor Canadian interests managed to provide conclusive support for their respective positions. The Americans were unable to find

⁴² The possibility exists that the U.S. contemplated using the LER argument in previous disputes, but there is no evidence to suggest that this was necessarily the case.

⁴³ This argument is limited in the sense that it assumes that a free market exists in softwood lumber between Canada and the U.S. The reality is that Canadian softwood exports were subject to a tax under the MOU, interim bonding requirements once the MOU was terminated, tariff-rate quotas under the SLA, and now duties in the post-SLA period.

enough empirical evidence to support their case against LERs. B.C. industry failed to assess “the impact of completely removing B.C.’s LERs” and, as a result, was unable to discredit U.S. claims that LERs kept down the price of lumber (ibid. p. 30).

The ITC released an affirmative preliminary determination of material injury in CVD 3 on December 27, 1991. On March 5, 1992, the ITA preliminarily found subsidies in the amount of 14.48%. The ITA then reassessed this figure down to 6.51% with its final determination released May 28, 1992 (Apsey & Thomas, 1997, p. 42).⁴⁴

In response to the ITC’s final determination of material injury, on July 15, 1992, Canada requested the establishment of a panel under Chapter 19 of the 1989 *Canada-U.S. Free Trade Agreement*.⁴⁵ The second panel, to review the ITA’s affirmative subsidy determination, was established on July 29, 1992.

The GATT Panel released its report concerning the bonding requirements and self-initiation of the third series of CVD investigations February 19, 1993. The Panel supported Canada’s challenge that the U.S. did not have the right to impose interim bonding requirements before it released its preliminary determinations. This, the Panel determined, was in violation of GATT Article 5 (ibid. p. 44). “The GATT expressly required that the country seeking to impose such duties previously notify the GATT of the domestic statutes which permitted it to do so and notify the GATT of the duties. The U.S. failed on both accounts (Ragosta 2000).” On the other hand,

⁴⁴ It is interesting to find that of the 6.51% determination, LERs were considered a 3.6% subsidy and stumpage only 2.9%. The latter is a far cry from assessments in earlier investigations which alleged subsidies of up 30%.

⁴⁵ Canada and the U.S. agreed to each establish a Secretariat to facilitate the general operation of Chapter 19 (dispute settlement), and the work of any panels or committees that may be convened pursuant to the Chapter. Panels work out of the Secretariat of the “amending Party’s Secretariat” (1903.2); in this case Canada. Because Canada was challenging an ITC determination, it was the role of the panel to determine whether the ITC had correctly applied, and followed the procedures as mandated by U.S. law.

the GATT Panel agreed with the U.S. that Canada's termination of the MOU justified its self-initiation of CVD 3 (Thomas & Apsey, 1997, p. 43).

How then did Canada and the U.S. react to the fact that the GATT Panel ruled in the U.S.'s favour, concerning Commerce's self-initiation of the third CVD investigation, but in Canada's favour, concerning the matter of bonding requirements? According to Ragosta (2000),

Canada lost the important question: can the United States investigate the log export restrictions as subsidies? Admittedly, the panel did not issue a final finding that the log export restrictions ARE subsidies, because Canada had challenged our right to proceed. Yet, the case is very favorable on both U.S. rights to bring CVD cases and the fact that the export restrictions are, in fact, subsidies. Let's put it this way: we were the ones celebrating this 'split' decision (Ragosta, 2000).

Ragosta notes that while the GATT Panel never ruled on whether LERs are subsidies, and thus inconsistent with the GATT, the Panel did determine that Commerce had the right to self-initiate the third CVD investigation on LERs.

Canadian producers see the GATT Panel determinations as a victory of their own. They point out that the Panel determination, that the U.S. did not have the right to impose interim bonding requirements, is evidence of protectionist forces behind U.S. trade remedy processes (Jadzyk, 1998).

Neither Canadian softwood producers nor their U.S. counterparts emerged as clear victors from the GATT Panel decisions — it was a split decision that had no immediate impact on the conditions of the bilateral softwood trade.

On May 6, 1993, the FTA panel unanimously determined that the U.S. Government needed to re-examine whether the provincial programs could distort the operation of normal competitive markets before it could determine that there was preferential pricing; examine whether LERs were specific to certain enterprises; determine whether there was a direct relationship between

LERs and the price of logs in B.C.; and show that provincial subsidies were disrupting normal competition in U.S. softwood markets (Apsey & Thomas, 1997, pp. 45-47).

The FTA Panel that was directed to review the ITC's affirmative finding of material injury released its determination on July 26, 1993. The Panel confirmed that there was a "significant" volume of spruce, pine and fir imported from Canada around the time of the ITC's investigation.⁴⁶ However, the Panel also found that the ITC had failed to show that these imports were the cause of material injury in U.S. markets. Therefore, the Panel remanded the ITC's determination for reconsideration (ibid. p. 49)

On September 17, 1993, the ITA came to a new subsidy determination of 11.54% (Hoberg & Howe, 1999, p. 8).⁴⁷ It argued that contrary to the decision of the initial FTA Panel, it did not need to prove market distortion in an affirmative determination of subsidies (Thomas & Apsey, 1997, p. 50).

The ITC again determined, on October 25, 1993, that Canadian softwood lumber exports were suppressing prices in the U.S. market. This decision was again remanded by the same FTA Panel, which indicated that material injury does not necessarily result from a higher volume of imports (Thomas and Apsey 1997: 51).

On December 17, 1993, the Panel reviewing the ITA's revised subsidy determination again remanded its decision for a lack of evidence that stumpage programs were specific or causing market distortion.⁴⁸

⁴⁶ It is difficult to judge whether the term "significant" means higher than usual imports, or just normally high imports. However, in this context, the term seems to imply that there was an unusually high volume of imports during the time of the investigation.

⁴⁷ This was a re-determination on remand based on the initial FTA Panel decision (during CVD 3) that unanimously found in favour of Canada.

⁴⁸ This reprimand became controversial because while the Panel upheld the initial decision, those Panellists who supported a reversal of the initial decision were American.

Soon afterward, a joint Senate Committee, considering how NAFTA might be implemented in the U.S. if passed, criticized both FTA Panels for exceeding their jurisdiction.⁴⁹ Specifically, the Committee stated that it was the sole mandate of the Panels to determine whether or not the ITA and ITC had correctly applied U.S. laws, not to pass judgement on the determinations of these agencies (Gastle & Castle, 1996, p. 840; Cashore, 1997, p. 23). The report indicated that it was not necessary for Commerce to show, “that the subsidy has the effect of lowering the price or increasing the output of a good before a duty can be imposed” (Cashore, 1997, 24). In other words, Commerce did not need to show that government subsidies made it cheaper for Canadian producers to produce greater volumes of softwood lumber. While Senate committees are entitled to weigh-in on matters that they feel fall under their jurisdiction, this Committee went too far in criticizing the independent FTA Panels. At the same time, the report came as no surprise. It simply reiterated the fact that there was strong support in the Senate for a continued fight against Canadian softwood lumber imports.

The CFLI then requested that the United States Trade Representative (USTR) challenge the Panel decisions, under Annex 1904.13 of the CUSFTA, through the Extraordinary Challenge Committee (ECC) (Thomas & Apsey, 1997, p. 57).⁵⁰ Here, the Coalition alleged that two Canadian panellists had ties with forest industries in Canada. This, the CFLI argued, made it impossible for the Panel to be objective in its consideration of the case. In addition, the Coalition argued that the Panels made legal errors in their determinations. The USTR acted upon

⁴⁹ Given that the Panel decisions thwarted the position of U.S. producers, this criticism came as no big surprise.

⁵⁰ The Extraordinary Challenge Committee consists of three retired judges who are selected jointly by Canada and the U.S. As the name suggests, the committee is used to “ensure that the panel’s decision is in accordance with its mandate as prescribed by the FTA.”

the request of the CFLI and brought these challenges before the ECC on April 6, 1994, as a final attempt to win support for the U.S. case in CVD 3.⁵¹

The ECC found in Canada's favour by upholding the Bi-national Review Panel decisions on August 16, 1994. This determination prompted Commerce to finally terminate its investigations and appeals pertaining to CVD 3.

When Canada agreed to enter into consultations with the U.S., the U.S. agreed to stop imposing bonding requirements and to refund bonds collected since March 17, 1994; the date of the Bi-national Review Panel's final decision.⁵² The outcome of this third dispute was the negotiated settlement reached between Canada and the U.S. in April 1996 — the Softwood Lumber Agreement (SLA).

Part II: The Indicators

(a) Market Share

When the U.S. initiated its third CVD case (CVD 3) in 1991, Canadian producers held 27.6% of the U.S. softwood lumber market. The Canadian share was up from 26.6% in the previous year, but was much less than the 29.7% retained when the previous softwood dispute was launched (1986). This loss in Canadian market share was -1.4 deviations from mean Canadian market share from 1972-2002. U.S. producers' share of the U.S. softwood lumber market increased 1.8% since the previous dispute (+0.2 standard deviations). Other countries' share fell marginally from 0.3% to 0.2%. In terms of market share, U.S. softwood producers

⁵¹ Only governments are entitled to appeal panel decisions through an ECC.

⁵² *Certain Softwood Lumber Products from Canada* (U.S. Determination on Remand), USA-92-1904-01. January 6, 1994, affirmed by the Panel at *Certain Softwood Lumber Producers from Canada* (Order), USA-92-1904-01, February 23, 1994 (Ch. 19 Panel). *Certain Softwood Lumber Products from Canada*, 59 Fed. Reg. 12,584 (Court Decision and Suspension of Liquidation) March 17, 1994 (as cited in Submission of Canada In the Matter of British Columbia's June 1, 1998 Stumpage Reduction, January 25, 1999).

were better-off than they were at the initiation of the previous softwood lumber dispute and Canadian producers were worse off.

(b) State of U.S. Economy

When the U.S. launched CVD 3 in October 1991, the U.S. economy had officially fallen into an economic recession. This was evident given two small, but consecutive, quarterly contractions in GDP.⁵³

Unemployment in the lumber and wood products sector was 9.8% when Commerce initiated CVD 3 in 1991. This was lower than the 10.3% rate of unemployment in this sector at the outcome of CVD 2 in 1986, but higher than the average 8.1% rate of unemployment rate from 1976-2002.

The overall rate of unemployment in the U.S. was 6.9% when the U.S. launched CVD 3 in 1991 (U.S. Bureau of Labour Statistics, 2001). This was almost on par with the 7.0% level at the outcome of CVD 2 in 1986, and was slightly higher than the 6.4% average level of unemployment recorded from 1976-2002.

(c) Uncertainty in Trade Negotiations/Other Bilateral Sectors of Trade to Which the U.S. Had Significant Stakes

When the U.S. launched CVD 3, in October 1991, President George Bush, Sr., and his Administration were involved in critical negotiations for the NAFTA. The Agreement held tremendous potential for liberalizing the movement of goods, services and investment between Canada, the U.S. and Mexico and was a pressing matter for both Canada and the U.S. The GATT-WTO Uruguay Round was also a top priority for the U.S. Administration, but also important to Canada (Destler, 1995, p. 218).

⁵³ GDP dropped from US\$6.71 trillion in 1990 to US\$6.68 trillion in 1991 (a contraction of 0.5%).

(d) Level of Protectionist Sentiment in the U.S.

In 1991, the U.S. initiated a total of 77 CVD and AD cases (11 CVD and 66 AD), which is 25 cases more than the 52 cases initiated on average each year from 1972-2002. Given a standard deviation of 28.7 for the data set, this number is +0.9 deviations from the mean.

The proposed NAFTA was highly controversial at the time when CVD 3 was launched. This is mainly because U.S. labour unions were able to use their vast resources to successfully instil fear among the U.S. public that the proposed Agreement could result in massive job losses to Mexico. Americans were already distressed about the state of the U.S. economy and were wary about expanding trade when even more jobs could be jeopardized. In fact, then-Presidential Candidate Bill Clinton may have secured his Presidency by successfully appealing to this sentiment (Dryden, 1995, p. 382).⁵⁴

In the same year, there were 9 GATT cases initiated against the U.S. by all other countries. This number is 3.5 more than the average 5.5 GATT/WTO cases launched annually against the U.S. from 1972-2002. Given a standard deviation of 4.5 for this data set, the number of cases initiated is 0.9 deviations above the mean and a relatively “high” number of cases. The fact that a high number of GATT cases were initiated against the U.S. provides some evidence that U.S.’ trading partners were distressed with U.S. trade policy. This level of discontent did not improve when the ITC and Congress showed significant resistance in Uruguay Round GATT/WTO negotiations. Both parties vehemently resisted efforts of other GATT nations to reform strong U.S. anti-dumping laws (Destler, 1995, pp. 241-242).⁵⁵

⁵⁴ Under pressure from big business, Clinton eventually changed his position as President and endorsed the benefits of NAFTA. Knowing that he would lose some political support by so doing, Clinton made his endorsement conditional. He encouraged Congress to enact legislation that would provide vocational assistance to those that lost jobs to Mexican firms, tighten environmental rules in North America, and create a joint U.S.-Mexican Commission that would improve working standards.

⁵⁵ In December 1991, GATT Secretary-General, Arthur Dunkel, proposed a series of anti-dumping reforms for Uruguay Round negotiations – he recognized this would be key to overcoming a negotiations stalemate. The U.S. had limited success in diluting the proposed anti-dumping reforms late in negotiations November-December 1993. However, Congress was later able to weaken the effect of the reforms, by issuing a strong “statement of action” as part of the Uruguay Round implementing legislation. The statement would guide how U.S. trade bodies applied the

Summary

Canada triggered the third CVD dispute, and the mass of challenges that followed, when it pulled out of the MOU in October 1991, in response to political pressure from several of the provinces. Commerce found subsidies in its final determination and the ITC found in its own final determination, that provincial subsidies were damaging U.S. softwood lumber producers. Canada challenged these determinations through FTA dispute settlement and the FTA Panels repeatedly remanded the findings of the Commerce and the ITC. Canada eventually agreed to negotiate a deal, when the U.S. agreed to refund some of the bonds it had imposed on Canadian lumber.

Canadian producers lost 2.3% of the U.S. softwood lumber market between the launch of CVD 2 and CVD 3. The U.S. economy was in a recession; unemployment in the U.S. lumber sector had fallen since the outcome of CVD 2, but was still slightly higher than the average annual rate from 1976-2002; and overall unemployment in the civilian workforce remained close to the level it was at the outcome of CVD 2 — slightly higher than the average from 1976-2002. The U.S. was involved in both NAFTA and GATT-WTO Uruguay Round negotiations — both were top priority for the U.S. Administration, and also of importance to Canada. The U.S. initiated a “very high” number of CVD and AD cases in 1991 and also had a “very high” number of GATT cases launched against it. Accordingly, U.S. protectionist sentiment was “very high” when CVD 3 was launched.

new U.S. anti-dumping laws. This political tinkering well illustrates the strength and determination of the USTR and Congress to defend the interests of domestic industries in the early-mid 1990s.

Chapter Six: The Softwood Lumber Agreement (SLA) and CVD-AD 4

Part I: What Happened

Completion of the Uruguay Round GATT negotiations created the WTO. Recognizing that Congress would have to enact legislation in order to implement the Round, the CFLI lobbied for the inclusion of statutory amendments to U.S. trade laws that would make it easier for it to secure subsidy determinations in subsequent petitions (Thomas & Apsey, 1997, p. 60). There was no need for the CFLI to re-conceptualise the softwood issue, or for it to develop any new strategic direction. The Coalition anticipated that Congress would amend U.S. trade laws in a manner that would ultimately leverage its bargaining position with Canada.

The Coalition was successful in securing amendments to Section 771(5) of the *United States Tariff Act of 1930 (19 U.S.C. 1677)*, through the enactment of Section 251(a)(5)(C) of the *Uruguay Round Agreements Act*. This eliminated the need for the ITA to consider the actual economic impacts of an alleged subsidy in its investigations (*ibid.*). The amendments also lessened the requirements for the ITA to find that “specific” subsidies existed. Hence, the ITA would only have to prove that *one* of the following conditions existed:

- (1) Actual recipients of the subsidy, whether considered on an enterprise or industry basis, are limited in number;
- (2) An enterprise or industry is a predominant user of the subsidy;
- (3) An enterprise or industry receives a disproportionately large amount of the subsidy;
- (4) The manner in which the authority providing the subsidy has exercised discretion in the decision to grant the subsidy indicates that an enterprise or industry is favoured over others (*ibid.* p. 61).¹

The Uruguay Round negotiations provided some clarification to the 1979 GATT Subsidies Code by defining subsidies as a “financial contribution from government which

¹ This simplified previous rules that only allowed Commerce to make a positive determination when it could prove all of these conditions existed.

confers a benefit.”² The negotiations also generated an extensive list of WTO-illegal government actions that would benefit domestic industries. The changes do not prohibit countries from implementing changes to their domestic trade laws, but do help clarify the role of WTO dispute settlement panels in rendering decisions in subsidy cases.

a) Consultations and the Negotiation of the Softwood Lumber Agreement

After Congress passed the *Uruguay Round Agreements Act*, Canadian softwood lumber producers decided they had had enough of the litigious nightmare that had resulted from repeated CVDs, various forms of appeals and U.S. trade law amendments (Thomas and Apsey, 1997, p. 65). Canadian producers realized that in order to put an end to a costly legal battle against U.S. softwood interests, the provinces would need to make some changes to their forestry practices (ibid.). The options were to increase stumpage rates in the provinces, adopt a forest management system consistent with the U.S. bidding system, or remove provincial raw log export restraints (LERs). The latter could result in a lower provincial supply of lumber and potentially drive-up the price of Canadian lumber, closer to that of the U.S.

Yet, it was also evident that after 13 years of fending off challenges from the U.S., major Canadian producers were not about to simply wave a white flag. With the consent of B.C., Alberta, Ontario and Quebec, Ottawa offered to enter into formal negotiations with the United States. The U.S. agreed to refrain from filing further CVD investigations during negotiations in the summer of 1995 (ibid.).

Negotiations led to some progress in the dispute. However, when no firm agreement had been reached by November of 1995, Montana Senator Max Baucus introduced a bill to bring “emergency relief from the flood of softwood lumber from Canada” (Thomas & Apsey, 1997, p.

² Article 1.1 from Agreement on Subsidies and Countervailing Measures (SCM)

65; Baucus, 1995). If enacted, the bill would have mandated Commerce to conduct a fourth CVD investigation. This provided further indication that certain Members of the Congress remained fully committed to do all in their power to support CFLI and its member constituents. The threat provided enough motivation to B.C. and Quebec to table new offers, which in turn provided impetus for Ottawa to enter into more significant negotiations with the U.S. (Thomas & Apsey, 1997, p. 65).³

At this point, Canada still needed to address the problem of competition between the provinces over U.S. softwood lumber markets. B.C. was willing to agree to some form of quota on its exports, but did not want the other provinces to gain its market share. Therefore, the Province pushed for an agreement that would apply to major softwood lumber exporters across Canada (Jadzyk, 1998).

On the U.S. side, the U.S. Government and the CFLI knew that the major softwood lumber exporting provinces had drastically increased stumpage rates during the course of the dispute (Cashore, et. al., 2001, p. 24).⁴ U.S. interests also anticipated that import quotas might help U.S. softwood lumber producers obtain a greater share of the U.S. market, and would bring them a higher return for their product (Apsey & Thomas, 1997, p. 69).

The CFLI also knew that a continued pursuit of countervailing duties might provide the appearance that it was willing to take all measures necessary to protect U.S. firms. In theory, this could weaken the merits of its case against Canadian softwood lumber imports and force some Members of Congress to distance themselves from the Coalition.

³ Canadian softwood lumber producers recognized that Baucus alone was well enough connected with the U.S. softwood lumber lobby to make negotiations even more difficult for Ottawa if the latter did not table a better offer.

⁴ For example, B.C. instituted what it called a “super stumpage” fee in 1994. This new fee system would collect higher fees once market prices hit \$250/cubic metre, and even higher fees when market prices exceeded \$400/cubic metre. This brought a 63% increase in fees for softwood from the interior, and an 81% increase for coastal lumber (Calculated from figures in Cashore et. al.).

At the same time, the U.S. lumber industry recognized Canadian producers' stake in the U.S. market and that Canada would need to offer some concessions in order to secure more certain economic access. Economic conditions in Asia in the 1990s made Canadian softwood producers even more dependent on U.S. markets. This was the result of the decade long slump in Japan after the bursting of the 'bubble economy' of the late 1980s and, subsequent to that, the Asian financial crisis of 1997 which affected other countries in the region. As an example of the impact of changes in Asia, Canadian softwood lumber exports to Japan fell 53% from \$1.6 billion in 1997 to \$770 million in 1998 (B.C. Stats, 1998, pp. 1-5). B.C. softwood lumber exports to Taiwan fell 28% from \$53 million in 1997 to \$39 million in 1998, and softwood destined for South Korea plummeted 76% from \$19.1 million to \$4.5 million over the same period (B.C. Stats, Not Dated, Online). Canadian producers looked to the booming U.S. economy to make up for this significant drop in Asian demand. However, despite the presence of NAFTA, the SLA had the effect of restricting the access that Canadian producers needed in the U.S. to recover from the Asian crash.

Thus, it became clear, and definitely more accepted by Canadian softwood lumber producers, that coming to an agreement with the U.S. would better serve their interests than would a continued fight with the U.S. A mutually-accepted and legally-binding agreement would also allow Canadian producers to spend more time on their businesses, and less money on legal fees. U.S. softwood lumber producers had been fighting Canadian imports for well over a decade, and were also most interested in negotiating an agreement with Canada.

The cat and mouse game came to a close on April 2nd, 1996, when Canada and the U.S. agreed to the Softwood Lumber Agreement (SLA). The SLA set a new five-year plan for softwood lumber exports from Canada to the U.S.

b) Major Provisions of the Softwood Lumber Agreement

The SLA regulated the exports of softwood lumber from B.C., Alberta, Ontario and Quebec to the U.S. for a period of five years, through the equivalent of a “tariff rate quota” (TRQ). Instead of the U.S. collecting tariffs on Canadian softwood exports, Ottawa would tax these exports.

Article I (1) of the Agreement (under “Actions by the United States of America”) states that the SLA must “ensure that there is no material injury or threat thereof to an industry in the United States from imports of softwood lumber from Canada.”⁵ This clause was essential to the U.S. because it legitimized the right of U.S. softwood lumber producers to seek protection from Canadian imports. The vagueness of this provision allowed the ITC to determine whether Canadian softwood imports were causing injury, or threatened to injure U.S. producers. Whether or not the imports were having this impact, was a matter for the ITC to determine.⁶

Article II of the Agreement formalized Canada’s responsibility for the issuance of export permits to softwood producers in the provinces of B.C., Alberta, Ontario and Quebec. Ottawa was responsible for collecting \$50 (U.S.) per thousand board feet for export volumes between 14.7 – 15.35 billion board feet, the lower fee base, and \$100 (U.S.) per thousand board feet above 15.35 billion board feet, the upper fee base.⁷ No fees were collected for exports up to and including the established base of 14.7 billion board feet per annum. Ottawa allocated export permits “prior to each year” and was responsible for ensuring that fees were automatically collected from exporters who moved 28.75% or more of their established base during any

⁵ Softwood Lumber Agreement between the Government of Canada and the Government of the United States of America 29th day of May 1996.

⁶ As with all other U.S. investigations, U.S. interests/industries that benefit from, and are injured by Canadian imports, have the right to lobby the ITC and Congress for action or non-action against Canadian imports. The ITC may also conduct firm-specific investigations on dumping petitions.

⁷ Subsequent events brought B.C. and the U.S. to negotiate higher taxes for B.C. producers in the fourth and fifth years of the Agreement.

calendar quarter. The SLA did not set provincial export quotas. Ottawa decided that rather than allocating Canada's quota in this manner, producers in B.C., Alberta, Ontario and Quebec would each year apply for export quota.

While this system was not a strict quota, it discouraged Canadian softwood lumber exporters from exceeding the established base. When the market price of softwood lumber was high enough to cover production costs and the export tax, Canadian producers would continue to export.

Article III (1) of the Agreement, (under "Trigger Price") sets the conditions that Canada may export additional volumes of softwood lumber, without paying extra export taxes. It explicitly states that Canada may export an additional 92 million board feet over four calendar quarters when the average price, per thousand board feet, of various species "equals or exceeds" \$410 (U.S.) for a full calendar quarter.

The most obvious explanation of this provision is that the U.S. did not want to experience periods where consumers would suffer due to a shortage in lumber. Moreover, a shortage of cheap softwood lumber would likely drive up prices. Instead, the Canadian lumber industries would be able to respond to the increase in demand and provide U.S. industries with more lumber at a reasonable price. For Canada, this provision allowed for easier access to markets in the U.S. if the price of softwood lumber increased.

With reference to Article VII of the Agreement ("General Provisions"), both Canada and the U.S. agreed not to "take action to circumvent or offset the commitments set out in this Agreement." Canada extended its commitment by "certifying" to the U.S. during each quarter that it had neither reason to believe that provincial timber pricing or forest management systems

were modified, nor that “these provinces (were) collecting revenues at levels lower than called for under those systems.”⁸

It is interesting to find that the “General Provisions” of the SLA gave Ottawa the added responsibility of certifying Canada’s compliance with the Agreement. One would think that subsections (1) and (2) of Article IV, whereby Canada and the U.S. agreed to exchange all relevant records monthly, would have been sufficient. This was not the case, and was additional evidence of tension and distrust between Canada and the U.S. over this longstanding dispute.

c) Conclusion of the Softwood Lumber Agreement

The five-year SLA expired on April 1, 2001. In the period leading up to this date, Washington exercised the preferred strategy of the U.S. network and attempted to bring Ottawa to negotiate a new deal.⁹ Canada and the U.S. were both nervous about the SLA expiring. However, Ottawa played it cool in an attempt to gain leverage over the U.S. in reaching a new agreement post-SLA and potentially reap short-term benefits once the export quota expired. Ottawa also understood that it was inevitable that a vehement dispute would resurface. The rules that had governed the bilateral softwood trade over the past five years no longer applied and the doors to potential new challenges swung open.

On April 2, 2001, the CFLI exercised their second option and requested Commerce launch CVD and AD investigations on softwood lumber (Inside U.S. Trade, April 2001). The ITA formally launched these investigations on April 23, 2001 (Inside U.S. Trade April 2001; *ibid*, June 2001).¹⁰ The initiative has already resulted in the imposition of dumping and CVD duties against Canadian softwood exports to the U.S.

⁸ Notice must be given no longer than 45 days after any changes have been adopted.

⁹ Members of the U.S. network have not changed since the last dispute. They include: the CFLI and its Congressional allies, USTR and Commerce.

¹⁰ Commerce held consultations with Canada before launching these new cases, in order to comply with GATT/WTO rules. Canada argued that the CFLI did not represent a large enough proportion of the U.S. softwood industry, and that there was insufficient price data submitted for the case to proceed – Commerce rejected these arguments but promised to revisit the former issue in its final determination.

On May 16, 2001, the ITC determined that Canadian spruce, pine and fir exports were “like or directly competitive” with U.S. softwood (Inside U.S. Trade, May 2001). The preliminary decision fell short of determining that Canadian softwood exports were “causing” material injury — it did find a “threat of injury” because imports could surge in the post-SLA period (Inside U.S. Trade, June 2001). Under U.S. law, even the threat of material injury is grounds for imposing interim duties, given affirmative subsidy and/or AD findings.¹¹

On June 29, 2001, a WTO dispute settlement panel ruled on Canada’s request¹² to examine “United States Measures Treating Export Restraints as Subsidies” (WTO, 2001). Canada sought to set the record straight about LERs, in anticipation of renewed problems from the U.S.¹³ Again, the U.S. argues that the use of export restraints, with raw logs or any other commodity, results in higher domestic supplies, and lower (subsidized) domestic prices.¹⁴ The Panel found against the U.S. by determining that:

An export restraint as defined in this dispute cannot constitute government-entrusted or government-directed provision of goods in the sense of subparagraph (iv) and hence does not constitute a financial contribution in the sense of Article 1.1(a) of the SCM Agreement.

At the same time, the Panel rejected Canada’s challenge that Section 771(5)(B)(iii) of the U.S. Tariff Act of 1930 was inconsistent with Article 1.1 of the SCM Agreement, because the Article “does not require the treatment of export restraints as financial contributions” (ICTSD, 2001). This ruling implies that if U.S. law actually mandated that Commerce treat log export restraints as subsidies, this would be inconsistent with the SCM Agreement. In summary, the U.S. Tariff Act and B.C. log export restraints were both declared consistent with the WTO SCM agreement.

¹¹ Canada will not challenge this law as inconsistent with NAFTA/WTO because its own standard is the same.

¹² Canada requested the establishment of a dispute settlement panel on July 24, 2000.

¹³ The export restraints argument was used by the U.S. softwood industry in CVD 3. However, because Canada and the U.S. negotiated the SLA, a final determination was never issued.

¹⁴ It could be argued that export quotas under the SLA have a similar impact as log export restraints that the U.S. opposes. This does not necessarily undermine the U.S. argument though, because the SLA was, as with all other negotiated deals, a compromise between Canada and the U.S.

Canada may attempt to rework its case against Section 771(5)(B)(ii) and bring a new case to the WTO in the future (ibid.).

On August 10, 2001, Commerce preliminarily imposed a 19.3% duty on Canadian softwood lumber exports. Commerce demanded that duties be applied retroactively, after finding that exports surged 31% from April-June 2001, compared to the three previous months.¹⁵ Commerce also indicated that, after assessing import data, it was inclined to tack-on AD duties at a later date.

Also on August 10, 2001, Canada requested that the WTO DSB establish a panel to review whether the U.S. "Continued Dumping and Subsidy Offset Act of 2000" (the "Byrd Amendment") was GATT-WTO compliant.¹⁶ The Byrd Amendment created a new requirement for U.S. customs authorities to distribute duties it collects from CVD and AD duty orders to "affected domestic producers" (i.e. the petitioners).

Canada requested consultations as the first step toward a WTO Panel review of Commerce's preliminary determination of subsidies on August 21, 2001. This included a challenge to (a) U.S. treatment of stumpage programs as a "financial contribution" by government, (b) a U.S. presumption that the alleged financial contribution were passed along to downstream producers that use softwood lumber to produce other goods, (c) U.S. measures that imposed interim bonding requirements based on preliminary determinations, (d) U.S. refusal to conduct expedited reviews when requested to do so by Canadian producers.

¹⁵ The WTO SCM Agreement required Commerce to show that softwood exports surged 15% or more, and/or that it had sufficient reason to believe that softwood was being sold below cost in U.S. markets (i.e. dumped) to claim critical circumstances and demand retroactive duties. Canada argued that there are seasonal variations in exports, and that exports are higher from April-June because this is the peak season for housing construction. Canada found an 11% increase in exports from comparing April-June 2001 to the same quarter in 2000.

¹⁶ The Byrd Amendment created a new requirement for U.S. customs authorities to distribute duties it collects from CVD and AD duty orders to "affected domestic producers" (i.e. the petitioners).

On August 23, 2001, the WTO dispute settlement body responded to Canada's second formal request¹⁷ that the DSB establish a panel to examine whether Section 129(c)(1) of the U.S. Uruguay Rounds Agreements Act was GATT/WTO-compliant.¹⁸ Canada argued that this measure prevented the U.S. from refunding duties collected when the WTO rules duties inconsistent with the WTO Subsidies and Countervailing Measures (SCM) Agreement. Chile, the European Commission, India and Japan exercised their rights to hold third party status on the case.

On October 31, 2001, Commerce preliminarily imposed AD duties on Canadian softwood imports at an average rate of 12.7%. The determination imposed a new requirement that exporters post an equivalent bond pending the final determination.

On November 5, 2001, one of Canada's largest softwood producers, Canfor Corporation, filed its Notice of Intent to sue the U.S. Government for \$250 million (U.S.) under NAFTA Chapter 11, for the losses it incurred from the imposition of countervailing and anti-dumping duties on Canadian softwood exports.

On November 9, 2001, fourteen Congressmen wrote President George W. Bush, Junior and Commerce Secretary Don Evans a letter warning of the significant adverse impact that the preliminary CVD and AD duties would have on an already-contracting economy.¹⁹ The Congressmen urged the President to consult with the Secretary and reverse the preliminary tariffs (Inside U.S. Trade, November 30, 2001). As will be evident from the following discussion, the initiative failed to convince the real decision maker, Commerce, to hold back on the CVD and AD investigations.

¹⁷ WTO law allows the respondent to block the first request.

¹⁸ This was the U.S. legislation in which Congress accepted and implemented the GATT/WTO Uruguay Round.

¹⁹ Senators Don Nickles (R-OK), Charles E. Grassley (R-IA), Richard J. Durbin (D-IL), Jim Bunning (R-KY), Jon L. Kyl (R-AZ), Evan Bayh (D-IN), Jeff Bingaman (D-NM), Chuck Hagel (R-NE), James M. Inhofe (R-OK), Jack Reed (D-RI), Peter G. Fitzgerald (R-IL), Richard G. Lugar (R-IN), Representatives Jim Kolbe (R-AZ), and Steny Hoyer (D-MD).

On November 15, 2001, Montana Senator Max Baucus spearheaded a letter from ten Senators to Secretary Evans.²⁰ The letter warned Evans that Canadian softwood lumber industries would flood U.S. markets when the preliminary CVD expired mid-December, and asked the Secretary to expedite his final determinations (Inside U.S. Trade, November 23, 2001).

On December 3, 2001, the preliminary duty imposed on Canadian softwood lumber for alleged subsidies expired.²¹ Canada announced on February 26, 2002, that it had pre-emptively filed its Notice of Intent for a NAFTA panel review of the U.S. final determination of subsidies.²² On the following day, Canada announced that it had filed its Notice of Intent for a NAFTA panel review of the U.S. final dumping determination.

The preliminary AD duty expired March 1, 2002. Canadian exports were duty-free from this date until March 22, 2002, when Commerce issued its final determinations on subsidies (19.34%) and AD (9.67%)²³ for a total of approximately 29% (Globe and Mail, March 2002). DOC corrected its subsidy rate to 18.79% and its “all other” dumping rate to 8.43%²⁴ on April 25, 2002.

On April 2, 2002, Canada, B.C., Alberta, Saskatchewan, Manitoba, Northwest Territories, Yukon Territories, B.C.LTC, OFIA, OLMA, QLMA and several individual producers submitted their formal NAFTA complaint on the matter of subsidies. One month later, on May 2, 2002, Canada and several domestic producers subject to U.S. anti-dumping duties submitted their own complaint to the Panel.

²⁰ Baucus has led the fight against Canadian softwood lumber for well over a decade. The other signatories were Trent Lott (R-MS), Thad Cochran (R-MS), Jeff Sessions (R-AL), Tim Hutchinson (R-AR), Zell Miller (R-GA), Blanche Lincoln (D-AR), Larry Craig (R-ID), Max Cleland (D-GA), and Michael Crapo (R-ID).

²¹ Under GATT-WTO law a preliminary duty can be applied up to 120 days.

²² NAFTA panels are responsible for determining whether the final determinations are consistent with U.S. laws.

²³ This was the “all other” dumping rate applied to all firms except the following six firms for which the ITC calculated firm-specific dumping margins: Abitibi 14.60%; Canfor 5.96%; Slocan 7.55%; Tembec 12.04%; West Fraser 2.26%; and Weyerheuser 15.83%.

²⁴ ITC adjusted dumping margins for the six individual firms: Abitibi 12.44%; Canfor 5.96%; Slocan 7.71%; Tembec 10.21%; West Fraser 2.18%; and Weyerheuser 12.39%.

On May 2, 2002, the ITC made its final determination that subsidized Canadian lumber “threatened” the U.S. lumber industry with injury. This made the interim duties final (DFAIT, On-Line i). On the same day, the ITC found that Canadian softwood lumber imports were being sold in the U.S. at less than cost value and were a threat to injury. This made the interim dumping duties final.

On May 3, 2002, Canada requested a review of the U.S. final affirmative finding of subsidies. The Panel was established October 1, 2002, and is expected to issue its determination around July/August 2003 (DFAIT, On-Line j).

On June 12, 2002, the WTO Panel reviewing Section 129(c)(1) of the U.S. Uruguay Round Agreements Act made its final determination. The Panel upheld the preliminary ruling that because the U.S. was not mandated to not return duties when the WTO finds U.S. determinations flawed, the U.S. measure was not WTO-inconsistent. If the U.S. applies the measure by refusing to refund duties determined to be WTO-illegal, Canada could potentially launch a new challenge (*ibid.*).

Canada made a request for review of the U.S. final finding of dumping on September 13, 2002. Canada alleges that Commerce (a) improperly initiated its anti-dumping investigation; (b) applied several WTO-inconsistent methodologies in its investigation; and (c) did not establish the proper product scope for the investigation (*ibid.*).

The WTO Panel charged with reviewing the Byrd Amendment issued its report September 16, 2002. The Panel found that this U.S. law was inconsistent with U.S. WTO commitments because the law required U.S. customs to distribute duties to affected U.S. industries (*ibid.*). The U.S. appealed this determination, and on January 16, 2003, the Appellate Body upheld the Panel decision.

The WTO Panel reviewing Commerce’s preliminary affirmative issued its final report September 27, 2002. The Panel determined that (a) provincial stumpage programs are indeed a

“financial contribution” but that the U.S. erred in using a cross-border comparison to show how the contribution provides “benefits” Canadian producers, (b) the U.S. erred in its belief that the alleged financial contribution would also be passed downstream, (c) U.S. interim bonding requirements were illegal, and (d) the U.S. was obligated to conduct the expedited reviews that Canadian producers had requested (DFAIT, On-Line j).

On December 20, 2002, Canada took the initial step to challenge the final ITC determination that Canadian softwood lumber threatens to materially-injure U.S. producers. Canada argues that the ITC decision was based on allegations, is inconsistent with WTO CVD and AD rules, and failed to consider all factors necessary to determine that there exists a threat to injury.

The possibility remains that Canada and the U.S. could still come to a new agreement on softwood lumber. It is not clear why Canada has softened its stance in recent months, but Canadian softwood exporters may now be feeling the impact of the duties on their pocket books. On January 7th, 2002, U.S. Under-Secretary, Grant Aldonas, unleashed a proposal to resolve the looming dispute (Bureau National Affairs, 2001). The deal would impose an interim export tax that would be phased-out if Commerce determined in “changed circumstances” reviews that more market-based forest management regimes have been implemented (ibid.). This proposal has formed the basis of discussions between Ottawa and Washington, B.C. and Washington, and Quebec and Washington. In the meantime, Canada continues to pursue the NAFTA and WTO legal challenges mentioned above.

Part II: The Indicators

(a) Market Share

When the U.S. launched its fourth CVD case and AD case in 2001 (“CVD-AD 4”), Canadian softwood lumber producers held 34.7% of the U.S. market. This was 7.1% more than

was the case when the U.S. launched its previous CVD investigation on softwood lumber ten years back and was a change of +1.3 standard deviations. Interestingly, this 34.7% Canadian share was only 1.2% more than was the case at the outcome of CVD 3 in 1994. From 1991-2001, U.S. producers' share of the U.S. softwood lumber consumption fell by 8.3%, or -1.6 standard deviations from the mean over the period of 1972-2002. Certainly the lion's share was won by Canadian producers, but other countries are now slowly, but surely building their way into the U.S. market. This means that the U.S. can no longer afford to focus its attention on Canadian softwood lumber producers as the sole source of U.S. softwood producers' problems. Taken together, the increase in Canadian market share, and new international sources of competition, seem to provide reasonable grounds for U.S. concerns about foreign sources of softwood lumber competition.

(b) State of the U.S. Economy

At the time when the U.S. launched CVD 4 in April 2001, which was just a few weeks after the SLA expired, U.S. economic activity remained near all-time highs. However, the U.S. economy was beginning to show signs of declining GDP growth. For example, GDP expanded 4.2% from US\$8.73 trillion in Q1 1999 to US\$9.10 trillion Q1 2000, but expanded only 2.5% to US\$9.33 trillion in Q1 2001 (U.S. Department of Commerce, January 2002).²⁵

Unemployment in the U.S. lumber and lumber products sector was 6.3% when the CVD and AD investigations were launched in 2001. This was well below the average 8.1% rate of unemployment from 1976-2002.

²⁵ Calculated from U.S. Department of Commerce, Bureau Economic Analysis (BEA) Gross Domestic Product (GDP) data.

The overall rate of unemployment in the U.S. remained near all-time lows with an annual rate of 4.8% in 2001.²⁶ This was significantly lower than the 6.4% average rate of unemployment from 1976-2002.

(c) Uncertainty in negotiations or certain bilateral sectors of trade to which the U.S. has significant stakes?

The U.S. was involved in a number of bilateral and multilateral trade and investment negotiations when CVD-AD 4 was launched. The Bush Administration made WTO services and agriculture negotiations a priority, and to a lesser extent comprehensive negotiations towards a Free Trade Area of the Americas (FTAA). Given that Canada and the U.S. hold similar positions on these initiatives, WTO and FTAA negotiations will likely have little or no impact on resolution of the bilateral softwood lumber dispute.

The mounting energy shortage in the U.S. has the potential to be brought to the forefront of negotiations. For example, in August 2001, Canadian Trade Minister, Pierre Pettigrew, was quoted in the context of the softwood lumber dispute:

I am inviting Americans to think carefully about their relationship with Canadians. We have heard what they are saying on the energy front, and I am saying it is up to them to realize that keeping us in a good mood is a good idea (National Post Online, August 2001).

Pettigrew may have been referring to the proposed Northern Pipeline Development project — a project that would deliver ample supplies of natural gas from the Canadian North to the U.S. mainland. The proposed project is extremely important to the U.S., and if Ottawa were to block the project, this would be a significant setback to the Administration's efforts to provide for the future energy demands of Americans. The Administration is, however, fortunate, in the sense that it would be difficult for Ottawa to block development of the Northern Pipeline Project as a way of gaining leverage in softwood lumber negotiations. This is the case for two reasons. First,

²⁶ However, there was some indication at the time that the U.S. economy was headed for some more difficult, if not less prosperous times. Indeed, in 2002, the overall rate of unemployment was 5.8%.

building the pipeline would potentially create a lucrative amount of business activity for the Canadian economy. With such significant economic potential in the project, corporate interests will make life very difficult for any government that stands in the way of the project. Second, natural resource management falls under the jurisdiction of provincial and territorial governments in Canada. Ottawa retains the right to involve itself in the matter, given that the proposed project is an international trade issue, the pipelines cross provincial boundaries, and the federal government has jurisdiction north of 60° latitude. At the same time, Ottawa could cause significant tension with the provinces by blocking an initiative that the provinces support.

(d) Level of Protectionist Sentiment in the U.S.

In 2001, the U.S. initiated a total of 95 CVD and AD cases against its trading partners (18 CVD, 77 AD).²⁷ This is a “very high” number compared to the average 52 cases launched annually from 1972-2002 and is +1.5 standard deviations from the mean.

In that same year, there were 8 WTO cases launched against the U.S. Given an average 5.5 cases was initiated against the U.S. annually from 1972-2002 and a standard deviation of 4.5 for the data set, this was a relatively “high” number of disputes (+0.7 standard deviations). Taken together, these two data sets indicate that U.S. protectionist sentiment was in the “high-very high” range when CVD-AD 4 was launched.

Summary

When the U.S. finally grasped that it would be difficult to secure a new agreement with Canada for the period following the SLA, it launched CVD-AD 4. Canada has launched several legal challenges to the U.S. subsidy and dumping determinations through both NAFTA and

²⁷ Such a copious number of trade challenges may have backfired on the U.S. The U.S. was forced to include a review of its domestic trade laws to secure an agenda for a new round of negotiations at the WTO Ministerial in Qatar (November 2001). This is something that the U.S. had been adamantly opposed to for decades as a GATT/WTO member. At the same time, this concession should by no means be interpreted as an admission by the U.S. that its trade laws favour U.S. firms.

WTO dispute settlement mechanisms. This includes several challenges to the consistency of certain U.S. laws with U.S. WTO commitments. Thus far, the WTO has found provincial export restraints WTO-consistent: that provincial stumpage programs can be considered subsidies, but that cross-border comparisons for calculating the level of subsidization may not be used; that the U.S. Byrd Amendment, which channels duties collected back to affected producers, is illegal; and that the U.S. measure which directs customs not to refund duties when the WTO finds Commerce determinations flawed, is WTO-consistent because it does not mandate for this response.²⁸

When the U.S. launched its fourth CVD case and AD case in 2001 Canadian softwood lumber producers held a slightly higher share than was the case at the outcome of CVD 3 1994 (i.e. a negotiated deal called the SLA). Economic activity in the U.S. remained near all-time highs, but the economy was beginning to show signs of slowing growth in GDP. Unemployment in the U.S. lumber and lumber products sector was well below the average annual rate from 1976-2002. The overall rate of unemployment remained near all-time lows, but there were signs of more difficult times to follow. The U.S. was involved in a number of bilateral and multilateral trade and investment negotiations, including the FTAA, WTO agriculture and services negotiations. The U.S. was also concerned about its growing energy shortage at the time. However, it was, and continues to be, difficult for Ottawa to block projects such as the Northern Pipeline Project, to gain leverage in softwood lumber negotiations. This is the case because of the economic activity these projects have the potential to generate. Ottawa would also cause significant tension with the provinces, should it block initiatives that the provinces support. In 2001, the U.S. initiated a very high number of CVD and AD cases relative to the number initiated over the period. In that same year, there were an average number of WTO cases

launched against the U.S. Taken together, these two measures indicate that U.S. protectionist sentiment was in the range of “high-very high” when CVD-AD 4 was launched.

²⁸ Given that there are several NAFTA and WTO pending, and that Canada and the U.S. are at the same time engaged in negotiations, it is difficult to determine what impact the CVD and AD findings will ultimately have on the softwood lumber trade.

Chapter Seven: Analysis, Conclusion

The discussion has provided a chronological account of the events that transpired in each of four softwood lumber disputes, described Canadian and U.S. trade policy-making processes and revealed some concrete information about the political and economic climate that existed when each dispute was launched. The analysis has shown that, contrary to the initial thesis statement, the set of political and economic indicators employed in the thesis does not explain the varying outcomes in the four disputes. Some fundamental questions remain about why the first CVD case was the only dispute that culminated in a “no subsidy” finding.

Clearly, the interests of Canadian producers were best served when Commerce found no subsidies in CVD 1. Canadian softwood lumber exports were unaffected by the outcome/determination — no restrictions, taxes or duties were imposed following the challenge. With the three subsequent disputes (CVD 2, CVD 3, CVD-AD 4), Canadian softwood lumber exports were subject to taxes, duties, and/or other limitations. It is impossible to measure the extent that market share, the state of the U.S. economy, the possibility of trade uncertainty and level of U.S. protectionist sentiment impacted Canadian and U.S. strategic directions in each dispute. It is certainly feasible to analyze the extent that each of the indicators relate to the outcome of the disputes.

What the Indicators Contribute to Understanding the Softwood Lumber Dispute

a) Market Share

At the time when CVD 1 was initiated, which was again the only dispute that clearly culminated in favour of Canadian softwood exporters, Canadian producers were winning U.S. producers’ market share. In theory, this trend could have motivated Commerce to find affirmatively, but clearly this did not happen. In fact, there are no intuitive trends that can be said of the market share indicator (see: Figures 1- 6). When both CVD 1 (1982) and CVD 2

(1986) were initiated, U.S. softwood producers' share of the U.S. market was on the decline, while Canadian producers' share was on the incline. Yet CVD 1 resulted in a no subsidies finding, and the latter a preliminary subsidies finding. Nor is there any logical trend for the two disputes that ended in negotiated settlements – CVD 2 and CVD 3. U.S. producers' share was on the decline when CVD 2 was launched (1986), on the incline when CVD 3 (1991) was launched, yet both disputes concluded with negotiated settlements. It is interesting to find that while total U.S. softwood consumption was on the decline when CVD 3 was initiated, U.S. producers' share of the U.S. market was actually on the incline. In other words, U.S. producers gained market share, even when there was a relatively small appetite for lumber. This of course avoids two important considerations – the domestic and international supply of softwood lumber at the time.

Figure 1. Canadian Softwood Lumber Producers' Share of U.S. Market in Year Softwood Lumber Dispute Launched

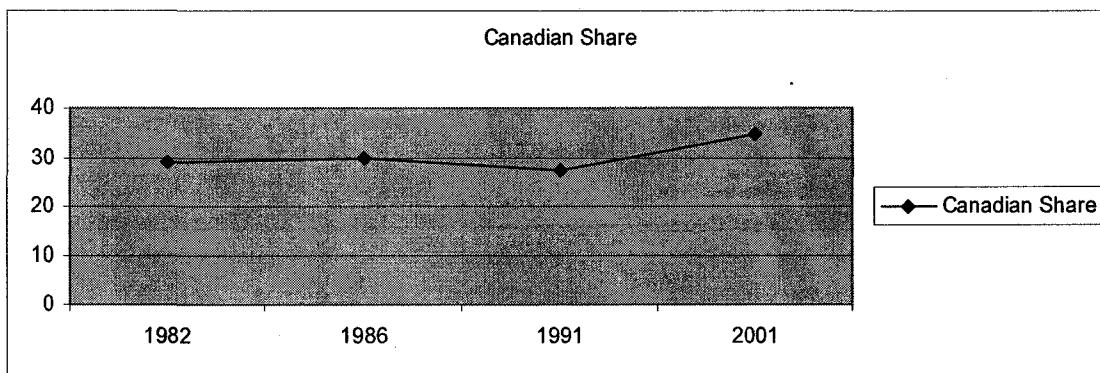


Figure 2. U.S. Softwood Lumber Producers' Share of U.S. Market in Year Softwood Lumber Dispute Launched

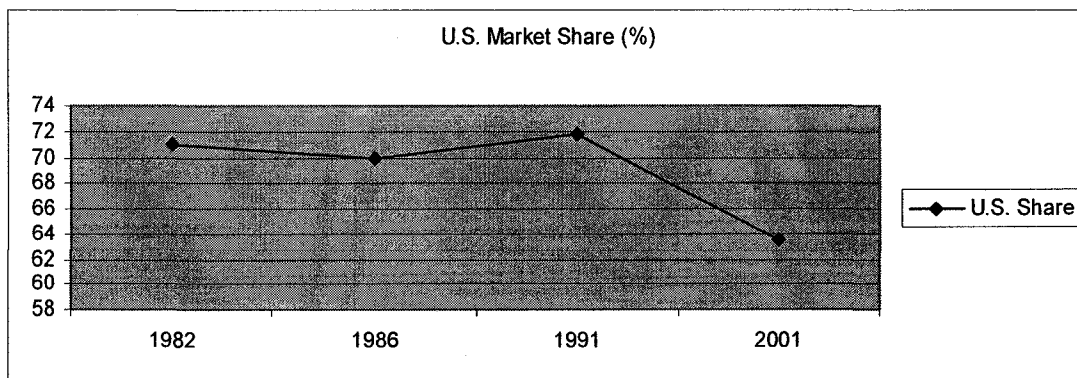


Figure 3. Other Countries - Producers' Share of U.S. Market - in Year Softwood Lumber Dispute Launched

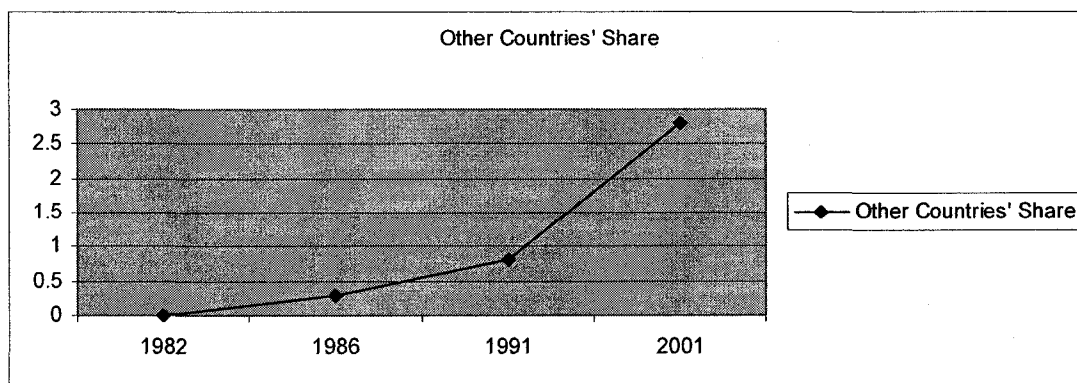


Table 2. Summary of Indicators and Outcomes for Softwood Lumber Disputes

	CVD 1 October 1982	CVD 2 May 1986	CVD 3 October 1991	CVD 4 April 2001	AVERAGE 1979 ¹ - 2002	STANDARD DEVIATION FULL DATA SET
MARKET SHARE²	↑	↑	↓	↑		
Canadian Producers' Share (%) of U.S. Softwood Lumber CONSUMPTION ³	29.0	29.7	27.6	34.7	31.2	
Standard Deviation from Mean (1979-2002)	-0.8	-0.6	-1.4	1.3		2.6
U.S. Producers' Share of U.S. Softwood Lumber CONSUMPTION⁴	↓	↓	↑	↓		
	71.0	70.0	71.8	63.5	72.2	
Standard Deviation from Mean	-0.3	-0.5	-0.4	-2.1		4.2
Other Countries' Share of U.S. Softwood Lumber CONSUMPTION⁵		↑	↓	↑		
	0.0	0.3	0.2	2.6	2.6	
				Top Exports to U.S. after Canada: Brazil Chile New Zealand Germany		
Standard Deviation from Mean	-0.7	-0.4	-0.8	0		3.1

¹ Accurate market share data only available from 1979.

² Development of this table required use of data from multiple sources. Canadian, U.S. and Other Countries' shares of U.S. Consumption do not add up to exactly 100%.

³ British Columbia. Ministry of Forests. Economics and Trade Branch. Canadian Share of the U.S. Softwood Lumber Market.

⁴ British Columbia. Ministry of Forests. Economics and Trade Branch. Shares in United States Apparent Consumption of Softwood Lumber.

⁵ Ibid, and U.S. Census Bureau (2004). TSUSA 20212 - 20230 SOFTWOOD LUMBER, ROUGH, DRESSED, OR WORKED. Mary.E.May@census.gov

Volume U.S. Softwood Consumption in millions board feet (mbf) ⁶	↑ 31,173 -2.0	↑ 43,922 -0.2	↓ 41,896 -0.5	↑ 54,409 1.3	45,073	6,988
Standard Deviation From Mean						
STATE OF U.S. ECONOMY	Bad Recession	Average-Good	Recession	Very Good	N/A Qualitative Measure	N/A Qualitative Measure
UNCERTAINTY IN TRADE FOR THE U.S.	None	FTA	NAFTA, GATT-WTO Uruguay Round	WTO Round, FTAA, Growing Energy Shortage	N/A Qualitative Measure	N/A Qualitative Measure
LEVEL OF PROTECTION IST SENTIMENT IN THE U.S.	High	Very High-Extremely High	High	Very High	N/A Qualitative Measure	N/A Qualitative Measure
OUTCOME	Commerce finds no subsidies-Canadian softwood lumber exports continue unaffected	Canada, U.S. negotiate MOU, 15% tax imposed on Canadian softwood lumber exports	U.S. terminates CVD petitions, Canada drops GATT challenge, Canada and U.S. negotiate SLA, U.S. refunds bonds	U.S. imposes CVD & AD duties, Canada launches NAFTA & WTO disputes, negotiations pending		

b) State of the U.S. Economy

If there was any discernible relationship between the state of the U.S. economy and the outcome of softwood lumber disputes, CVD 1 would have been a logical place to find it, because the U.S. was enduring a severe economic recession when the dispute was launched. In other

⁶ Random Lengths. Compilation of market statistics data Annual Yearbooks. janna@randomlengths.com.

words, if there was any merit to the argument that the U.S. Administration finds what it wants to find in its CVD and AD investigations, 1982 would have been the time for alleged number crunching. Far from this, this thesis found no such relationship for this particular indicator.

c) Uncertainty in Trade for the U.S.

There were no major outstanding trade matters between Canada and the U.S. when CVD 1 was launched. Therefore, in this one dispute where Canadian producers were clear victors, it is impossible to analyze whether the presence of trade uncertainty (at launch of a dispute) relates to the outcome of that dispute. At most, one can deduce that when the U.S. had nothing else at stake in CVD 1, Canadian producers happened to do well.

When CVD 2 was launched, FTA negotiations were taking place. At launch of CVD 3, NAFTA and GATT/WTO Uruguay Round negotiations were taking place. In both instances, there were no looming trade disputes or negotiations that involved both parties and that the U.S. had particular vested interests in.

When CVD 4 was launched, there was, and remains to be, one such outstanding trade matter — energy. Yet, despite the fact that Canada is one of the largest sources of U.S. energy, Canada has done absolutely nothing to use this issue as a possible means of gaining leverage on softwood lumber. Therefore, as the case history suggests, even when there are outstanding trade matters in which the U.S. holds weighted stakes, this bears no marked influence on the outcome of that dispute.

d) Protectionist Sentiment in the U.S.

There are possible intuitive patterns between the level of U.S. protectionist sentiment at the time when each dispute was launched and the outcome of each dispute. That is, Canadian

softwood producers may be more likely to secure a favourable outcome when U.S. protectionist sentiment is low, in relative terms, at the time when a dispute is launched.

The “no subsidies” outcome of CVD 1 was very much positive for Canadian producers. Again, nothing had changed so as far as Canadian softwood lumber exporters were concerned, it was business as usual. This was the case despite the indication of a “high” level of U.S. protectionist sentiment.

The outcome of CVD 2 was unsettling for Canadian industry because Commerce had so recently dismissed U.S. claims outright, but then produced an affirmative preliminary finding (of subsidies) in its new investigation. The negotiated outcome that followed certainly created a logical pattern, given the “very high” relative level of protectionist sentiment in the U.S. when the dispute was launched. This outcome, other factors of possible relevance aside, should fall conceptually between a no subsidies/dumping determination and an affirmative finding.

When CVD 3 was initiated, U.S. protectionist sentiment was “high” and again the final outcome of the dispute was a negotiated settlement. Again, this outcome should fall conceptually between a no subsidies or no dumping determination and an affirmative finding – other factors aside.

When CVD-AD 4 was initiated, the level of protectionist sentiment in the U.S. had increased one half of one interval to “high-very high”. It presently appears that the U.S. may refund duties it has already collected from Canadian softwood lumber producers, as it has been directed to do by the WTO dispute settlement panels. At the same time, the possibility still exists that the dispute could culminate in a negotiated settlement.

Thus, there does not appear to be a logical relationship between the level of U.S. protectionist sentiment and the outcome of a softwood lumber dispute. Protectionist sentiment was strong in each dispute, as evident from the “high” to “very high” qualitative values. Yet there is no evidence that an affirmative, negative or negotiated outcome is any more likely when U.S. sentiment falls at or between either of these intervals.

Figure 4. Total Countervailing Duty and Anti-Dumping Cases Initiated by the U.S. Against All Other Countries Annually 1972-2002

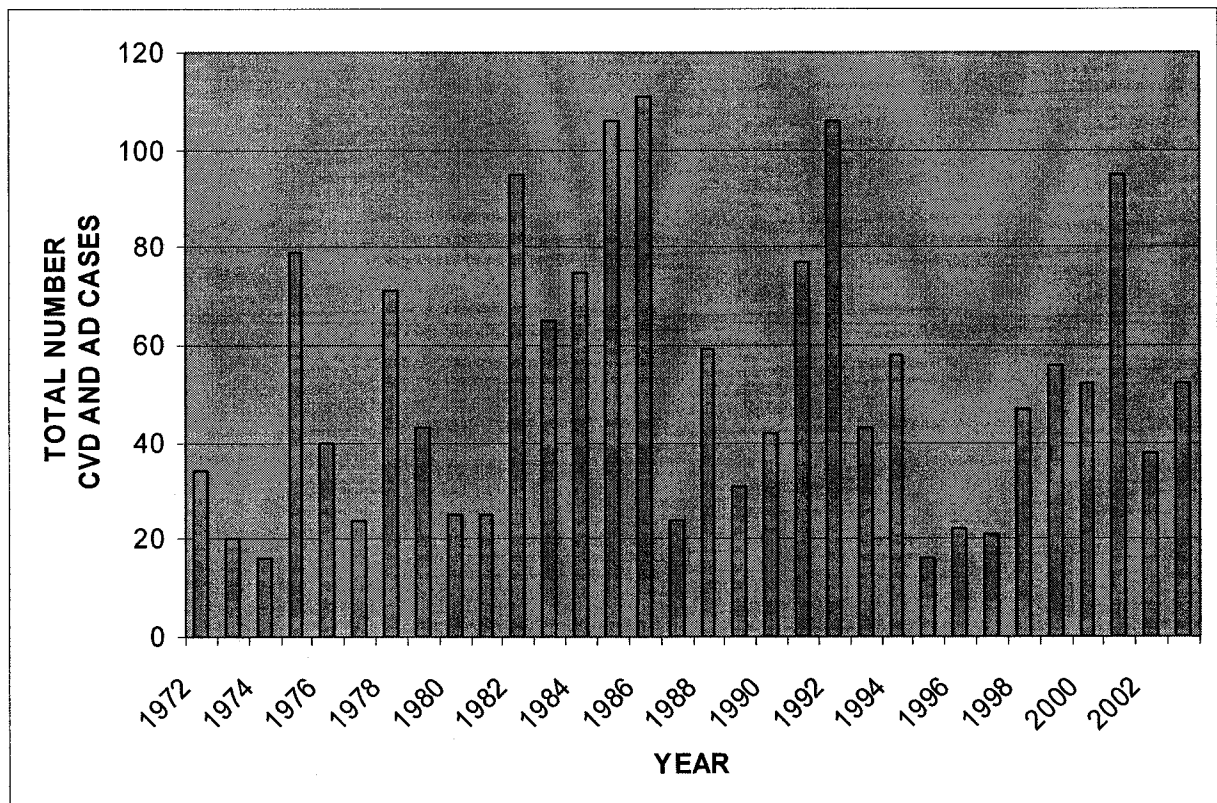
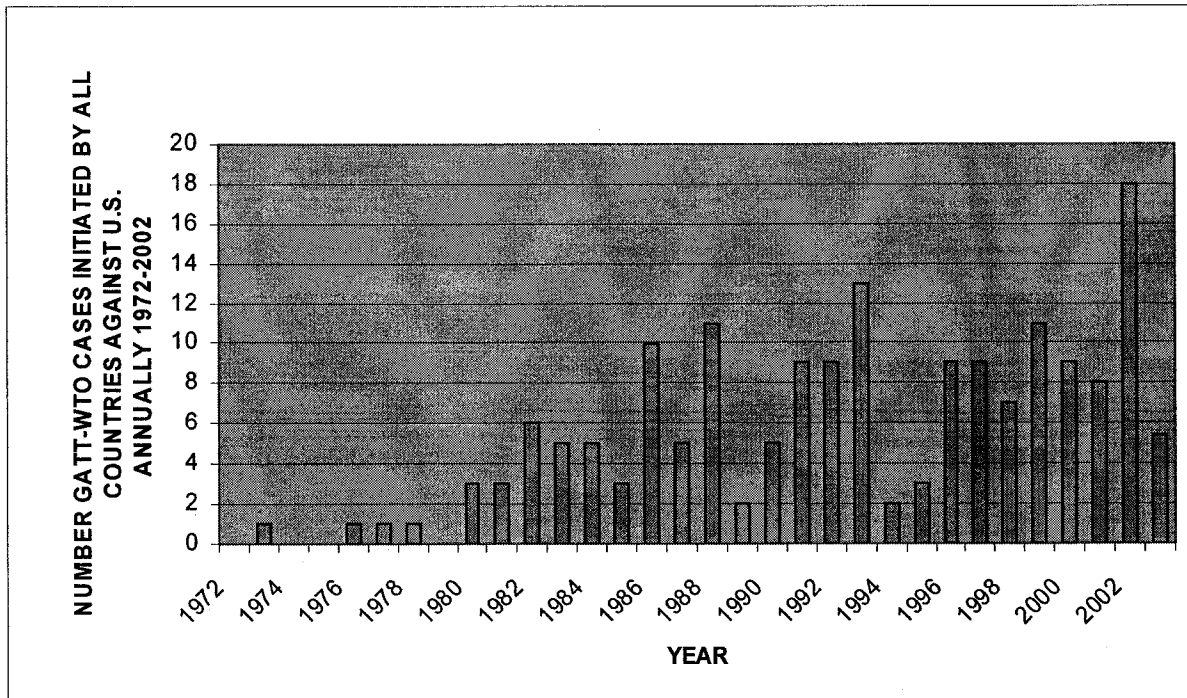


Figure 5. Total GATT-WTO Cases Initiated Against the U.S. by All Other Countries Annually 1972-2002



This thesis has shown that it is not enough to package the outcome of softwood lumber disputes as having positive, negative or mixed benefits for Canadian softwood lumber exporters.

Market share may be the most accurate measure of how Canadian softwood lumber producers fared from dispute-to-dispute. However, there were no logical trends found in terms of market share leading up to the initiation of a CVD and/or AD case and the outcome of that dispute. For example, while U.S. producers' share of the U.S. market was on the decline when CVD 2 was initiated, the reverse was true for CVD 3, yet both culminated in negotiated settlements with mixed implications for Canadian producers.

Attempting to make sense of the relationship between the state of the U.S. economy and the outcome of that dispute is equally complicated. For example, one cannot conclude that when the U.S. economy is weak at the time when a dispute is launched, the outcome tends to be

negative for Canadian producers (i.e. subsidies/dumping found and duties charged on U.S.-bound lumber). It is as difficult to assess the probability of reaching a positive, negative, or mixed outcome when the U.S. economy is strong when a dispute is launched. Canada could have, or at least attempted to use its access to energy as a means of gaining leverage in softwood lumber CVD-AD 4, but it chose not to do so.

The analysis has shown that there are no discernible relationships between the indicators examined and the outcome of disputes. Yet this is not because the indicators selected are implausible or immeasurable. The basic explanation here is that the outcome of softwood lumber disputes cannot be sufficiently explained with only these four indicators. In retrospect, one will be hard pressed to find one set of political-economic indicators that can be employed to wholly explain the varying outcomes.

e) Implications for Future Research

There are a range of other indicators that could have been examined such as “trade balance”. For example, can Canada even retaliate against U.S. duties when running a large trade surplus, given that more sectors would lose than gain from such a policy? Another option was to compare mean “value of softwood lumber exports” from Canada to the U.S. before the launch of each CVD case, with the mean value of exports after the treatment. This indicator would examine whether the U.S. price of softwood lumber increased following the launch of a dispute. If so, the U.S. could, in theory, be more inclined to launch investigations. The “volume of softwood lumber exports” from Canada to the U.S. could have looked at whether the U.S. is more inclined to negotiate a resolution when importing a relatively lower volume of lumber from Canada. Yet, neither the mean value nor volume of softwood lumber exports are as informative

to Canada and the U.S. as is market share — the best measure of how well Canadian softwood exporters are faring in U.S. markets.

Given that many CVD and AD disputes span prolonged periods of time, it may have made more sense to examine the indicators at a time closer to the outcome of each dispute. The difficulty in structuring an analysis in this manner is that disputes tend to follow their own timeframes within broad statutory guidelines. One possibility would be to examine the indicators at the point when a preliminary subsidy or dumping determination is made. The problem with this method is that there are not always final determinations in disputes — both the second and third disputes are cases in point.

When CVD-AD 4 concludes it would be worthwhile to compare Canadian producers' market share at the time when each dispute was initiated, to the share Canadian producers hold at the outcome of each dispute. The rationale for this is that when it comes down to it market share is what really matters to both Canadian and U.S. softwood lumber producers. Both sides are ordained to employ tactics that will protect their existing U.S. market share and provide opportunity for growth. These political and economic tools are presently being employed and there is no reason to suspect that this will ever change. This market share intelligence can provide new information on how Canadian softwood producers fare in these disputes in both the short and long-term.

The possibility also exists that it may simply be impossible to predict the outcome of softwood disputes in any calculable manner, given the complexity and cross-cutting nature of many potential variables.

Conclusion

This thesis set out to test that softwood lumber disputes are highly politicized and that certain economic and political indicators may help to explain the outcome of disputes.

The indicators provide some interesting information about the political and economic conditions surrounding each of the disputes. It has, however, been a challenge to find logical relationships between the indicators and the outcome of softwood lumber disputes.

It is not easy to determine how the current CVD and AD duties are affecting Canadian softwood lumber producers, or how its bottom line might be affected in the future. Thus far, many Canadian softwood lumber producers have responded to U.S. duties by increasing output. The intent may have been to absorb short-term financial gains, eat the cost of the U.S. duties in order to make a statement to the U.S. that duties are not the answer, and/or maintain U.S. market share pending NAFTA and WTO dispute settlement deliberations. Given that Canada has been exporting higher volumes of softwood lumber to the U.S. and generating less revenue overall, market share may well be the primary motive.

The U.S. strategy may be that a financial threshold exists for Canadian softwood lumber producers and that, at some point, Canadian exporters will be unable to continue absorbing the cost of the U.S. duties. This circumstance would generate significant leverage for the U.S. and could force Canada to concede to some longstanding, fundamental U.S. demands for provincial forestry reform.

The U.S. has on a number of occasions put forward proposals to subject Canadian lumber to interim export taxes/duties, which would be reduced or eliminated, subject to U.S. changed circumstances reviews of provincial forestry reforms. This would materialize the primary objective of U.S. softwood lumber producers.

This thesis has filled several knowledge gaps on softwood lumber and has, in the process, generated a number of important questions that could be addressed in subsequent research. For

example, what other explanations and/or indicators could be used to account for disparities in the outcome of softwood disputes? The analysis has shown that, contrary to the initial hypothesis, the indicators do not necessarily contribute a logical explanation for predicting the outcome of disputes.

The analysis has shown that resolution of the current dispute may be more closely related to the extent that Canadian softwood lumber producers are able to continue absorbing duties, and how the remaining WTO and NAFTA appeals conclude, than the four political-economic indicators examined.

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