UNITED STATES-CANADA FREE TRADE AGREEMENT
ARTICLE 1904 BINATIONAL PANEL REVIEW
U.S.A.-92-1904-01

IN THE MATTER	**Before:**	**Richard G. Dearden (Chair)**
CERTAIN SOFTWOOD LUMBER		**Lawson A.W. Hunter, Q.C.**
PRODUCTS FROM CANADA		**Morton Pomeranz**
		Michael Reisman
		Paul Weiler

DECISION OF THE PANEL
(May 6, 1993)

Appearances:

M. Jean Anderson, Bruce H. Turnbull, Douglas A. Nave, David W. Oliver, and Deborah E. Siegel, on behalf of the Government of Canada.

Lawrence A. Schneider, Claire E. Reade, Michael T. Shor, and Matthew Frumin, on behalf of the Government of Alberta.

Homer E. Moyer, Grant D. Aldonas, Philip J. Ferneau, Susan Ginsburg, John E. Davis, Stuart E. Benson, James B. Altman, Daniel M. Flores, Peter B. Miller, and Angela Lykos, on behalf of the Government of British Columbia.

Mark S. McConnell, Lynn G. Kamarck, Deanna Tanner Okun, and Leslie A. Delagran (Economist), on behalf of the Government of Ontario.

Elliot J. Feldman, Michael A. Hertzberg, Matthew J. Clark, and Jonathan C. Cahn, on behalf of the Gouvernement du Québec.Charlene Barshefsky, W. George Grandison, John R. Labovitz, Richard Diamond, and Jeffrey A. May, on behalf of the Canadian Forest Industries Council and Affiliated Companies.

John B. Rehm and Munford P. Hall, on behalf of MacMillan Bloedel Limited.

Randolph J. Stayin, Mark J. Andrews, and David Lubitz, on behalf of the Québec Lumber Manufacturers' Association.

John E. Corrett III, James A. Valeo, Thomas O. Gormand, and John R. Coogan, on behalf of Donohue, Inc.

Richard L. Cys, Edward B. Cohen, and David W. Tremaine, on behalf of J.D. Irving Limited.

Craig L. McKee, Gary N. Horlick, and Eleanor C. Shea, on behalf of Noranda Forest, Inc.

Alan W. Wolff, Michael H. Stein, Robert Griffen, and John Ragosta, on behalf of the Coalition for Fair Lumber Imports.

William D. Hunter, Craig Giesze, Joan MacKenzie, Marguerith Trossevin, and Jeffrey Lowe, on behalf of the Investigating Authority.

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I. INTRODUCTION

This Panel was constituted pursuant to Article 1904.2 of the *Canada-United States Free Trade Agreement* ("*FTA*") to review the final affirmative countervailing duty determination ("*Final Determination*") of the International Trade Administration, U.S. Department of Commerce ("Commerce"), regarding certain softwood lumber products from Canada.[1] The *Final Determination* was challenged by a number of government and private parties from Canada, specifically the Government of Canada, the provincial governments of Alberta, British Columbia, Manitoba, Ontario, Québec and Saskatchewan, the territorial governments of the Northwest Territories and the Yukon, the Canadian Forest Industries Council (and affiliated companies), the Québec Lumber Manufacturers' Association ("QLMA"), and the Canadian Lumbermen's Association located in Québec ("Canadian Complainants"). One Canadian company appeared before the Panel, namely, Macmillan Bloedel of British Columbia. In addition, the Coalition For Fair Lumber Imports ("Coalition") filed a complaint concerning a number of findings made by Commerce in the *Final Determination*.

Counsel for the parties to this proceeding have raised many serious and complex issues regarding the validity of the *Final Determination* issued by Commerce. The Panel is grateful for the detailed written briefs filed by the Parties and the candid and helpful submissions made by counsel during the two days of oral argument held in Washington on February 11-12, 1993.

Set out below is the background to these proceedings, and thereafter the Panel's analyses of its jurisdiction, the standard of review, Commerce's decision to countervail certain stumpage programs and log export restrictions, as well as decisions governing several other issues.

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[1] 57 Fed. Reg. 22,570 (May 28, 1992).

II. BACKGROUND

For context, the Panel summarizes below Commerce's consideration of the importation of Canadian softwood lumber products into the United States during the past ten years and sets out the procedural history of these proceedings.

A. Lumber I

The *Final Determination* under review is the end result of the third in a series of Commerce investigations of Canadian softwood lumber imports. On October 7, 1982, Commerce received a countervailing duty ("cvd") petition from the U.S. Coalition for Fair Canadian Lumber Imports ("Coalition").[2] In its petition, the Coalition complained that both the federal and provincial governments in Canada subsidized the production of certain softwood lumber products exported to the U.S., principally through the provision of "stumpage" to Canadian producers at rates said to be administratively set and artificially low.[3] Commerce commenced a cvd investigation on October 27, 1982.

On May 31, 1983, Commerce issued a final negative determination, finding *inter alia* that stumpage programs provided no subsidy to Canadian softwood lumber producers which was countervailable under U.S. law. Analysing the stumpage programs under 19 U.S.C. § 1677(5)(B)(ii), Commerce concluded that stumpage rights were neither provided to a "specific enterprise or industry, or group of enterprises or industries" within the meaning of the cvd statute nor were the stumpage

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[2] Certain Softwood Lumber Products from Canada, 48 Fed. Reg. 24,159 (1983) ("Lumber I").

[3] "Stumpage programs" constitute the system by which individuals and enterprises acquire rights from the Crown in right of the province to cut and remove standing timber from Crown lands. The vast majority of public forests in Canada are owned by provincial governments. Under the *Constitution Act, 1867*, the provinces bear the responsibility for managing and administering these "Crown" forests.

rights "specific" under Commerce's specificity test. Commerce also concluded that stumpage was not provided at "preferential" rates within the meaning of the *Tariff Act of 1930*.[4]

B. Lumber II

On May 19, 1986, Commerce received a second cvd petition from a reconstituted Coalition for Fair Lumber Imports.[5] The Coalition's principal allegation was again that the stumpage systems of the provinces of Alberta, British Columbia, Ontario and Québec constituted countervailable subsidies. The petition claimed to have new evidence that government policies limited the use of stumpage programs, and alleged that the applicable law had changed since Lumber I. Commerce commenced a second cvd investigation.[6]

Following an affirmative injury determination by the ITC, Commerce published its preliminary determination in Lumber II wherein it found that Canadian stumpage systems conferred a subsidy upon Canadian lumber producers.[7] Rejecting its finding in Lumber I that stumpage was used by "wide-ranging and diverse industries", Commerce found that the provincial stumpage systems were "specific" within the meaning of the cvd statute.[8] Commerce also found that the governments had exercised discretion in their administration of the stumpage programs. With respect to the preferentiality of stumpage rates, Commerce relied on its *Preferentiality Appendix*, first referenced in its decision in Carbon Black from Mexico.[9] Concluding that its preferred reliance on competitively bid sales of stumpage as the benchmark for measuring price discrimination was unavailable on the

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4 48 Fed. Reg. 24,159 (1983) at 24,167.

5 51 Fed. Reg. 21,205 (1986) ("Lumber II").

6 51 Fed. Reg. 21,205 at 21,207.

7 Certain Softwood Lumber Products from Canada, 51 Fed. Reg. 37,453 (1986).

8 51 Fed. Reg. 37,453 at 37,456.

9 51 Fed. Reg. 37,453 (1986) at 37,457.

facts, Commerce settled upon the third alternative in the *Appendix*, the government's cost of producing the good (timber) as the appropriate measure of preferentiality. Commerce's calculation indicated a short-fall in provincial revenue, and therefore found preferential treatment. Commerce determined that the benefit attributable to Canadian stumpage systems was approximately 14.5% *ad valorem*.[10]

C. Memorandum of Understanding

On December 30, 1986, the United States and Canada entered into a Memorandum of Understanding ("*MOU*") concerning softwood lumber. Pursuant to the terms of the *MOU*, the Government of Canada agreed to collect a 15% charge on exports of softwood lumber to the United States, which charge could be reduced or eliminated for provinces that instituted replacement measures, *e.g.* increasing their stumpage fees. In return, the Coalition withdrew its petition and Commerce terminated the countervailing investigation, declaring the preliminary determination in Lumber II to be "without legal force and effect".[11]

On December 16, 1987, the *MOU* was amended. The *Amendment to the MOU* eliminated the export charge for British Columbia's softwood lumber exports on the basis of replacement measures to be enacted by the provinces. The *MOU* also expressly exempted the Atlantic provinces (New Brunswick, Newfoundland, Nova Scotia and Prince Edward Island) from the payment of the 15% export charge, apparently in recognition of the dominance in those provinces of market-determined rates for government-provided stumpage.[12]

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[10] 51 Fed. Reg. 37,453 at 37,457. Note that the total subsidy rate was 15% *ad valorem* due to the other Canadian subsidy programs.

[11] Certain Softwood Lumber Products from Canada, 52 Fed. Reg. 315, amended, Certain Softwood Lumber Products from Canada, 52 Fed. Reg. 2,751 (1987).

[12] *MOU*, at paragraph 3.

For its part, Québec implemented changes to its stumpage system, resulting in a phased reduction in the level of export charges collected under the *MOU*. As of 1991, the U.S. government had acknowledged that these changes were sufficient to reduce Québec's export charge to approximately 3%.

In 1991, the Government of Canada in conjunction with the provincial governments of Alberta, British Columbia, Ontario and Québec, undertook a joint study of the four provincial stumpage systems, applying the "TSPIRS" methodology employed in certain instances by the U.S. Forest Service. The Joint Study was said to have demonstrated that stumpage revenues in all four of these provinces exceeded the provinces' costs of administering their stumpage systems. On this basis, Canada concluded that the *MOU* had served its purpose and gave notice to the United States on September 3, 1991 that it intended to exercise its right to terminate the *MOU* effective October 4, 1991. On October 4, Canada ceased to collect the export charges provided for in the *MOU*.

D. Lumber III

(i) Self-Initiation

On October 31, 1991, Commerce formally self-initiated a third countervailing duty investigation into softwood lumber imports from Canada ("Lumber III").[13]

Commerce prepared and provided a background memorandum from Joseph A. Spetrini, Deputy Assistant Secretary for Compliance, to Eric I. Garfinkel, Assistant Secretary for Import Administration, with regard to Commerce's basis for self-initiating its investigation.[14] Commerce determined that Canada's unilateral termination of the *MOU*, which was the basis for the withdrawal

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[13] 56 Fed. Reg. 56,055 (1991).

[14] Memorandum of J.A. Spetrini to E.I. Garfinkel (Department of Commerce) re: Basis for Self Initiation of Countervailing Duty Investigation: Certain Softwood Lumber Products from Canada (C-122-816) (October 23, 1991), Pub. Doc. No. 3 at 4.

of the cvd petition and the termination of the cvd investigation in 1986, constituted "special circumstances" necessary to self-initiate a cvd investigation.[15] Commerce also concluded that it had evidence of subsidy, material injury, and causation sufficient to warrant the initiation of a formal investigation.

Commerce excluded the four Atlantic provinces from the self-initiated investigation.[16] Commerce stated that the basis for such exclusion was the *MOU*'s exemption of the Maritimes, and thus the lack of "special circumstances" necessary to self-initiate.[17]

In its Reasons for Self-Initiation, Commerce expressly considered whether it should initiate an investigation into the restrictions placed on the export of logs by Canadian federal and provincial government regulations.[18] Commerce concluded that it lacked evidence demonstrating that the restrictions in question had a measurable downward effect on log prices; it acknowledged that theoretically export regulations may limit the export of logs and thereby suppress provincial demand, lowering the price of logs to domestic lumber producers.[19] Commerce invited interested parties to submit evidence that could serve as a basis for launching an investigation into log export regulations.

On November 8, 1991, the Canadian Complainants requested that Commerce designate its investigation "extraordinarily complicated", and extend its deadline for making a preliminary determination for an additional 65 day period.[20] On the same day, Commerce issued its initial questionnaire to the Canadian parties.

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[15] As required by Article 2.1 of the *Agreement on Interpretation and Application of Articles VI, XVI, and XXIII on the General Agreement on Tariffs and Trade* (the *"GATT Subsidies Code"*). See 56 Fed. Reg. 56,055 (1991).

[16] 56 Fed Reg. 56,055 at 56,056-57.

[17] 56 Fed. Reg. 56,055 at 56,057-56,058.

[18] 56 Fed. Reg. 56,055, amended 56 Fed. Reg. 56,058 (1991).

[19] 56 Fed. Reg. 56,055 at 56,057.

[20] In accordance with 19 § U.S.C. 1671 B (c)(1); see Pub. Doc. No. 28.

On November 21, 1991, the Canadian Complainants formally objected to Commerce's decision to self-initiate its investigation, and requested the termination of the investigation.[21] Commerce denied this request on December 5, 1991.[22]

On December 9, 1991, 334 company exclusion requests were filed; the Coalition filed its objections to these requests. On January 17, 1992, Commerce declared it impracticable to investigate all 334 companies for exclusion, and stated it would only investigate 11 companies that produced lumber entirely from U.S. origin logs. Questionnaires were issued to these companies.[23] Commerce subsequently accepted questionnaire responses from additional companies that produced lumber primarily from U.S. origin logs.

In the early part of December, the Coalition filed submissions that log export restrictions in British Columbia, Alberta, Ontario and Québec constituted countervailable subsidies, and requested that Commerce include the export restrictions in its investigation.[24] In support of these allegations, the Coalition submitted *inter alia* two studies: Jay Gruenfeld Associates, "British Columbia Log Price Data Export and Domestic Log Prices, Selected Grades 1984-1990" (November, 1991) ("Gruenfeld Study"); and M. Margolick and R. Uhler, "The Economic Impact of Removing Log Export Restrictions in British Columbia", Forest Economics and Policies Analysis Project (April, 1986) ("Margolick-Uhler Study"). The Canadian Complainants objected to the Coalition's submissions, by correspondence of December 13 and 23, 1991.[25] On December 23, 1991 (formally published on January 6, 1992), Commerce initiated an investigation of the log export regulatory

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[21] Correspondence of Robert C. Cassidy, Jr. to the Honorable Robert A. Mosbacher, Sr.: Pub. Doc. No. 52.

[22] Correspondence of J.A. Spetrini to R.C. Cassidy, Jr.: Pub. Doc. No. 91.

[23] Pub. Doc. Nos. 160 and 161.

[24] Pub. Doc. Nos. 80 and 104.

[25] Pub. Doc. Nos. 100 and 115.

policies of Alberta, British Columbia, Ontario and Québec.[26] On December 24, 1991, Commerce issued its initial questionnaires regarding provincial log export regulations.[27]

On January 6, 1992, Commerce formally declared its investigation to be "extraordinarily complicated" in light of the issues involved in its investigation of provincial log export regulations,[28] and postponed its preliminary determination by 30 days. On February 11, 1992, Commerce announced that it would postpone the release of the preliminary determination until March 5, 1992.[29]

During meetings with Commerce in late February and early March, 1992, Canadian Complainants learned that Dr. William Lange, a U.S. Forest Service economist, had been appointed to Commerce's investigatory team and was to participate in the verification of Canadian Complainants' questionnaire responses. Dr. Lange acted as chief spokesman for the U.S. Coalition for Fair Lumber Imports during Lumber II. On March 3, and again on March 12, Canadian Complainants objected to Dr. Lange's participation in the Department's investigation on the grounds of likelihood of, or potential for, bias.[30]

(ii) Preliminary Determination

Commerce issued a preliminary affirmative countervailing duty determination ("*Preliminary Determination*") in Lumber III on March 5, 1992. In this *Determination*, Commerce found that the stumpage systems in Alberta, British Columbia, Ontario and Québec conferred a weighted average

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[26] Memorandum of J.A. Spetrini to A.M. Dunn (December 23, 1991), Pub. Doc. No. 119 and 57 Fed. Reg. 397 (1992).

[27] Pub. Doc. No. 121.

[28] 57 Fed. Reg. 397 (1992).

[29] 57 Fed. Reg. 4,989 (1992).

[30] Letter from R.C. Cassidy, Jr. et al. to the Hon. Allan M. Dunn (March 2, 1992), Pub Doc. No. 332; Letter from L.M. Shambom to the Hon. Allan M. Dunn (March 12, 1992), Pub. Doc. No. 382.

subsidy of 6.25%. Commerce found as well that the log export regulations in British Columbia conferred a weighted average subsidy of 8.23%. The combined weighted average rate of 14.48% was applied to softwood lumber exports from all jurisdictions other than the Atlantic provinces.[31]

In the *Preliminary Determination*, Commerce found that provincial stumpage programs were "specific" because "only one group of industries ... uses stumpage: the primary timber processing industries, which is comprised of two major industries, the solid wood industry and the pulp and paper industry."[32] Commerce abandoned the `inherent characteristics' test applied in Lumber I, reasoning that Congress had intended the demise of such test by its amendments to the *Tariffs and Trade Act* in 1988.

In finding preferentiality, Commerce determined its benchmark on the basis of the purported differences in the prices charged different stumpage holders by the governments of Alberta, British Columbia and Ontario. With regard to Québec, however, the difference between the prices charged by the government and by private sellers in that province furnished the benchmark.

While Commerce found that log export regulations in Alberta, Ontario and Québec did not confer countervailable subsidies, it did countervail British Columbia's log export regulations on the ground that they had a "direct and discernible" effect upon log prices in B.C.

Commerce preliminarily excluded six companies.

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[31] Certain Softwood Lumber Products from Canada, 57 Fed. Reg. 8,800 (1992).

[32] *Ibid.* at 8,804.

(iii) Final Determination

Following its *Preliminary Determination*, Commerce proceeded to verify the submissions of Alberta, B.C., Ontario, Québec and the Government of Canada. Dr. William Lange participated in the verifications conducted in British Columbia and in Québec.

A two day public hearing was set for the week of April 26 to April 29, 1992.

On April 21, 1992, the Canadian Complainants and the Coalition submitted their case briefs for the hearing. On April 24, the Canadian Complainants registered an objection to the Coalition's inclusion of allegedly new factual information in their brief, specifically the Newport Study and the Flynn-Cox Study (and attachments). On April 27, 1992, the Canadian Complainants and the Coalition submitted their rebuttal briefs. With their rebuttal brief, Canadian Complainants submitted a supplementary analysis by Dr. W.F. Finan which responded to the allegedly new materials.[33] On April 29, 1992, the day the public hearing began, Commerce advised the Canadian Complainants that all briefs would be accepted.

On May 28, 1992, Commerce published its *Final Determination*,[34] finding that the stumpage systems of Alberta, British Columbia, Ontario and Québec conferred a weighted average subsidy of 2.91% on softwood lumber exports. The individual provinces were assessed the following rates: Alberta - 1.25%; B.C. - 3.30%; Ontario - 5.95% and Québec - 0.01%.

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[33] Dr. W.F. Finan, "Evaluation of Relationships between Log Exports and Prices in British Columbia" (April 27, 1992); Pub. Doc. No. 501.

[34] Certain Softwood Lumber Products from Canada, 57 Fed. Reg. 22,570 (1992).

Commerce further determined that British Columbia's log export regulations conferred a subsidy of 4.65% on softwood lumber producers in that province, yielding a weighted average subsidy of 3.60%.

Taken together, Commerce assessed a "country-wide" weighted average rate of 6.51% on softwood lumber exports from all provinces and territories under investigation.

In its *Final Determination*, Commerce confirmed its preliminary finding that the provincial stumpage systems were "specific" to the "primary timber processing industries".[35] Commerce adhered to its conclusion that Congress had precluded the application of an `inherent characteristics' test, but stated that even if it was not precluded, such a test was not required. Commerce also rejected the Canadian Complainants "purposeful government action" test, on the basis that it would put natural resource subsidies beyond the reach of U.S. cvd law, a result said to run contrary to Congressional intent.[36]

With respect to preferentiality of stumpage pricing, Commerce affirmed the benchmarks it applied in its Preliminary Determination, as refined by the results of the verification. Commerce rejected the Canadian Complainants' "market distortion" argument, concluding on the basis of the statute and its legislative history that Commerce is "precluded from measuring the benefit conferred by stumpage programs on the basis of a market distortion analysis, such as the effect of stumpage prices on output".[37] Commerce went on to state, however, that even if such an inquiry was relevant, Canadian Complainants failed to establish that no market distortion could be caused by stumpage programs. Commerce rejected the use of cost as the benchmark, finding no basis for departing from the preferred statutory standard, price discrimination.

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[35] 57 Fed. Reg. 22,570 at 22,583.

[36] 57 Fed. Reg. 22,570 at 22,582.

[37] 57 Fed. Reg. 22,570 at 22,588.

With regard to log export regulations, Commerce reaffirmed its *Preliminary Determination* on the basis of several economic studies, including the Newport Study, an update of the Coalition's Margolick-Uhler Study.

Commerce rejected Québec's request for an exclusion from the investigation on the ground that Québec's subsidy rate was found to be *de minimis*, stating that neither the statute nor Commerce's practice provided for the assessment of specific countervailing duties for political subdivisions.[38] Commerce found that 19 U.S.C. § 1671e(a) requires that it combine an average subsidy rate from all countervailable programs into a single rate and apply that average net benefit to all exports of the class or kind of merchandise subject to the investigation, unless it was determined that certain exporters or producers had significantly different subsidy rates.

Commerce's *Final Determination* excluded 15 companies on the basis that these companies produced lumber exclusively or predominantly from U.S. origin logs. Commerce affirmed its determination that it was impracticable to investigate the remainder of the company exclusion requests and stated that it was under no statutory obligation to investigate.[39] Commerce affirmed that remanufactured products would not be excluded from the determination.

E. The Chapter 19 Panel Review Process

This Panel convened on July 29, 1992 after the timely request for Panel Review by the federal and certain provincial governments in Canada. During September - October, 1992, the Panel was seized of several motions that included:

1. The Coalition's Motion to strike the Panel for lack of jurisdiction;

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[38] 57 Fed. Reg. 22,570 at 22,578-22,580.

[39] 19 U.S.C. § 1671e(a)(2)(B) and 19 C.F.R. § 355.20(d) were said to provide only for company-specific rates where the producer or exporter is government-owned, not where the government is the grantor of the subsidy.

2. The Coalition's Notice of Motion to strike the Canadian Parties' new non-record evidence (Pearse and Stigler texts, and QLMA-CLA/Q assertions);

3. The Canadian Complainants' Motion to strike the Coalition's untimely factual information (Newport study, Flynn-Cox study and attachments);

4. The Canadian Complainants' Motion to strike the Coalition's new non-record evidence (Hufbauer Report).

The Panel scheduled a preliminary oral hearing for November 17, 1992, primarily to consider the Coalition's Motion to strike the Panel for lack of jurisdiction. Such hearing was adjourned by Notice of the Binational Secretariat (U.S.) dated November 16, 1992, due to the inability of one of the panellists to attend.

On November 20, 1992, the U.S. Secretariat issued a Notice of Suspension of the Panel Review, due to the withdrawal from the Panel of one of the panellists, Barry E. Carter. Pursuant to Rule 78 of the *Article 1904 Panel Rules*, this proceeding was suspended until a replacement panellist could be selected.

By Notice of December 18, 1992, the U.S. Secretariat advised the parties that a substitute panellist, W. Michael Reisman, had been named to serve on the Panel. Pursuant to Rule 78, the suspension was removed and the Panel Review resumed. New deadlines for filing of documents were provided the parties, and a two day oral hearing was scheduled to commence on February 11, 1993.

By Order of December 28, 1992, the Panel extended the dates for the provision of the parties' rebuttal briefs and reply briefs, and also set a date for the provision of a Joint Appendix (or case book of authorities), and a Supplementary Appendix, if necessary.

On January 4, 1993, the Panel issued three separate Orders which:

1. denied the Coalition's Motion to strike the Canadian Parties' alleged new non-record evidence (Pearse and Stigler texts, and QLMA-CLA/Q assertions);

2. denied the Canadian Complainants' Notice of Motion to strike the Coalition's untimely factual information (Newport study, Flynn-Cox study, et al) "without prejudice to the rights of all participants to address the issues raised in this motion as part of their overall argument on the merits of this case"; and

3. granted the Canadian Complainants' Motion to strike the Coalition's new non-record evidence (Hufbauer Report) "without prejudice to the Coalition's right to incorporate in its legal argument the points made by Prof. Hufbauer to the assertion that the Department of Commerce's determination on this issue is contradicted by both common sense and technical economic analysis". The Panel further ordered that the Coalition was not entitled "to support its assertion by the kind of new empirical evidence that is exhibited in Hufbauer's regression analysis of the data already in the record", and indicated that the Panel would ignore the references in the Coalition's brief to the Hufbauer Report to the extent they were inconsistent with the order.

By Order dated January 26, 1993, the Panel denied the Coalition's Motion to strike the Panel for lack of jurisdiction, with reasons for such decision to follow in this decision (set out *infra*).

On January 29, 1993, the Panel held a pre-hearing conference call with counsel for all the parties to determine the applicable procedures for the hearing and received submissions as to the allocation of time during the hearing. The Panel also invited counsel to address certain issues in oral argument. Upon careful consideration of the submissions made by counsel during the pre-hearing conference call, the Panel issued an Order on February 2, 1993, allocating the time for oral submissions between the parties.

On February 11 and 12, 1993, the Panel heard oral argument. During the argument, the Panel granted leave to Commerce pursuant to Rule 70 to file a subsequent authority, namely, a preliminary Report of the GATT *Subsidies Code* Panel concerning Commerce's self-initiation of its investigation in Lumber III. The Panel noted that although it admitted this preliminary Report as a subsequent

authority, it had serious concerns about the weight, if any, to be given to the GATT Report. The parties requests to file responses to Commerce's filing of this Report were also granted by the Panel.

Subsequent to the hearing, Commerce sought leave to file a revised version of the *Subsidies Code* Panel Report under Rule 70 of the *Article 1904 Panel Rules* by letter of March 4, 1993. Thereafter, the Canadian Complainants and Québec moved to file a response to the submission of the revised Report in excess of one page as required by Rules 17 and 70(3). By letter of March 19, 1993 the Coalition sought leave to file a response to Canada and Québec's submissions regarding this revised Report. Finally, by letter of March 24, 1993 the Canadian Complainants filed their objection to one of the Coalition's assertions in its March 19, 1993 letter.

In April of 1993 the Panel issued Orders granting Commerce leave to file the revised *Subsidies Code* Panel Report and granting the Canadian Complainants, Québec and the Coalition leave to file their submissions in this regard. In the same month, the Panel also granted Commerce leave to file the decision of the Extraordinary Challenge Committee in Live Swine from Canada[40] as a subsequent authority.

[40] ECC-93-1904-01 USA (April 8, 1993).

III. JURISDICTION OF THE PANEL

By Notice of Motion dated September 29, 1992, the Coalition requested that the Panel determine that Article 2009 of the *FTA* ousts the Panel's jurisdiction to review the *Final Determination* in Lumber III because it "arises out of" the softwood lumber *Memorandum of Understanding*. Article 2009 states:

> The Parties agree that this Agreement does not impair or prejudice the exercise of any rights or enforcement measures arising out of the Memorandum of Understanding on Softwood Lumber of December 30, 1986.

The Coalition argues that the "plain words of Article 2009 are dispositive",[41] stating that both the United States Trade Representative and Commerce have "interpreted this dispute as `arising out of' the *MOU*". In the Coalition's submission, the parties to the *FTA* saw fit to remove the jurisdiction of Chapter 19 binational panels in this circumstance.

The Canadian Complainants first ask that this Panel apply the express text of Article 1904 and section 516A of the *Tariff Act of 1930*[42] to the facts at instance, and find jurisdiction. The Canadian parties submit that the legislative history of Article 2009 reflects no intention other than to ensure the continued effect of the *MOU* upon the coming into force of the *FTA* (*i.e.* to grandfather the *MOU*). The Canadian Complainants also assert that:

> Canada's lawful termination of the *MOU*, on October 4, 1991, eliminated any rights or enforcement measures which existed or were contemplated under the *MOU*. ... Canada had no continuing obligations under the agreement, and there were, therefore, none for the United States to enforce. As all "rights" and "enforcement measures" preserved by Article 2009 ceased to have meaning with termination of the *MOU*, they

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[41] Notice of Motion of Sept. 29, 1992, at p. 16.

[42] hereafter 19 U.S.C. § 1516A.

> cannot be impaired or prejudiced with this Panel's review of the *Final Determination* in this case.[43]

The Canadian parties listed a number of distinct `rights' and `enforcement measures' created by the *MOU*, and in existence during the *MOU*'s operation, that they argue Article 2009 was designed to secure as opposed to the broad right of recourse to the Court of International Trade which the Coalition asserts is envisaged by Article 2009.[44]

Commerce also disagrees with the Coalition's position, and asks that the motion be denied. Commerce's position may be summarized as follows. The Canadian Complainants filed a timely request for a binational panel review in accordance with Article 1904 of the *FTA* and 19 U.S.C. § 1516A. Neither Chapter 19 of the *FTA* nor the U.S. statute implementing Chapter 19 expressly divests a binational panel of jurisdiction over softwood lumber. Indeed, Commerce argued that this Panel is precluded from even considering this question because Article 2009 is not referenced in Chapter 19 nor is Chapter 19 referenced in Article 2009. In Commerce's view, the interpretation of Article 2009 is therefore outside the Panel's jurisdiction.[45] Regardless, it was Commerce's submission that:

> ... Article 2009 is not a jurisdictional provision, but rather is a broad `grandfather' clause designed to ensure, inter alia, that the *FTA* did not supersede the *MOU* or render the Understanding null and void. Second, Article 2009, by its express terms, does not deprive a Chapter 19 panel of jurisdiction over, or exempt from the provisions of the Agreement, legal disputes involving softwood lumber. As such, Article 2009 cannot divest this Panel of jurisdiction in this binational panel review.[46]

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[43] Canadian Parties' Joint Response, at pp. 20-22.

[44] Canadian Parties' Joint Response, at pp. 23 ff.

[45] Commerce argued that only binational panels convened pursuant to Chapter 18 of the *FTA* can interpret provisions outside Chapter 19 or entertain disputes regarding the interpretation or application of the *FTA*, citing the text of Art. 1801 in support.

[46] Commerce's Response of October 30, 1992, at pp. 2-3.

The Panel agrees with the submissions of Commerce and the Canadian parties that the plain language of Article 1904 and § 1516A grants a binational panel exclusive jurisdiction where "interested parties", who were parties to a proceeding before Commerce, file a timely request for review of a final determination covering merchandise of Canadian origin. Nowhere in Article 1904 or any other provision of Chapter 19 is this Panel divested of the jurisdiction to review a final determination of Commerce regarding softwood lumber. Neither the three exceptions to jurisdiction in Article 1904, nor the fourth exception found in § 1516A(g)(3)(A)(iv) of the *Tariff Act*[47] deprives the Panel of jurisdiction. The Panel concurs with Commerce that the "striking absence" of specific language in Chapter 19 addressing disputes involving softwood lumber lends support to the contention that neither Party to the *FTA* sought to exempt softwood lumber from Chapter 19 review. The Panel finds that if the Parties to the *FTA* intended Chapter 19 not to govern subsequent softwood lumber trade disputes, the intention would have been expressly stated in Chapter 19. Thus, by simple application of the express provisions of Chapter 19, this Panel holds that it has jurisdiction to review Commerce's *Final Determination*.

Assuming *arguendo* that the Coalition's motion requires that the Panel consider the meaning to be ascribed Article 2009 of the *FTA*, and assuming without deciding that the Panel has jurisdiction to do so, it is nonetheless the Panel's view that the Coalition's interpretation of the effect of this Article on the Chapter 19 review process is unsupportable for a number of reasons briefly set out below.

First, the legislative history that the Coalition proffered as evidence of an intention of the *FTA* Parties to exclude any matter which can be said to have `arisen out of' the *MOU* is unconvincing. The Coalition cited no legislative statement made either prior to or contemporaneous with the coming into force of the *FTA* that indicates any intent other than to include Article 2009 as a broad grandfather clause, in the words of the Canadian Parties, to "ensure[] that if, during the life of the *MOU*, either

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[47] This exception deals with circumstances where a panel review is dismissed for lack of jurisdiction, *i.e.* failure to meet the criterion set out in Article 1904.

Party was unable or unwilling to carry out its obligations, nothing in the *FTA* would preclude the exercise of any enforcement measure, that otherwise might be available to the other Party.",[48] *e.g.* border measures where the U.S. believes Canada is failing to meet its obligations under the *MOU*.

The Coalition also failed to produce any Senate Committee or House Committee Report that even hinted at the removal of softwood lumber from the purview of the *FTA* Chapter 19 review process, even though unique treatment was expressly considered for various other sectors and products. The only `legislative' statement that may be said to support the Coalition's position was made four years after the *FTA* came into force.[49] This is not a persuasive indication of the legislative intent at the time of the drafting of Chapters 19 and 20 of the *FTA*.[50] Similarly, the Coalition failed to proffer any persuasive evidence that it was the Canadian government's intention to withdraw disputes that may be said to be related to the *MOU* from the binational panel review process envisaged by Chapter 19.

Second, a contextual review of Article 2009 within Chapter 20 of the *FTA* readily reveals that it is not a provision that grants or precludes jurisdiction. The text of Article 2009 does not exempt softwood lumber, or disputes in relation thereto, from the *FTA*. However, Article 2005 by contrast, specifically "exempts" cultural industries from the provisions of the *FTA*. The absence of similar `jurisdictional' language in Article 2009 clearly supports the Panel's finding.

Finally, and perhaps most importantly, the Panel is of the view that once the *MOU* was terminated in accordance with its terms, any "rights" or "enforcement measures" that existed under the *MOU* ceased to exist. Upon termination, neither Party bore any obligations or had any rights

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[48] Canadian Parties' Joint Response, at pp. 17-18, and 24.

[49] Senator Max Baucus, *Congressional Record* (March 10, 1992) at S 3000.

[50] See County of Washington v. Gunther, 452 U.S. 159 (1981) at 176 and Teamsters v. U.S., 431 U.S. 324 (1977) at 354 regarding the weight to be accorded statements made after legislation is passed.

which could be said to "arise out of" the *MOU*, in the words of Article 2009.[51] The Panel finds it difficult to understand how this panel review can be said to "impair or prejudice" the exercise of rights or enforcement measures that are no longer in existence.

For the above mentioned reasons, the Panel finds that it has jurisdiction to review the *Final Determination* in Lumber III, in accordance with Article 1904 of the *FTA*.

[51] See *Restatement (Third) of Foreign Relations Law of the United States*, § 332 (1986). S

IV. STANDARD OF REVIEW

Article 1904(3) of the *FTA* requires this Panel to "apply the standard of review described in Article 1911 and the general legal principles that a court of the importing country otherwise would apply to a review of a determination of the competent investigating authority."[52] While the scope of this Panel's review is limited to the Administrative Record before the agency, the Panel may also consider, as provided under Article 1904(2):

> The relevant statutes, legislative history, regulations, administrative practice, and judicial precedents to the extent that a court of the importing party would rely on such materials in reviewing a final determination of the competent investigating authority.

Since the United States is the importing country in this proceeding, Article 1911 of the *FTA* directs the Panel to apply the standard of review of 19 U.S.C. § 1516 A (b)(1)(B). Under that provision, the Panel must "hold unlawful any determination, finding, or conclusion found...to be unsupported by substantial evidence on the record or otherwise not in accordance with law." This standard has been applied and discussed in previous binational panel decisions.[53]

The standard of review requires that Commerce's decision: (1) be supported by substantial evidence on the record; and, (2) be otherwise in accordance with the applicable law.

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[52] Article 1911 defines "general legal principles" as "principles such as standing, due process, rules of statutory construction, mootness, and exhaustion of legal remedies."

[53] *e.g.* Live Swine from Canada, U.S.A. 91-1904-03 (May 19, 1992); Replacement Parts for Self-Propelled Bituminous Paving Equipment from Canada, U.S.A. 90-1904-01 (May 24, 1991); New Steel Rails from Canada, U.S.A. 89-1904-08 (August 30, 1990); Fresh Chilled or Frozen Pork from Canada, U.S.A. 89-1904-11 (Aug. 24, 1990); and In re Red Raspberries from Canada, U.S.A. 89-1904-01 (Dec. 15, 1989).

"Substantial evidence is more than a mere scintilla. It means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion."[54] Substantial evidence is "something less than the weight of the evidence, and the possibility of drawing two inconsistent conclusions from the evidence does not prevent an administrative agency's finding from being supported by substantial evidence."[55] However, "[a] reviewing court is not barred from setting aside [an agency] decision when it cannot conscientiously find that the evidence supporting that decision is substantial, when viewed in the light that the record in its entirety furnishes, including the body of evidence opposed to the [agency's] view".[56] Substantial evidence has been held to mean "`such relevant evidence as a reasonable mind might accept as adequate to support a conclusion', taking into account the entire record, including whatever fairly detracts from the substantiality of the evidence."[57]

Binational panels, as the reviewing body, may not engage in *de novo* review.[58] Panels must limit their review to the evidence on the record.[59]

The decision of the U.S. Supreme Court in Chevron U.S.A. Inc. v. Natural Resource Defence Council is widely recognized as the *locus classicus* of judicial review of administrative action, particularly as regards an agency's interpretation of the law it is mandated to apply. Chevron stands for the proposition that in determining whether an agency's application and interpretation of a statute is in accordance with law, a court need not conclude that "the agency's interpretation [is] the only

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54 Matasushita Electric Industrial Co., Ltd v. United States, 750 F.2d 927,933 (Fed. Cir. 1984), citing Consolidated Edison Co. v. NLRB, 305 U.S. 197, 229 (1938). See also Ceramica Regiomontana, S.A. v. United States, 636 F. Supp. 961, 966 (CIT 1986); *aff'd per curium*, 810 F.2d 1137 (Fed. Cir. 1987).

55 Consolo v. Federal Maritime Commission, 383 U.S. 607,619-20 (1966).

56 Universal Camera Corp. v. N.L.R.B., 340 U.S. 474, 488 (1951).

57 Atlantic Sugar Ltd. v. United States, 744 F. 2d 1556, 1562, (Fed. Cir. 1984), quoting Consolidated Edison Co. v. NLRB, 305 U.S. 197, 229 (1938).

58 American Lamb Co. v. U.S., 785 F.2d 994, 1001 (Fed. Cir. 1986) .

59 PPG Industries, Inc. v. U.S., 928 F.2d 1568, 1572 (Fed. Cir. 1991).

reasonable construction or the one this court would adopt had the question initially arisen in a judicial proceeding."[60] In Chevron, the Supreme Court articulated the standard as follows:

> When a court reviews an agency's construction of the statute it administers, it is confronted with two questions. First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction of the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute.
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> [...]
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> > "... If [the agency's] choice represents a reasonable accommodation of conflicting policies that were committed to the agency's care by the statute, we should not disturb it unless it appears from the statute or its legislative history that the accommodation is not one that Congress would have sanctioned." United States v. Shimer, 367 U.S. 374, 382, 383 (1961)[61]

"The granting of discretionary authority to an agency implies that the exercise of discretion be predicated upon a judgment anchored in the language and spirit of the relevant statute and regulations."[62] A panel standing in the stead of a reviewing court may "not permit the agency under the guise of lawful discretion or interpretation, to contravene or ignore the intent of Congress."[63]

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60 Chevron U.S.A. Inc. v. Natural Res. Def. Council, 467 U.S. 837, 843 n. 11 (1984).

61 *Ibid.* at 842-43, 844-45. A review of the Chevron doctrine, and the U.S. Supreme Court's practice following Chevron, has been written by T.W. Merrill in "Judicial Deference to Executive Precedent", 101 Yale L.J. 969 at pp.980-93.

62 Freeport Minerals v. U.S., 776 F.2d 1029, 1032 (Fed. Cir. 1985).

63 Cabot Corp. v. U.S., 694 F. Supp. 949, 953 (C.I.T. 1988).

Agency interpretations of statutes which they are charged with administering shall be sustained if permissible, unless Congress has directly spoken to the precise question at issue,[64] or unless the text of the statute and/or its legislative history indicates that the agency's interpretation is not one Congress would have sanctioned.[65] In K Mart Corp. v. Cartier, Inc.,[66] the Supreme Court described the inquiry as to whether Congress had made its intentions known as an inquiry into the statute's "plain meaning", by looking, in Justice Kennedy's words, "to the particular statutory language at issue, as well as the language and design of the statute as a whole".[67] In Immigration and Naturalization Service v. Cardozo-Fonesca,[68] Justice Stevens footnoted that "... an agency interpretation of a relevant provision which conflicts with the agency's earlier interpretation is `entitled to considerably less deference' than a consistently held agency view."[69]

A reviewing court's "duty is not to weigh the wisdom of, or to resolve any struggle between, competing views of the public interest, but rather to respect legitimate policy choices made by the agency in interpreting and applying the statute."[70] The task of the reviewing body is to ascertain whether the agency's action falls within a "range of permissible construction".[71]

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64 Rhone Poulenc, Inc. v. United States, 899 F.2d at 1185, 1190 n. 9 (Fed. Cir. 1990), citing Chevron, *supra*, at 842-45.

65 P.P.G. Industries, Inc. v. U.S., 928 F.2d 1568, 1572 (Fed. Cir. 1991), citing U.S. v. Shimer, 387 U.S. 374, 382-83 (1961).

66 486 U.S. 281, 291 (1988).

67 Kennedy's J.'s opinion on this issue was adopted by the Majority of the Court; his conclusions as to the validity of ss. 133.21(c)(1)-(3) of Regulations made pursuant to s. 526 of the *Tariff Act of 1930* were adopted in part and rejected in part by the Majority of the Court. See also Kennedy J.'s Majority opinion in Public Employees Retirement System of Ohio v. June M. Betts, 109 S. Ct. 2854, 2863 (1989): "No deference is due to agency interpretations at odds with the plain language of the statute itself. Even contemporaneous and long standing agency interpretations must fall to the extent they conflict with statutory construction."

68 480 U.S. 421, 446 n. 30 (1987).

69 citing in support Watt v. Alaska, 451 U.S. 251, 273 (1981).

70 Suramerica de Aleaciones Laminadas C.A. v. U.S., 966 F.2d 660, 665 (Fed. Cir. 1992).

71 *Ibid.*

Where there is an absence of clearly discernible legislative intent, binational panels must limit their inquiry to the question of whether Commerce's statutory interpretations are "sufficiently reasonable".[72] An agency's interpretation is "sufficiently" reasonable if it has a rational basis which comports with the object and purpose of the statute.[73] Reviewing courts have rejected Commerce's "exercise of administrative discretion if it contravenes statutory objectives".[74]

The Extraordinary Challenge Committee in Live Swine from Canada[75] made the following findings regarding the role of Chapter 19 binational panels:

1. Panels must follow and apply the law, not create it. Panels must understand their limited role and simply apply established law. Panels must be mindful of changes in the law but must not create them;[76]

2. Panels may not articulate the prevailing law and then depart from it in a clandestine attempt to change the law;[77]

3. Panels must conscientiously apply the standard of review;[78] and,

4. Panels are not appellate courts and must show deference to an investigating authority's determinations. In particular, panels must be careful not to unnecessarily burden an investigating authority on remand.[79]

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[72] American Lamb Co. v. U.S., 785 F.2d 944, 1001 (Fed. Cir. 1986), citing Chevron, U.S.A. Inc. v. National Res. Def. Council, 467 U.S. 837 (1984).

[73] Georgetown Steel Corp. v. U.S., 801 F.2d 1308, 1314-18 (Fed. Cir. 1986) rev'g *sub nom* Continental Steel Corp. v. U.S., 615 F. Supp. 548 (C.I.T. 1985).

[74] Ipsco, Inc. v. U.S., 899 F.2d 1192, 1195 (Fed. Cir. 1990).

[75] Live Swine from Canada, ECC-93-1904-01USA (April 8, 1993).

[76] *Ibid.* at 14.

[77] *Ibid.* at 14.

[78] *Ibid.* at 11, and Fresh, Chilled and Frozen Pork from Canada, ECC-91-1904-01USA (June 14, 1991).

[79] *Ibid.* at 14.

In sum, the above mentioned principles have guided the Panel's review in this proceeding.

V. STUMPAGE PROGRAMS

A. Introduction

The major issues argued before the Panel regarding the countervailability of provincial stumpage programs were:

1. whether the stumpage programs confer benefits on a specific group of industries ("specificity"); and,

2. whether the stumpage programs provide timber to Canadian softwood lumber producers at preferential rates ("preferentiality").

These issues are analyzed in detail below.

B. Specificity

The Canadian Complainants take issue with Commerce's finding that the stumpage programs in question confer benefits on a "specific group of industries" as required by section 771(5) of the *Tariff Act of 1930*,[80] as amended.

Specifically, the Canadian Complainants allege that the *Final Determination* was contrary to established statute and case law, and inconsistent with prior agency practice in that it:

(1) failed to consider all relevant evidence, including that which fairly detracts from the agency finding, in basing a finding of specificity solely upon the limited number of users of the program, and in failing to consider other relevant evidence, including that relating to the criteria enunciated in the agency's own Proposed Regulations;

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[80] hereafter 19 U.S.C. § 1677(5).

(2) rejected the "inherent characteristics" test upon which it had relied in finding that the same stumpage programs were not specific in Lumber I, thereby finding the stumpage programs to be specific despite a lack of government action as required by the statute;

(3) provided no reasonable explanation for changes in prior agency practice as regards the definition of the appropriate industry, industries or group of industries which receive stumpage benefits; and

(4) in considering the significance of the number of actual beneficiaries of the program, failed to consider the relevance of the universe of potential users of the program.

The Canadian Complainants argue that the cumulative effect of the legal errors listed above was to apply a standardless, subjective and *ad hoc* test in place of the objective criteria developed through the cases and prior administrative practice, and a failure to base its conclusions upon substantial record evidence. The Canadian Complainants argue that if this Panel confirms Commerce's findings in respect of stumpage specificity, an agency decision regarding specificity will essentially become an unreviewable exercise of pure discretion.

In order to assess the merits of these complaints, it is first necessary to ascertain the appropriate legal standard for determining specificity as mandated by the statute, and as developed through voluminous case law on the subject. The history of the so-called "*de facto* specificity test" is outlined below. Only then can we ascertain whether Commerce has, in this case, applied a test for specificity which is "effectively precluded by the statute"[81] or otherwise contrary to law.

[81] PPG Industries, Inc. v. U.S., 928 F.2d 1569, 1573 (Fed. Cir. 1991), per Nies J. at 1573.

(i) The History of the *De Facto* Specificity Test

In order to find that a domestic program is countervailable, Commerce must decide not only that it provides a subsidy, but also that the benefits are "provided or required by government action to a specific enterprise or industry, or group of enterprises or industries".[82]

The interpretation of the word "specific" in 19 U.S.C. § 1677(5)(A) has come to be known as the specificity test. Like all words, it must be interpreted in the context of the legislation in which it appears, and in light of the intent of Congress in enacting that legislation. Therefore, it is important to bear in mind that the purpose of the countervailing duty legislation is more than simply the protection of U.S. domestic producers. In the words of Nies C.J. in the case of PPG Industries, Inc. v. U.S.:

> The view that these complicated statutes have only one purpose, namely, to protect U.S. industry from every competitive advantage afforded by foreign governments, is simplistic and myopic. The congressional debates and the objectives listed in the GATT *Subsidies Code* indicate that numerous public policies, some of which conflict with overcoming a competitive advantage, entered into enactment of these statutes and must be considered by ITA [Commerce].[83]

The so-called *de facto* specificity test derives from the special rule enacted by Congress in 1988, which requires Commerce, when investigating the existence of a domestic subsidy, to "determine whether the bounty, grant or subsidy in law or in fact is provided to a specific enterprise or industry, or group of enterprises or industries".[84] Moreover, the special rule specifically provides that "[n]ominal general availability, under the terms of the law, regulation, program, or rule establishing a bounty, grant or subsidy, of the benefits thereunder is not a basis for determining that

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[82] Section 771(5)(A)(ii) of the *Tariff Act of 1930*, as amended, codified at 19 U.S.C. § 1677(5)(A)(ii) (emphasis added).

[83] 928 F.2d 1568, 1575 (Fed. Cir. 1991).

[84] 19 U.S.C. § 1677(5)(B), emphasis added.

the bounty, grant, or subsidy is not, or has not been, in fact provided to a specific enterprise or industry, or group thereof".[85]

As recognized by the Court of International Trade ("CIT") in Roses, Inc. v. United States,[86] the special rule enacted as part of the *Omnibus Trade and Competitiveness Act of 1988* was meant to codify the CIT's 1985 holding in Cabot Corporation v. United States.[87] The Court in *Cabot I* held that Commerce could not base a finding of non-specificity simply on the basis of nominal general availability, but that it must further determine whether the program was in fact provided to more than a specific enterprise, industry, or group thereof.[88]

The CIT in Cabot I pointed out that there is a distinction between benefits such as defence, education, highways and other infrastructure that are provided to and used by all businesses, and benefits which, although available to all takers, by their nature can only be enjoyed by a particular group of recipients. The CIT referred to the first class as "general benefits" which are not countervailable, and the second class as "generally available" benefits which may or may not be countervailable depending upon whether they are in fact provided to a specific group of recipients.

Even before the *de facto* test was codified, it had been applied again by the CIT in PPG Industries Inc. v. United States.[89] This case dealt with a trust fund established by the Mexican

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85 19 U.S.C. § 1677(5)(B).

86 743 F.Supp. 870, 876 (CIT 1990), hereafter "Roses I". Cases referred to in this decision having the same names are distinguished by referring to the decisions numerically, in chronological order. The numbers used are for ease of reference in the decision only and bear no relation to numbers used in other decisions or by parties to these proceedings in their briefs.

87 620 F. Supp. 722 (CIT 1985), hereafter "Cabot I".

88 Cabot I was a review of an ITA determination regarding, among other things, the provision of low-cost carbon black feedstock to producers of carbon black, a material used in the manufacture of rubber, paints, inks, plastics and carbon paper. While the carbon black feedstock was nominally available to any industrial user in Mexico, it was in fact used only by two carbon black plants, which in turn produced only one commodity, carbon black.

89 662 F. Supp. 258, 265 (CIT 1987), hereafter "PPG I".

government to provide protection against exchange rate fluctuations to Mexican companies that had rescheduled their foreign-denominated debt. PPG, an American manufacturer of float glass, complained that the program provided a countervailable subsidy to Mexican manufacturers of float glass who accounted for 8% of the debt registered under the program. PPG argued that the eligibility requirements for the program reduced the number of users and rendered the program "specific". To this argument the Court responded:

> ...the mere fact that a program contains certain eligibility requirements for participation does not transform the program into one which has provided a countervailable benefit...There may, of course, be situations in which narrowly-drawn eligibility requirements *de facto* render the benefit one which is provided to a specific enterprise or industry or group of enterprises or industries.[90]

A little more than a year after its decision in PPG I, the CIT decided the second Cabot Corporation v. United States.[91] In that case, Commerce had again failed to use the *de facto* test from *Cabot I* and had determined that the low-cost provision of carbon black was not specific. The CIT again held that Commerce had disregarded the distinction between "general benefits" and "generally available benefits" that the Court had drawn in Cabot I, and had therefore failed to examine all relevant factors in determining whether or not countervailing duties should be imposed. The determination was remanded to Commerce.

Two years later, the CIT decided Roses I. At issue was a financial incentive program offered by the Mexican government to the agricultural sector of the economy. One of the arguments advanced by the American flower producers was that the use of the words "group of enterprises or industries" in the statute was intended to broaden the applicability of the statute, and that the word "specific" did not apply to the words "group of enterprises or industries". In other words, a subsidy provided to any group of industries, no matter how large or diverse a portion of the economy they

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[90] *Ibid.* at 266.

[91] 694 F. Supp. 949 (CIT 1988), hereafter, "Cabot II".

represented, could be countervailed. The Court held that "specific" modifies "group", and that specificity of some kind is always a prerequisite to the imposition of countervailing duties in respect of domestic subsidies.

Further, the CIT in Roses I held that Cabot I could not be interpreted as supporting the proposition that "any benefit not traditionally provided by governments or all benefits directed specifically towards the business community are countervailable".[92] In addition, it admonished Commerce to refrain from an overly narrow approach to the specificity test, pointing out that it is always the actual users of the program whose specificity must be assessed:

> "If the test [as now embodied in the Proposed Regulations] is applied mechanically, it may fail to address the relevant issues. In deciding whether a countervailable domestic subsidy has been provided ITA [Commerce] must always focus on whether an advantage in international commerce has been bestowed on a discrete class of grantees despite nominal availability, program grouping, or the absolute number of grantee companies or "industries".[93]

In PPG Industries v. United States[94] the CIT reiterated the point it had made in PPG I - that the existence of eligibility requirements for the exchange rate stabilization program for foreign debt refinancing (*i.e.*, the prerequisite that the company actually have qualifying foreign debt), did not of itself provide evidence of specificity.

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92 743 F. Supp. 870, 876 (CIT 1990).

93 *Ibid.* at 881.

94 746 F. Supp. 119 (CIT 1990), hereafter, "PPG II".

Later, in 1991, PPG I was appealed to the United States Court of Appeals for the Federal Circuit.[95] Chief Judge Nies of the Court of Appeals opined that:

(1) To interpret Congress' intent as being to countervail all foreign subsidies was not supported by the record (at 1574);

(2) The GATT *Subsidies Code* is an aid for U.S. courts when interpreting U.S. countervailing duty law. The multiple policy objectives of the Code indicate that the protection of domestic industry is not the only purpose of U.S. countervailing duty law (at 1575);

(3) In 1984, Congress rejected an amendment that would have made all natural resource subsidies *per se* countervailable where an industry was a disproportionate user, regardless of whether it was specific or not (at 1576);

(4) "Specific" does not simply mean "identifiable" (at 1577);

(5) The factors stated by Commerce as being generally relevant to determining specificity [now contained in the Proposed Regulations] are appropriate and consistent with prior case law (at 1576); and

(6) Eligibility requirements are not determinative of specificity (at 1578).

The essence of Chief Judge Nies' reasoning in PPG III was derived from Cabot I: first, *de jure* specificity must be considered, then all relevant factors, including those posited by Commerce in the

[95] 928 F.2d 1568 (U.S.C.A., Fed. Cir. 1991), hereafter, "PPG III".

Lumber II case and now codified in section 355.43(b) of the Proposed Regulations[96] must be considered on a case by case basis to determine *de facto* specificity.[97]

A few months after the Court of Appeals decided PPG III, the CIT once again had an opportunity to consider the *de facto* specificity test. The case was Roses Inc. v. United States,[98] which, after the remand in Roses I, had again been appealed to the CIT. Commerce had this time applied all four factors from its Proposed Regulations and determined on remand that the agricultural loan program was not specific. The CIT upheld Commerce's determination that the agricultural sector was not specific. Once again the court held that all factors must be considered: "Commerce does not perform a proper *de facto* analysis if it merely looks at the number of companies that receive benefits under the program; the discretionary aspects of the program must be considered from the outset".[99]

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[96] These factors have been codified by Commerce at paragraph 355.43(b) of their Proposed Regulations (54 Fed. Reg. 23366, at 23379), which provides as follows:

(1) *Domestic programs*. Selective treatment, and a potential countervailable domestic subsidy, exists where the Secretary determines that benefits under a program are provided, or are required to be provided, in law or in fact, to a specific enterprise or industry, or group of enterprises or industries.

(2) In determining whether benefits are specific under paragraph (b)(1) of this section, the Secretary will consider, among other things, the following factors:

(i) The extent to which a government acts to limit the availability of a program;
(ii) The number of enterprises, industries, or groups thereof that actually use a program;
(iii) Whether there are dominant users of a program, or whether certain enterprises, industries, or groups thereof receive disproportionately large benefits under a program; and
(iv) The extent to which a government exercises discretion in conferring benefits under a program.

[97] The Panel notes that Nies C.J. was only joined in the result by Smith J., and that Michel J. filed a dissenting opinion in PPG III. The Panel also notes, however, that neither Roses II nor PPG IV (*infra*), both of which followed PPG III, adopted the reasoning of Michel J. when analyzing specificity. In fact, the PPG IV opinion was actually written by Michel J. for the Court, and quotes extensively, not from Michel J.'s own dissenting opinion, but from Nies C.J.'s opinion in PPG III.

[98] 774 F. Supp. 1376 (CIT 1991), hereafter, "Roses II".

[99] *Ibid.* at 1380.

The most recent case dealing with the issue is PPG Industries v. United States ("PPG IV").[100] On the issue of specificity, the Court of Appeals adopted the reasoning of Chief Judge Nies in PPG III, an adoption which is all the more relevant since the PPG IV opinion was written by the dissenting judge in PPG III. The Court spelled out the factors that Commerce must consider on a case by case basis - the factors developed by the Department of Commerce itself (at 1239-40):

> At least three factors must be considered on a case-by-case basis to determine whether a program is specific in its application. First, the ITA must consider the extent to which the foreign government acted to limit the availability of the program. Second, the ITA must consider the number of enterprises or industries which actually use the program. Third, the ITA must consider the extent to which the foreign government exercises discretion in making the program available.

(ii) Commerce's Application of the Specificity Test in this Case

1. Is Commerce obligated to consider all four of the factors contained in the Proposed Regulations in coming to a determination of specificity?

The Canadian Complainants assert that the finding of specificity in this case is contrary to law in that 1) Commerce is required by law to consider all the relevant factors and evidence when determining specificity and at a minimum must consider all four factors listed in the Proposed Regulations, and 2) Commerce in fact considered only one factor, the limited number of users, in this case and failed to consider record evidence which fairly detracted from its conclusion.[101]

Commerce, on the other hand, maintains that it is only required to consider all four factors in the Proposed Regulations before finding that a program is not specific; an affirmative finding of

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[100] 978 F.2d 1232 (U.S.C.A., Fed. Cir. 1992), hereafter, "PPG IV".

[101] Canadian Complainants' Joint Brief, September 29, 1992, IV.B.III.c.

specificity can be based upon any one of the criteria in the Proposed Regulations.[102] Further, even if it is required to consider all of the factors listed in the Proposed Regulations, Commerce maintains that it did consider the other three factors in this case, but determined that one factor, the limited number of users, required a finding of specificity.[103]

As a preliminary matter, this Panel finds that Commerce is required as a matter of law to consider all relevant evidence in determining whether the actual recipients of a particular program form a "specific group of industries", and cannot base its decision solely on evidence of the number of industries represented by the program recipients.

As a matter of general U.S. administrative law, it is well established that an agency must base its decision upon all record evidence, including that which fairly detracts from the evidence in support of its decision.[104] Commerce itself has indicated in its Proposed Regulations the factors which will generally inform its decision regarding the specificity of a particular group of program beneficiaries. These factors can be labelled for ease of reference as 1) government action, 2) number of users, 3) dominant or disproportionate use, and 4) government discretion.

Commerce argues in its Response[105] that these criteria are to be used in a sequential manner, and that it is only necessary to consider subsequent factors if a finding of specificity cannot be based upon the preceding factor. This Panel must defer to the reasonable exercise of agency authority, and certainly it is not the intention of this Panel to interfere with the rule-making authority of Commerce and its power to issue and apply the Proposed Regulations. The Proposed Regulations have, in fact, been upheld by the United States Court of Appeals in PPG III as forming the appropriate standard to apply in *de facto* specificity cases. The interpretation and application of those Proposed

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[102] Response of the Investigating Authority, January 6, 1993, IV.C.III.

[103] 57 Fed. Reg. 22,570 (1992) at 22,583.

[104] Universal Camera Corp. v. NLRB, 340 U.S. 474 (1951).

[105] pp. C-26 and following.

Regulations need not be that which the Panel would have chosen but it must, however, be reasonable. Unfortunately, the sequential application of the four factors posited by Commerce is not reasonable and results in a failure by Commerce to consider all relevant evidence in the record before it.

To begin with, Commerce argues that it determines *de jure* specificity on the basis of "government action" embodied in the legislation and the regulations and only goes on to consider the number of users of the program if the program does not identify its recipients on its face. If that were the case, however, any program which identified recipients on the face of the legislation would be found to be countervailable, regardless of the number or diversity of the enterprises or industries so named. A program which, for example, explicitly provided for cash grants to all agricultural producers would be found to be countervailable, despite the ample case law and Commerce's own policy against finding that all of agriculture is specific. With respect, this Panel finds that it is simply impossible to make any kind of reasonable specificity finding, whether *de jure* or *de facto*, without considering the number of enterprises or industries either actually receiving or entitled to receive the benefits in question.[106]

Commerce asserts that the passages cited from the various PPG and Roses decisions to the effect that Commerce must address all four factors in a specificity test are not on point. Those cases involved negative specificity determinations, whereas the present case involves a positive specificity determination. We have examined those cases in light of their facts and do not find that their logic is applicable only to negative specificity determinations. If the existence of a dominant user within a non-specific group may indicate specificity, so too may the lack of dominant user indicate a lack

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[106] In Lumber I, Commerce determined that the Forest Industry Renewable Energy Program ("FIRE") identified a discrete class of beneficiaries on its face and was therefore specific. It failed to go on to consider whether the group of recipients so identified was actually specific in terms of the number of users and industries represented. It did, however, explicitly consider this factor in the context of its analysis of the stumpage program. After determining that the stumpage program was not specific because the limitation on the number of users was due to the inherent characteristics of the resource, Commerce went on to find that, regardless of the inherent characteristics test, there were too many users in too wide a range of industries for the program to be considered to be specific. Had Commerce addressed the number of users as part of its *de jure* analysis of the FIRE program, the "internal inconsistency" in Lumber I may well have been resolved by a finding of non-specificity for the FIRE program as well (Lumber I, at 24,161 and 24,167).

of specificity. Similarly, if the exercise of government discretion is probative, so too is the lack of such government discretion. We do not question the existence of extreme fact situations, such as that presented in the Cabot I cases, in which the absolute number of users is so small when compared to any imaginable yardstick[107] that this factor outweighs any possible influence that a lack of discretion or a lack of dominant user may have. The PPG cases, however, upheld Commerce's determination that 1200 firms in 63 industries receiving benefits under the FICORCA exchange rate program were not specific. Clearly, the 3600-odd stumpage users in this case, representing between two and twenty-seven industries (depending upon the definition of industry being used), do not fall into the category of extreme cases.

This is not to say that Commerce could not, after having considered all of the evidence, determine that a particular program is specific where there is more than a trivial number of users and/or industries, no dominant or disproportionate user, and no government discretion. It is within Commerce's discretion to decide the weight to assign to the various relevant factors in a particular case. Rather, we find, as have other binational panels and the U.S. courts referred to above, that Commerce cannot ignore these factors in coming to its determination. In so doing, it must consider all of the evidence, and provide a reasonable analysis of the weight it assigns to such evidence.

We also note that Commerce itself, in Lumber II, stated that:

> Based upon our six years of experience in administering the law, we have found thus far that the specificity test cannot be reduced to a precise mathematical formula. Instead, we must exercise judgment and balance various factors in analyzing the facts of a particular case in order to determine whether an "unfair" practice is taking place.

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[107] *E.g.*, GDP, the applicable sector of the economy (be it manufacturing, services, agriculture, etc.), the absolute number of commodities produced in the economy or that sector - to name a few possible yardsticks.

Commerce went on to list some of the factors which are relevant to that determination - essentially the same as those which became formalized in the Proposed Regulations - before concluding that: "[t]he Department must consider all of these factors in light of the evidence on the record in determining specificity in a given case".[108]

While this Panel is obligated to show deference to the agency's expertise, we are entitled to ensure that the agency's interpretation of the statute is reasonable. We find that it is simply not reasonable for Commerce to posit, as it has in this case, that it is not required to consider evidence relating to all four of the factors listed in the Proposed Regulations, as well as any other relevant record evidence, before coming to a conclusion on specificity.

2. Rejection of the "Inherent Characteristics" Test

Canadian Complainants argue that Commerce improperly rejected the inherent characteristics test which had been a basis for its 1983 finding that the stumpage programs in question were not specific. In Lumber I, Commerce found that "[t]he only limitations as to the types of industries that use stumpage reflect the inherent characteristics of this natural resource and the current level of technology".[109] Even if the number of users had been small enough to be specific (the opposite of Commerce's actual conclusion in that case), the fact that the government did nothing to limit the number of actual users out of the universe of potential users meant that the stumpage programs would have been found to be non-specific.

In the *Preliminary Determination* and the *Final Determination* in the case under review in this proceeding, Commerce held that Congress had rejected the inherent characteristics test when it codified the *de facto* specificity test in 1988. Since the number of users of any natural resource is intrinsically limited by the inherent characteristics of that resource, Commerce reasoned that the

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[108] 51 Fed. Reg. 37,453 at 37,456 (emphasis added).

[109] 48 Fed. Reg. 24159, at 24,167.

inherent characteristics test resulted in the "absurd" rule that no natural resource subsidies would be countervailable. In Commerce's opinion, the legislative history of the 1988 amendment indicates that Congress intended to entirely reject the inherent characteristics test. Even if, as Canada argues, Congress did not intend to reject the test entirely, it certainly did not mandate its use. Commerce submits that, given the illogical results which flow from the test, it is not unreasonable for Commerce to reject its use in this and future cases.

Insofar as the inherent characteristics test, as applied by Commerce prior to 1985, would result in the *per se* non-countervailability of natural resource subsidies, this Panel agrees with Commerce that it should be, and has been, rejected.

After reviewing the legislative history and the case law cited by the various parties in this case, this Panel does not, however, find it reasonable to interpret the 1988 amendment as having had the purpose of completely eliminating the "inherent characteristics" of the resource from consideration as a relevant factor. Calling the inherent characteristics test by another name (the "generally available benefits rule"), the Senate Finance Committee Report says that "[i]n a subsequent review of the determination under review in the *Cabot* case, Commerce Department recognized that it had applied this test in an overly restrictive manner and determined that there were too few users of carbon black feedstock in Mexico to find that the benefit ... was generally available".[110] Thus, the very legislative history cited by Commerce indicates that Congress turned its mind to the question and recognized that the fact that a benefit was on its face generally available could still have some relevance. Indeed, the very fact that government discretion is one of the factors considered by Commerce in applying the *de facto* specificity test implies that the reason why a population of users is limited can be relevant to the analysis. If the number of actual users is limited, a finding that this is not due to the exercise of government discretion indicates that some other factor, such as the inherent characteristics of the natural resource in question, may be at work. Therefore, although we cannot agree with the Canadian Complainants that government action beyond the enactment of the relevant legislation is

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[110] S. Rep. No. 71, 100th Cong, 1st Sess. 123 (1987) (emphasis added).

a prerequisite to a finding of specificity (a position which leads, as Commerce points out, to a finding of *per se* non-countervailability for most natural resource subsidies), neither do we find it reasonable to say, as has Commerce in this case, that the factors determining the actual number of users are entirely irrelevant.[111]

3. Did Commerce in fact base its decision on only one factor in this case?

Commerce claims that, although not required to, it did in fact consider all of the factors in the Proposed Regulations in coming to its conclusion in this case.[112] Thus, it is Commerce's position that even if it is wrong in saying that only one factor need be considered to find specificity, this did not result in remandable error in this case.

At the outset, we wish to point out that this Panel is charged with determining whether Commerce's decision, as articulated in the *Final Determination*, is in accordance with law. The parties in an administrative hearing are entitled to a reasoned explanation, in light of the evidence on the record, of how and why an agency came to a particular conclusion.[113] On the other hand, isolated comments in the *Final Determination* cannot be taken out of context to the exclusion of the rest of the *Final Determination*. It is the agency's reasoning, as articulated in the *Final Determination* taken as a whole, which is the subject of this review. What, then, was the basis of the finding of specificity in this case, as evidenced by the *Final Determination* itself?

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[111] In order to avoid any potential confusion due to the differing terminology of the parties in this case, we wish to point out that we also reject the Canadian argument that a program that is in fact being used by the entire potential universe of users cannot be found to be specific. This argument does, indeed, amount to the same thing as applying the inherent characteristics test in the *per se* fashion which was rejected by the CIT in 1985 and by Congress in 1988. A comparison of the population of actual users with the universe of potential users is also implicit in the government discretion analysis, however, and must be considered along with all other relevant evidence in determining specificity.

[112] Commerce's Response Brief, January 6, 1993, IV.C.III.

[113] Greater Boston Television Corp. v. FCC, 444 F.2d 841 (D.C. Cir. 1970), *cert. denied* 403 U.S. 923 (1971).

Commerce stated that it considered all four factors and found one factor to be determinative in this case. It then went on to say that:

> This discussion does not mean that we have abandoned the specificity criteria in the Proposed Regulations, or that we have ignored them in this case. On the contrary, we have considered all of them, and determine that one of them - the limited number of users - requires a finding of specificity.[114]

We have looked to the *Preliminary Determination* for evidence of any consideration by Commerce of the factors other than the number of users. In the *Preliminary Determination*, however, Commerce does not examine the evidence on the record concerning the existence or lack thereof of a dominant or disproportionate user, nor does it consider any evidence concerning the existence or lack thereof of government discretion.[115] Rather, it turns the "inherent characteristics" test on its head and says that 1) because of the inherent characteristics of the commodity, nothing other than the number of industries receiving the good is relevant,[116] 2) the use of the resource in

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[114] 57 Fed. Reg. 22,570 at 22,583.

[115] In the *Preliminary Determination*, Commerce "considers" the remaining three factors in the Proposed Rules as follows (at 8884):

"...the extent to which the government acts to limit the availability of a program is not instructive in this case because a government need not take any further action, through special rules, regulations or eligibility criteria, to limit the availability or use of a program that is already in fact limited by the nature of the input provided."

"...when, as in this case, the universe of recipients is limited by the nature of the benefit, the factors of dominant use or disproportionality provide little, if any, guidance."

"The last factor, government discretion, is also not instructive in this case because the inherent characteristics of the input limit its use to the primary timber processing industries."

[116] *Preliminary Determination*, 57 Fed. Reg. 8800 at 8804; *Final Determination*, 57 Fed. Reg. 22,570 at 22,582.

question defines the "group" of beneficiaries,[117] and 3) being linked by their use of the input in question, and being less than the entire economy, the group is specific.[118]

The administrative case law is clear that a court can only uphold an agency determination on the same basis as that articulated by the agency.[119] Furthermore, the Court of Appeals for the Federal Circuit has stated in PPG IV that Commerce must consider all of the factors in the Proposed Regulations "in light of the evidence in the record in determining the specificity in a given case".[120] Nowhere in either the *Preliminary Determination* nor the *Final Determination* is there a reference to any record evidence regarding government action, disproportionate use, or government discretion.

Commerce counters that the three factors are not logically probative in this case because the number of users, as in the administrative review of Carbon Black from Mexico, is simply too few. As discussed above with regard to the appeals of Carbon Black in the Cabot cases, however, the facts in Carbon Black were extreme. The cases, and Congress's discussion of them,[121] cannot be said to stand for the proposition that factors other than the number of users can never be relevant in determining the specificity of a natural resource subsidy.

The evidence on the record shows that the number of users and the range of products produced by Canadian stumpage users are not so few as to render unreasonable a finding of non-specificity. Factors other than the number of users should therefore be taken into account. There was evidence on the record regarding factors such as the lack of dominant or disproportionate use of stumpage by the softwood lumber industry, as well as evidence both for and against the exercise

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117 *Final Determination*, *Ibid.* at 22,583.

118 *Ibid.* at 22,586.

119 FPC v. Texaco, 417 U.S. 380, 397 (1974); Burlington Truck Lines v. United States, 371 U.S. 156, 168-69 (1962); SEC v. Chenery Corp., 332 U.S. 194 (1947).

120 at 1577 (emphasis added).

121 S. Rep. No. 71, 100th Cong. 1. Sess. 123 (1987).

of government discretion in these programs. This evidence could reasonably have informed Commerce's analysis and assisted it in making its determination. This evidence, although not necessarily controlling, is nonetheless legally relevant and we direct Commerce to consider this and all other relevant record evidence in reconsidering the specificity of Canadian stumpage programs on remand.

(iii) Remand

The Panel remands the *Final Determination* to Commerce for an express evaluation and weighing of all four factors enunciated in its Proposed Regulations, as well as any other factors relevant to *de facto* specificity.

C. Preferentiality

(i) Stumpage, Natural Resource Economics, and Legal Subsidy

In the event that, on remand, Commerce finds that the softwood lumber industries satisfy the standards for "specificity", *supra*, that still leaves the question of whether the government programs at issue in this case meet the legal requirements of "subsidy". Both the stumpage programs and the log export restraints that Commerce found countervailable in Lumber III raise important issues of principle about the scope and interpretation of the governing legislation. One question is whether countervailing duty (cvd) law applies to border measures such as British Columbia's restrictions on the export of logs, on the grounds that such a program affords "cost savings" to domestic producers. This issue is dealt with in the next section of this decision. The other novel question is whether a government's pricing policies for access to a "natural resource" can amount to a subsidy if it has no

effect on the output or price of the products generated from the natural resource.[122] This is the issue addressed in this section of the Panel decision.

Commerce found that different Canadian provinces sold cutting rights to timber on publicly-owned lands at "preferential rates" measured against the "benchmark" prices charged in alternative markets. As such, this provincial government action constituted a "subsidy" under 19 U.S.C. § 1667(5), requiring imposition of a countervailing duty on the various softwood lumber products generated from those logs and exported to the United States.

The provinces challenge the specific calculations which led Commerce to find preferential pricing on their part. However, the Canadian Complainants argue that even if different provincial stumpage rates were lower than prices found in alternative timber markets, this would not amount to a "subsidy" under the prevailing legislation.

That Canadian argument has two components. One component is the economic thesis that in the case of a natural resource (such as access to standing timber), while the price charged will determine the division of economic rent for that resource between its owner (here the government) and purchasers (private logging firms), such stumpage prices cannot alter the output or price of logs. For that reason, stumpage cannot affect the output or price of downstream products into which the logs are incorporated for sale in the United States. The other component of the argument is the legal contention that some such economic effect from a government's pricing policy (i.e., a "market distortion") is a necessary feature of any judgment that a "subsidy" has been conferred by a foreign government that warrants imposition of a countervailing duty upon the downstream products imported into the United States.

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[122] This issue of economic rent theory as applied to a natural resource such as standing timber was briefly alluded to in the Preliminary Determination in Lumber I, but was not mentioned in either the Final Determination dismissing the petition in that case or in the Preliminary Determination in Lumber II. Thus, Lumber III is the first occasion that Commerce has found that natural resource pricing policies are countervailable.

Turning first to the legal materials, the relevant language of 19 U.S.C. § 677(5) reads as follows:

> (5) Subsidy.
>
> (A) In general. The term "subsidy" has the same meaning as the term "bounty or grant" as that term is used in section 303 of this Act [19 U.S.C. § 1303], and includes, but is not limited to, the following:
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> (ii) The following domestic subsidies, if provided or required by government action to a specific enterprise or industry, or a group of enterprises or industries, whether publicly or privately owned, and whether paid and bestowed directly or indirectly on the manufacture, production, or export of any class or kind of merchandise:
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> ***
>
> (II) The provision of goods or services at preferential rates.

The principal Supreme Court decision interpreting this provision, Zenith Radio Corp. v. United States,[123] stated the following to be the statutory purpose of the law:

> The countervailing duty law was intended to offset the unfair competitive advantage that foreign producers would otherwise enjoy from export subsidies paid by their government.[124]

And Commerce itself, in the introduction to its recently proposed Regulations for making cvd assessments, stated that:

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[123] 437 U.S. 443, 455-56 (1978).

[124] Reasoning from that premise, the Court upheld an administrative decision that Japan's remission of indirect domestic taxes on goods intended for export did not constitute a countervailable subsidy because this government policy simply avoided the double taxation that would result from stacking on top of Japan's domestic tax the United States' domestic taxes imposed on goods sold in this country.

> Conceptually, the regulations are based upon the economic model articulated by the Department in its final determinations in Carbon Steel Wire Rod from Czechoslovakia and Carbon Steel Wire Rod from Poland [...] and sustained by the Court in Georgetown Steel Corp. v. United States [...]. This model, which generally defines a subsidy as a distortion of the market process for allocating an economy's resources, underlies the Department's entire methodology. (emphasis added)

As one might surmise from the above Commerce statement, the key precedent debated in this aspect of these proceedings was Carbon Steel Wire Rod from Poland.[125] That case dealt with a variety of preferential actions taken by the Communist government of Poland respecting export of carbon steel wire rod products to the United States. Reversing its Preliminary Determination based on the literal language of the *Act* ("whenever any country... shall pay or bestow... any bounty or grant"), Commerce there found that cvd law did not apply to products coming from a nonmarket economy (NME).

In the *Final Determination* in Lumber III, Commerce sought to delimit the scope of Wire Rod as implying no more than that "it was meaningless to talk of subsidies in the context of nonmarket economies".[126] However, when one goes back and reads Wire Rod, it is clear that in order to reach its specific ruling in that case, the Department had to spell out more deeply than in any decision before or since the underlying philosophy of cvd law:

> In a market economy, scarce resources are channelled to their most profitable and efficient uses by the market forces of supply and demand. We believe a subsidy (or bounty or grant) is definitionally any action that distorts or subverts the market process and results in a misallocation of resources, encouraging inefficient production and lessening world wealth.
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> In NME's resources are not allocated by a market. With varying degrees of control, allocation is achieved by central planning. Without a market, it is obviously meaningless to look for a misallocation of resources caused by subsidies. There is no

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[125] 49 Fed. Reg. 19,374 (1984), upheld in Georgetown Steel Corp. v. United States, 801 F.2d 1308 (Fed. Cir. 1986).

[126] 57 Fed. Reg. 22,570 at 22,588.

> market process to distort or subvert. Resources may appear to be misallocated in an NME when compared to the standard of a market economy, but the resource misallocation results from central planning, not subsidies.
>
> It is this fundamental distinction -- that in an NME system the government does not interfere in the market process, but supplants it -- that has led us to conclude that subsidies have no meaning outside the context of a market economy.
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> In the absence of government intervention, market economies are characterized by flexible prices determined through the interaction of supply and demand. In response to these prices, resources flow to their most profitable and efficient uses. To identify subsidies in this pure market economy, we would look to the treatment a firm or sector would receive absent government action. In the absence of the bounty or grant, the firm would experience market-determined costs for its inputs and receive a market-determined price for its output. The subsidy received by the firm would be the difference between the special treatment and the market treatment. Thus, the market provides the necessary reference point for identifying and calculating the amount of the bounty or grant.[127]

Relying on this language, Canadian Complainants here contend that since government pricing of natural resources, such as the right to harvest standing timber, cannot have any market distorting effect upon either output or price of logs, there is no legal basis for imposing a countervailing duty upon the downstream softwood products generated from those logs.

As we shall develop below, Commerce did take issue with the economic thesis advanced by the Canadians. But its principal ground for rejecting this argument was Commerce's disagreement with the "contention that the countervailing duty law requires a market distortion test".[128] As Commerce put it, "[t]he issue in Wire Rod was whether Congress intended that the countervailing duty law applied to imports from nonmarket economy countries".[129] Thus, Commerce's negative answer to that specific question in Wire Rod would carry no implication that Commerce must focus

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[127] 49 Fed. Reg. 19,374 at 19,375.

[128] 57 Fed. Reg. 22,570 at 22,587.

[129] 57 Fed. Reg. 22,570 at 22,587.

on market distortion issues in making judgments about the "subsidy" quality of government actions in market economies such as Canada's.

As the Canadian Complainants contend, that conclusion by Commerce in Lumber III simply does not square with the logic of its reasoning in Wire Rod. In the latter case, Commerce was candid in saying that "Congress never has confronted directly the question of whether the countervailing duty law applies to NME countries," and so the Department had "to determine as best we can what Congress would have said if it had dealt with [that] question".[130] It was to that end that Commerce spelled out in Wire Rod the economic policy (quoted above) that underlies countervailing duty law. From that premise,[131] Commerce went on to explain why no one government action in a nonmarket economy could be found to influence output or price in exported goods.

> Assume that the government in a market economy made a payment to a producer on each of his sales. Theoretically, the market economy producer would respond by increasing his output. In an NME, the payment upon sale could be effected merely by increasing the administered price. Would the new, higher price result in increased output by the NME enterprise?
>
> If the NME government controls the inputs the producer needs and does not make these inputs available, then output could not be increased, despite the higher price. Moreover, if the enterprise had to expand its plant to produce more output, and had to rely on the government for investment funds or centrally managed enterprises for the machinery and equipment, then output would not be increased unless the funds or equipment were provided. Thus, the simple price increase, with no further action by the government, would not lead to increased output. The government action would have no economic result. Even if the government gave the producer the investment funds necessary for plant expansion, without the needed inputs, output could not increase. Neither of the actions, the price increase or the government "provision" of capital, would have the effect of a bounty or grant.[132]

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130 49 Fed. Reg. 19,374 at 19,377.

131 And quoting the Federal Court of Appeals to the effect that "it is the economic result of the foreign government's action that controls," Zenith Radio Corp. v. United States, 562 F.2d 1209, 1216 (1977) aff'd. 437 U.S. 443 (1978).

132 49 Fed. Reg. 19,374 at 19,376.

There is no question that the specific ruling in Wire Rod about nonmarket economies is not applicable to this case. However, the crucial reasoning through which Commerce arrived at that ruling -- "the economic model articulated by the Department" -- is precisely applicable to the Canadian Complainants' arguments made in this case. What Commerce itself has said about the model that underlies its "entire methodology" -- "which generally defines a subsidy as a distortion of the market process" -- cannot thus be legally ignored in considering whether government decisions about the pricing of access to a natural resource could influence the output and price of products generated from that resource, and thence justify imposition of a countervailing duty.[133]

In defense of its refusal to apply "market distortion" analysis to the judgment about whether a "subsidy was being offered in market economies, Commerce pointed to the legislative history of the *Trade Agreements Act of 1979*, and in particular to the Congressional directive (at 19 U.S.C. § 1677(6)) that allowed Commerce to subtract only certain financial factors from the gross subsidy in order to arrive at a net subsidy. The specified factors do not include all offsetting costs potentially faced by subsidy recipients -- such as, for example, the extra costs of operating in a remote and underdeveloped region in which the subsidy was designed to encourage development. By implication, then, Congress intended Commerce not to consider the latter amounts when calculating a net subsidy. From that premise, Commerce contended in Lumber III that it would be anomalous to engage in

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[133] Indeed, the government's brief in Wire Rod defending the decision in a review proceeding in the Federal Circuit Court of Appeal, made this point in terms that as we shall see below are strikingly relevant to the natural resource thesis advanced by the Canadians here.

> [T]he signal that a subsidy transmits to a firm is a false signal in the sense that the government is promoting economic behaviour which the market otherwise would not condone. In response to these false price signals, the firm uses "too much" of the subsidized input or produces an excess of the subsidized output, because the firm is paying "too low" a price for the input or receiving "too high" a price for its output. It is these results -- too much being consumed, too much being produced -- that [Commerce] found to be the distortion caused by subsidies and the evil at which the cvd law is directed.

(As quoted in the Canadian Complainants Joint Brief, Sept. 29, 1992, at C-23 - C-24). The Federal Court upheld Commerce's Wire Rod ruling in Georgetown Steel Corp. v. United States, 801 F.2d 1308, 1315-16 (Fed. Cir. 1986), on precisely that ground.

precisely this type of "net effects" analysis when determining whether a subsidy existed in the first place.

As the Canadian Complainants argue, that rationale offered by Commerce simply does not square with the broader legislative and departmental approach to cvd subsidy decisions. First, there is a clear legal distinction between § 1677(5), which governs identification of countervailable subsidies, and § 1677(6), which governs measurement of the subsidy for purposes of determining how much of a countervailing duty to impose, which distinction Commerce relies on in dismissing requests for provincial exclusions. That distinction is significant because in the case upon which Congress was focused when adopting the policy embodied in § 1677(6), there was no doubt that a government policy to grant financial benefits to firms to locate in underdeveloped regions did constitute a subsidy in the "market distortion" sense of that term. Indeed, even if a government does no more than grant sufficient benefits to a firm to offset the additional costs of locating in that region (thus leaving no net benefit at all), such a government action is designed to alter the market signal that is supposed to influence where production will be located and carried on. Thus such government action would be countervailable according to the theory articulated in Wire Rod.

Most importantly, in this very case, Commerce in fact used the "market distortion" approach in deciding whether a subsidy had been granted in a market economy. Commerce did so with respect to British Columbia's restraints upon log exports which, according to the Department (as elaborated upon in another part of this decision), produced a drop in the aggregate market demand for British Columbia logs and thereby reduced the price that had to be paid by domestic softwood lumber producers. Though there is no explicit language in § 1677(5) covering such a governmental border measure, Commerce found that restraint of log exports was a subsidy precisely because of its alleged distorting effects on the market economy. Commerce could not, then, refuse to consider the argument that another government policy in that same market economy was not a subsidy because it did not have a market distorting effect.

(ii) Dr. Nordhaus' Study

The Panel concludes that the Department made a fundamental legal mistake in determining that it was "precluded from measuring the benefit conferred by stumpage programs on the basis of a market distortion analysis, such as the effect of stumpage prices on output."[134] However, in its *Final Determination*, Commerce went on to offer a number of comments about the Canadians' economic theory as developed by their principal expert witness, Dr. William Nordhaus. Upon close examination of the decision, it is not entirely clear whether the Department intended to undertake full-scale analysis of the record on the assumption, *arguendo*, that its legal interpretation of the statute was incorrect. However, after considering the comments made by Commerce in this part of the *Determination*, this Panel finds that the Department both misunderstood the theoretical analysis developed by the Canadians of a natural resource market, and ignored the crucial empirical evidence offered by the Canadians to corroborate their theory about the softwood lumber market in that country.

No one in this case challenged the principles of classical Ricardian economic theory regarding natural resources. According to this 150-year old theory, the market for natural resources does not exhibit the normal elasticities in supply and demand whereby if prices go up (or down), purchase and production of the good will correspondingly go down (or up). Rather, because of the fact that natural resources have a basically fixed supply and strictly limited alternative uses, no such output and downstream price effects will flow from movements in resource prices, at least within what is called the "normal range." No matter how high the price charged by the owner within that range, as long as the purchaser of the right to harvest the natural resource can sell the product downstream for a higher price, the producer will harvest and sell as much of the resource as it can while making a profit on each unit sold. By the same token, no matter how low the price charged by the owner, the producer will not be able to harvest and sell more of this resource because the fixed (*i.e.*, inelastic) supply of the latter means there is no more of the resource available for that purpose. The price set

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[134] 57 Fed. Reg. 22,570 at 22,588.

for the natural resource does play a key role in determining how the financial value -- the economic rent -- of the resource will be divided between owner and purchaser. It does not, however, have any market distorting impact on the output of the resource and thence on the amount and price of downstream products.

There are two important qualifications to this thesis. One concerns the situation in which the price charged for the resource is or becomes "excessive" for some reason. The resource price is excessive if, when added to the costs of harvesting and transporting the resource, it makes the total cost of production greater than the price that will be paid by downstream users. In such a case, where the producer will incur a loss on extraction and sale of each unit, reduction in price of the resource does permit an increase in levels of production. However, such a resource price effect is not market "distorting". The price has simply been moved to the normal range one would expect in a competitive market in which owners of a resource try to set their prices at a level where they can make some sales and profits, rather than leave the resource lie fallow.

A different qualification must be made at the other end of the price range. Here, rather than charge a positive price for the resource, the owners enter into a contractual arrangement whereby producers actually secure a "net benefit" from purchase and harvesting of the resource. For example, the resource may be located in a remote region where costs of extraction and transportation are themselves higher than the sale price of the same resource located in more accessible locations. If the owner (in particular, a government) has other social and political reasons for wanting to see this region developed, it may charge a nominal price for the resource, but pursuant to a contract whereby the owner makes considerably greater expenditures on extraction and transportation of the resource. This is done in order to lower the ultimate cost to producers sufficiently to make production in this location profitable. Such an in-kind net benefit will have an impact on output of the resource in question, precisely because it alters the normal market signals regarding this particular resource location. It is at this level, and only at this level, that government decisions about pricing natural

resources can constitute a countervailable "subsidy" if one adopts the market distortion analysis of the legislation.[135]

Neither Commerce nor the Coalition disputed the validity of this mode of analysis in unquestioned natural resource contexts (*e.g.*, oil drilling rights). Nor did either suggest that stumpage arrangements between Canadian provinces and producers conferred net benefits upon the latter: domestic firms are paying Canadian governments a positive price for the logs they are harvesting from public lands. With respect to the economic side of the issue, the focus of the debate in these proceedings was about whether softwood lumber is a true natural resource, such that reduction in the stumpage price charged by governments within the normal range would not affect output and downstream prices, and reduction of prices charged in the excessive range would simply move output towards the competitive market level.

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[135] It may be helpful to clarify the above distinctions through a numerical illustration of the operation of what everyone concedes is a natural resource market -- oil drilling rights. Assume that it costs $5 a barrel for producers to drill, extract, and transport oil to refineries, another $5 for refineries to process, deliver, and sell oil products in the retail market, and the consumers of various oil products are prepared to spend on average $15 a barrel for the finished product. That means that as between owners and potential purchasers of the oil underground (or offshore), the normal price (or royalty) range would be somewhere between one cent and $5 a barrel.

If the royalty were set at $4 a barrel, this means the producer would realize a net $1 for each barrel extracted and sold, and so would be prepared to buy and extract as much oil as it could because a profit would be made on every such barrel. Contrariwise, if the royalty were set at $1 a barrel, the producers would not extract and sell any more barrels of oil, because there simply are no more available in this location. Thus, while determination of the royalty in that normal range will determine whether the owner or the producer reaps the lion's share of the economic rent inherent in the oil, it will not effect total output at all. And irrespective of the royalty they must pay owners, producers of the oil will sell it to downstream refineries at whatever price that competitive wholesale market will bear (which itself is dependent on levels of demand in the retail market).

One qualification to that generalization is a situation in which the royalty price charged by a particular owner is excessive, perhaps because its location (in Arctic seas) makes drilling and transportation costs higher ($8 a barrel rather than $5). If the owner in that location chooses to set the royalty at $1 instead of $4, that will affect the production of the resource in this location, but only by moving it to levels of output and price that one would expect in a normal competitive market. Suppose, though, that the total costs of drilling and transportation are $11, so that taken together with the $5 cost of refining and retailing, this oil cannot be sold in a competitive retail market in which the prevailing price is $15 a barrel. The government-owner may decide, however, that it is important for public policy reasons to stimulate production in this area. Thus, while charging a royalty of $1 per barrel extracted, the government also provides transportation facilities to producers that amount to expenditures of $3 a barrel. In that case, the government would be conferring a net benefit of $2 per barrel, rather than charging a real price of $1: by doing so the government would be conferring a "subsidy" in the market distorting sense of that term.

With respect to this question, the Canadians rely principally on the evidence of Dr. Nordhaus who filed a lengthy opening statement, conducted (along with Dr. Robert Litan) an econometric investigation of recent trends in the British Columbia timber market, filed three more statements in response to submissions from the Coalition and the *Preliminary Determination* by Commerce, and spent most of one day testifying before and being examined by Department officials. The only contrary evidence developed for this proceeding was a brief written statement by a Dr. William McKillop taking issue with Dr. Nordhaus' original submission. McKillop did not respond either orally or in writing to Dr. Nordhaus' rebuttals of his assertions. Close examination of what Commerce said on this score indicates that the Department thoroughly misunderstood the nature and implications of the relevant economic analysis, and that it totally ignored the specific empirical corroboration developed by Dr. Nordhaus for his thesis.

Commerce stated first that Dr. Nordhaus' position was that provincially-administered stumpage rates would necessarily be higher than those charged in competitive markets, and that output will always be lower.[136] Doctor Nordhaus made no such assertion about an issue that is indeterminate from an economic point of view. The Canadian evidence was that the actual relationship between timber harvesting prices and outputs in these two settings is an empirical matter, dependent on such factors as whether logging firms have the political clout to extract lower prices from governments, or whether a government wishes to pursue a policy of readily sustainable yield for the longer run that generates lower harvesting levels than would be adopted by a private firm seeking to maximize present profits. The point of Dr. Nordhaus' analysis is that whatever the actual level at which a government sets the price or harvest level, as long as the prices are in the normal range the particular price selected will itself have no impact on output levels (by comparison with an external benchmark price). If the government price is within the excessive range, the reduction of the price will affect output, but only by channelling both price and output towards, not away from, levels that one would expect to find in a competitive market.

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[136] see 57 Fed. Reg. 22,570 at 22,589.

Next, Commerce imputed to Dr. Nordhaus the view that the supply of harvestable logs was absolutely fixed, thereby ignoring what forestry experts (such as Dr. McKillop) realize are possible variations in the intensive and extensive margins in timber harvesting. (The intensive harvest margin refers to trees that may be uneconomic to harvest within a currently harvestable stand. The extensive harvest margin refers to entire stands of trees that are uneconomic to market at the current price.) The fact is that in his several later statements and his oral testimony, Dr. Nordhaus reiterated that the phenomena of intensive and extensive timber harvest margins fit perfectly comfortably with his theory as illustrative of the excessive price range.[137] However, the key economic implication of such potential sources of harvestable softwood timber is that provincial government prices that allow such stands to be harvested are actually market perfecting rather than market distorting, in line with what one would expect in a competitive market.

Finally, Commerce misstated Dr. Nordhaus' thesis to be purely static, thus allegedly ignoring the fact that owners of timber have a reservation price below which they will not sell harvesting rights now because they expect to be able to sell these rights for a higher price in the future. The fact is that while in the text of his original statement Dr. Nordhaus employed static analysis to convey the core elements of the natural resource-economic rent thesis, he included a Mathematical Appendix which demonstrated that precisely the same analysis of price effects holds true of a dynamic analysis over time. Then, in a text of his subsequent statements, Dr. Nordhaus reiterated that while the dynamic perspective adds the further question of when, not just whether and how much, wood will be harvested, the key determinant of the latter is not the stumpage price (at least in the normal or excessive range), but the rate of interest by which such expected future prices are discounted to present values. Indeed, Dr. Nordhaus noted that one implication of this dynamic mode of analysis is that (all other things being equal), one would expect immediate output to be somewhat greater in

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[137] Excessive price ranges are likely to be the byproduct of any administered stumpage system (public or private) that charges a standard price per unit of timber extracted, because it is extremely difficult to adjust the price to variations in the cost of harvesting particular stands or trees. Another potential cause of excessive prices -- fixed stumpage rates that became too costly in the face of falling downstream demand -- can be avoided by tying stumpage rates to movements in log prices.

private profit-maximizing markets where this interest rate-discount factor is more salient than it is in political-governmental markets concerned with insuring that the resource is preserved for future generations.

From an administrative law perspective, some might be inclined to treat the above as a matter of complex economic theory about which Commerce had the discretion to judge which position it found most persuasive.[138] Indeed, this is an area in which the Panel was particularly sensitive to the limitations imposed by the applicable standard of review. It is not the Panel's role to decide which of two competing economic theories is "correct". Where complex expert evidence is involved, a Panel should be particularly wary of interfering with an administrative agency's determination based on its specialized expertise.

Nonetheless, if the Panel looked merely for the existence of expert testimony on both sides, and went no further, Commerce's decision could be reviewed only if one side failed to present any expert testimony at all. This is not the proper approach by a reviewing tribunal. The Panel cannot abdicate responsibility to decide whether Commerce's *Determination* was supported by "substantial evidence on the record". Such an evaluation is impossible without at least some examination of the evidence itself -- the nature of the substantive arguments advanced by both sides. Under the applicable standard of review, Commerce's determinations cannot be reversed by a reviewing court (or binational panel) even if the latter believes Commerce's findings go against the preponderance of evidence. However, there must be substantial evidence supporting Commerce's determination; and

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[138] That was the argument advanced by both Commerce and the Coalition, relying on some observations by the Supreme Court in Zenith Corp. v. United States, cited above. We do note how different was the context in Zenith, in which the ruling in question reflected a Departmental policy that had existed for eighty years, and one that rested on traditional economic theory regarding the likely effects of double taxation. Here Commerce has imposed for the first time ever a countervailing duty respecting an alleged subsidy for a natural resource, in the face of classical Ricardian theory which was misstated in its decision, and without ever developing an alternative economic basis for its judgment about the market for this resource.

"[t]he substantiality of evidence must take into account whatever in the record fairly detracts from its weight".[139]

As the Canadians demonstrated through their analysis of the Record for purposes of this appeal, not only was there no substantial analytical rebuttal of the Nordhaus thesis, but only the Canadians offered any empirical evidence relating specifically to the relationship between provincial stumpage programs and the corresponding lumber markets. That evidence consisted of an econometric study by Dr. Nordhaus (together with Dr. Litan), which found empirical corroboration of the natural resource thesis in the British Columbia stumpage market (which comprises the vast bulk of Canadian softwood lumber production and exports).[140]

The Nordhaus/Litan study was made possible by, in effect, a natural experiment about the relationship between stumpage rates and log output occasioned by the Preliminary Determination in Lumber II and the *Memorandum of Understanding* between the United States and Canada. The *MOU* required British Columbia to raise its stumpage rates by an average of 15% in order to get relief from the export tax. British Columbia chose to raise its stumpage rates by very different amounts -- ranging from zero to 700% -- for six different species produced in eight different regions. Thus Drs. Nordhaus and Litan had a total of 48 observations for each of two different time comparisons through which to investigate whether higher prices in fact generated lower output. The fact there were such sharply different price increases for different timber lots made it possible for the first time to conduct such a price-output test while implicitly controlling for any external variables that affected demand for softwood lumber products (and thence softwood logs) from all these regions and species.

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[139] See Universal Camera Corp. v. NLRB, 340 U.S. 474, 488 (1951).

[140] The Coalition did place on the record certain data pertaining to Québec shipments of softwood lumber from 1980 to 1990. However, Commerce did not place any weight on this material in its *Final Determination*. In any event, this evidence is not a "study"; it is simply general data submitted by the Gouvernement du Québec in response to a Commerce questionnaire. The Coalition's own rebuttal brief acknowledges that it represents no more than "anecdotal" evidence. (See Coalition's Rebuttal Brief of January 6, 1993, at p. 129). The reason is that, unless the Nordhaus/Litan econometric study, this data regarding changes in Québec's lumber shipments before and after the MOU did not control at all for other variables that affected shipments. (A note accompanying the data states explicitly that other factors, such as housing starts and exchange rate, affected the levels of lumber shipments.)

Doctor Nordhaus' theoretical hypothesis was that higher prices in the normal region would produce no variation in output (contrary to the Coalition's position which is that higher prices would always generate correspondingly lower output). The actual finding from the study was that timber production showed virtually no response to stumpage charges. In particular, a 100% increase in price was associated with only a 2.8% decline in output. As Dr. Nordhaus put it, this was "essentially zero from a financial point of view and insignificantly different from zero from a statistical point of view." However, in its decision Commerce did not even mention, let alone try to refute, such a crucial piece of evidence on this issue -- the only empirical evidence available in these proceedings about the softwood lumber market that was the subject of this case.

(iii) Remand

We conclude that, in this case, Commerce should have considered whether or not these provincial programs could and did have a distorting effect on the operation of normal competitive markets before concluding that these governmental policies involve the type of "preferential" pricing that constitutes a countervailable subsidy within the meaning of the *Tariff Act*. Accordingly, we remand this part of the stumpage decision back to Commerce for review of all the evidence regarding the natural resource market for standing timber in light of the legal principles formulated in this decision.

VI. LOG EXPORT RESTRAINTS

A. Introduction

As a result of a petition filed by the Coalition, Commerce conducted an examination into various Federal and provincial regulations which restrict the export of logs. In the *Final Determination*,[141] Commerce confirmed its preliminary finding that "export restrictions maintained by the Province of [British Columbia] constitute a countervailable domestic subsidy."[142] Commerce confirmed its finding that British Columbia's log export restrictions are *de jure* specific.[143] Commerce also confirmed its finding that "the log export restrictions in Alberta, Ontario, and Québec did not confer a benefit" and, therefore, do not provide a countervailable subsidy to lumber producers.[144] Commerce then calculated the value of the benefit conferred by the B.C. log export restrictions, divided this value "by the value of B.C.'s lumber shipments plus the value of its by-product shipments produced during the lumber production process," and then "weight averaged this rate by B.C.'s share of exports to the United States of the subject merchandise."[145] On the basis of these calculations, Commerce determined that imports of the subject merchandise to the United States were to be assessed a countervailing duty at a rate of 3.60% *ad valorem*.

The Canadian Complainants argue that B.C.'s log export restrictions do not constitute subsidies as a matter of law. The Coalition urges affirmance of Commerce's decision in this respect, but seeks review of other aspects of the determination. The Coalition argues that Commerce erred in finding that the log export restrictions of Alberta, Ontario, and Québec do not constitute

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141 57 Fed. Reg. 22,570.

142 *Ibid.* at 22,606.

143 *Ibid.* at 22,605.

144 *Ibid.* at 22,604.

145 *Ibid.* at 22,620.

countervailable subsidies. The Canadian Parties urge affirmance of Commerce's decision in this respect.

This section of the decision discusses the economic theory behind Commerce's determination on log export restrictions in B.C.; examines previous administrative determinations and judicial precedents bearing on the determination; evaluates the extent and the validity of Commerce's determination as a departure from previous administrative practice; and, finally, considers such legal support as there may be for the departure in the *Final Determination*, the authorizing statute, the legislative history surrounding the authorizing statute, and GATT law and decisions.

Prior to dealing with the issues of specificity and the meaning and scope of the definition of "subsidy" in this context, the Panel wishes to deal with a procedural issue raised by the Canadian Parties about the evidence relied upon by Commerce to determine that B.C.'s log export restraints constituted a countervailable subsidy.

B. Motion To Strike Newport Study

Commerce issued its affirmative *Preliminary Determination* regarding provincial stumpage systems and British Columbia's log export regulations on March 5, 1992. All factual information was required to be submitted to Commerce on March 13, 1992 (*i.e*. the business day immediately preceding the commencement of verification).[146]

From March 16 through March 27, 1992, Commerce verified the accuracy of the questionnaire responses and expert studies submitted by Canadian Complainants.

On April 21, 1992, Canadian Complainants and the Coalition submitted their case briefs to Commerce. The Coalition's case brief contained *inter alia* the following information:

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[146] 19 C.F.R. § 355.31(a)(1)).

(1) a review and update of the Margolick-Uhler Study prepared by Carl A. Newport dated April 1992, (Newport study);

(2) a report by Bob Flynn and David Cox entitled "An Examination of British Columbia Log Export Restrictions dated April 20, 1992 (Flynn-Cox study); and

(3) letters and affidavits from mill owners regarding alleged purchasing practices, competition and product distribution in the lumber products industries.

Canadian Complainants objected to the Coalition's inclusion of this allegedly new factual information on the ground that the submission of this information violated Commerce's regulation governing the timeliness of filing factual information.[147] The same day, Commerce responded that it had identified certain documents submitted by several interested parties containing what appeared to be new factual information most of which appeared to be related to arguments previously made. The Department invoked its authority under 19 C.F.R. § 355.31(b)(1) to request this information for the following reasons:

- The parties representing both domestic interests and Canadian interests have submitted in their case brief what appears to be new factual information;
- This information appears to be related to arguments previously made in this proceeding as opposed to information supporting totally new arguments;
- Since the statute affords no opportunity for postponement of the Final Determination, the Department has the choice in these last three weeks of the proceeding either to focus on the merits of the important issues raised in this investigation or to spend its time identifying and weeding out the arguably new factual information in the thousands of pages of case briefs.

The Department noted in its response of April 24, 1992, that all parties would have an opportunity to comment in their rebuttal briefs on any of the arguably new factual information

[147] Pub. Doc. No. 494 (April 24, 1992).

contained in another party's case brief. The Department expressly stated that it was not determining whether certain information in those briefs did, in fact, constitute new factual information.[148]

The Coalition submitted its rebuttal brief to Commerce on April 27, 1992. The same day, the Canadian Complainants submitted their rebuttal brief which included a Second Supplemental Report by Professor Kalt which analyzed the allegedly new factual information submitted by the Coalition after the verification process commenced.

On April 29, 1992, Canadian Complainants objected to Commerce's decision to retain untimely and unverified information in the record in violation of the Department's own regulation establishing the time limits for the submission of factual information.[149] Canadian Complainants emphasized that retention of this information in the record was highly prejudicial in light of the significant nature and extent of the information and the fact that Canadian Complainants had no realistic opportunity to rebut this information. Canadian Complainants also noted that under the statute and regulations, Commerce was required to verify the accuracy of all factual information relied on in making its final determination.

During the hearing conducted by Commerce on April 29, 1992 the Assistant Secretary stated:

> We have accepted both the direct and the rebuttal briefs that contained allegedly new information, and we are going to allow the parties to address, in their discussions here today, as they did in their rebuttal briefs, any of that allegedly new information. I will however, underscore again, no more new information, either on direct or rebuttal, during this hearing.[150]

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148 Pub. Doc. No. 496.

149 Pub. Doc. No. 504.

150 Pub. Doc. No. 506, Vol. 1, at pp. 9-10 (Transcript of proceedings before Commerce).

The Department's *Final Determination* found that British Columbia's log export regulations artificially depressed domestic log prices and thereby afforded a competitive benefit to British Columbia's lumber producers. Canadian Complainants allege that Commerce's *Final Determination* rested solely on the untimely and unverified data provided by the Coalition in its April 21, 1992 case brief - data submitted long after the March 13th deadline for the submission of new factual information.

The Canadian Complainants filed a Motion To Strike the Coalition's Untimely Factual Information From The Administrative Record (September 29, 1992) alleging that the decision of Commerce to accept and retain the Coalition's untimely information in the record and to rely on this information in its *Final Determination* violated the plain meaning and purpose of Commerce's own regulation, and was contrary to fundamental principles of administrative law and agency practice. The Canadian Complainants alleged that Commerce's reliance on this untimely and unsolicited factual information without providing Canadian Complainants with a meaningful opportunity to rebut or comment on this information was highly prejudicial. Accordingly, the Canadian Complainants alleged that this information should be stricken from the record on review.

This Panel issued an Order denying the Canadian Complainants' Motion To Strike but without prejudice to the rights of all participants to address the issues raised in the Motion as part of their overall argument on the merits of this case (January 4, 1993).

For the reasons set out below, the Panel rules that Commerce properly accepted the factual information filed by the Coalition after the March 13th deadline.

(i) Secretary's Request for Factual Information - Section 355.31(b)

Section 355.31(a)(1)(i) of Commerce's Regulations contains the general rule governing time limits for submissions of factual information. New factual information for final determinations must

be submitted the day before the scheduled date on which verification is to be commenced (in this case, March 13, 1992). There are two exceptions to this general rule:

1. the Secretary of Commerce may request any person to submit factual information at any time during a proceeding;[151]

2. any interested party may submit factual information to rebut, clarify or correct factual information submitted by an interested party 10 days after the date such factual information is served on the interested party.[152]

The Panel need not decide whether the second exception applies in that it rules that the first exception governs.

1. No Requirement that the Secretary Request the Information in Advance

Pursuant to 19 C.F.R. § 355.31(b)(1), the Secretary of Commerce may request any person to submit factual information at any time during a proceeding. Although the Secretary does not have an unfettered discretion to allow untimely submissions and cannot act arbitrarily in such a way as to cause substantial prejudice to a party, the scope of section 355.31(b) is quite broad.

The United States Court of International Trade held in Floral Trade Council of Davis, California v. United States:

> Clearly, the regulations give ITA flexibility to obtain information necessary to its decision; if information it deems "critical" is submitted, albeit without a request, ITA has discretion under the regulations to consider it. Certainly, ITA abuses its discretion if it arbitrarily accepts information which is not truly critical. FTC has not shown such abuse. Moreover, FTC cannot claim prejudice because it was given a

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[151] 19 C.F.R. § 355.31(b)(i).

[152] 19 C.F.R. § 355.31(a)(2).

> special opportunity to submit information in rebuttal which it did [FTC was given 13 days to respond]. In addition, FTC has not demonstrated that it has any truly contradictory data. This entire issue appears to rest on speculation.[153]

The Canadian Complainants claim that Commerce can only rely on the authority of § 335.31(b) if it has requested the information in advance of it being filed. The Panel rejects this interpretation. The plain wording of the section is that the information can be requested "at any time". The object and purpose of the Regulations would be defeated if Commerce could not request necessary information that has been brought to its attention by an interested party before it makes a request. Commerce's interpretation is reasonable and the Panel defers to the agency's interpretation of its own Regulations.

(ii) No Prejudice

The Canadian Complainants have argued that they were prejudiced by the decision to retain the Coalition's untimely filed information, because they were provided no meaningful opportunity to rebut or comment on the Coalition's alleged new information.

The U.S. Supreme Court held in American Farm Lines v. Blackball Freight Service et al.:

> ...it is always within the discretion of the court or an administrative agency to relax or modify its procedural rules adopted for the orderly transaction of business before it when in a given case the ends of justice require it. The action of either in such a case is not reviewable except upon a showing of substantial prejudice to the complaining party.[154]

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153 775 F. Supp. 1492 at 1499.

154 397 U.S. 563 at 539.

The Panel finds that the Canadian Complainants were not substantially prejudiced by Commerce's decision to retain and rely upon the information filed by the Coalition after verification commenced.

Firstly, the Panel notes that Commerce gave the Canadian Complainants five days to respond to the information filed by the Coalition and an opportunity to make arguments to Commerce about this information during the hearing held on April 29, 1992. Secondly, Professor Kalt, a consultant retained by the Canadian Complainants, prepared a Second Supplemental Report dated April 27, 1992, consisting of twenty-two pages of text (plus attachments) in response to the disputed information filed by the Coalition. The fact that the Canadian Complainants did not receive as much time as they would have liked to respond to this information does not mean that they suffered substantial prejudice within the meaning of that term in American Farm Lines. Commerce was under a stringent deadline to issue its *Final Determination* in this case and in light of the circumstances prevailing at the time, the Panel cannot find that granting the Canadian Complainants only five days to respond constituted substantial prejudice.

The Panel also notes that during oral argument counsel for the Canadian Complainants were asked what evidence would have been submitted to Commerce (other than Professor Kalt's Second Supplemental Report) if Commerce allowed more than 5 days to respond. The responses provided to the Panel to this question (Transcript of Hearing, Vol. II, pp. 16, 56-62) do not establish substantial prejudice.[155] Accordingly, for the reasons given, the Panel rejects the Canadian Complainants' objections to Commerce's admission and consideration of the Newport Study.

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[155] The Canadian Complainants motion also claimed that Commerce was required by 19 USC § 1677e(b) and its 19 C.F.R. § 355.36 to verify all factual information upon which it relies. The Panel finds that in the circumstances of this case and in the light of the nature of the Newport study, Commerce properly conducted whatever verification may have been required of this document.

C. Specificity

In both the *Preliminary Determination*[156] and the *Final Determination*, Commerce found British Columbia's log export restrictions to be *de jure* limited to a specific group of industries. The "finding" in the *Preliminary Determination* amounted, however, to no more than a mere assertion that "[t]he export restrictions benefit a specific group of industries, the primary timber processing industries". The specific group of beneficiaries was not defined, rather, the reader was referred back to the discussion of stumpage programs for the definition of the primary timber processing industries.

The *Final Determination* recognized that there had been no separate specificity analysis in the *Preliminary Determination* for the log export issue, but confirmed its earlier finding in the following terms:

> The BC log export restrictions, on their face, benefit only BC users of logs (i.e., the solid wood products industry and the pulp and paper products industry). See Part 12, section 135, 136, and 137 of the BC Forest Act. Accordingly, the domestic benefits conferred by these export restraints are *de jure* limited to a specific group of industries. See Leather [from Argentina, 55 Fed. Reg. 40212 (D.O.C. 1990)] at 40,213 ("The embargo applies only to cattle hides, which are sold primarily, if not exclusively, to leather tanners (and, therefore,) is limited to a specific industry.").[157]

The Canadian Complainants allege that the lack of articulated reasons for the above finding requires a remand on this point, and further that the determination of *de jure* specificity is unsupported by any record evidence.

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156 57 Fed. Reg. 8,000 at 8813.

157 57 Fed. Reg. 22,570 at 22610 (1992).

(i) The Meaning of *De Jure* Specificity

The jurisprudence cited in these proceedings with respect to *de jure* specificity is not nearly as voluminous as it is with respect to *de facto* specificity. This is perhaps a reflection of the relative ease with which courts have dealt with the issue in the past.

19 U.S.C. § 1677(5)(B) itself instructs Commerce to "determine whether the bounty, grant, or subsidy in law or in fact is provided to" a specific enterprise, industry, or group thereof. The "specificity" which Commerce is engaged in determining relates quite clearly to the recipients of the bounty or grant, and not, as counsel for the Coalition argued at the oral hearing,[158] to the subject matter of the regulation.

Commerce in Carbon Steel Wire Rod From Malaysia[159] identified *de jure* specificity as "the extent to which a foreign government acts (*as demonstrated in the language of the relevant enacting legislation and implementing regulations*) to limit the availability of a program" (emphasis added). In analyzing the legislation in that case, Commerce said that "the language of the Investment Incentives Act does not appear to limit pioneer status benefits to specific industries or companies".[160]

The U.S. Court of Appeals in PPG III also outlined the test for *de jure* specificity, saying that "[i]f the domestic subsidy is provided by its terms to a particular enterprise or industry or group of enterprises or industries, it is countervailable without further inquiry".[161]

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158 Transcript (February 12, 1993) at p. 191.

159 53 Fed. Reg. 13,303 (D.O.C. 1988), at 13,304.

160 *Ibid.* at 13,304.

161 928 F.2d 1568, 1576 (Fed.Civ.1991) (emphasis added).

Examples of other cases in which Commerce found the programs in question to be expressly limited to a specific recipient or group of recipients include Carbon Steel Wire Rod from France[162] and Certain Steel Products from France,[163] both of which dealt with a special rescue plan for recapitalizing and restructuring the steel industry in France. Similarly, Carbon Steel Flat-Rolled Products from Korea[164] dealt with accelerated depreciation for taxation purposes that was made available to "a domestic person carrying on an important industry". The Enforcement Decree for the provision designated particular industries, such as steel producers, as being eligible for the special depreciation.

It follows that a *de jure* specificity analysis must involve a search for language, such as express eligibility requirements, which expressly limits the class of program recipients on the face of the statute or the regulations.

(ii) The Specificity Analysis Regarding Log Export Restrictions[165]

This Panel must decide, not whether Commerce's finding of *de jure* specificity of log export restrictions is correct, but whether it is reasonable. We note that we are limited to upholding this finding, if at all, on *de jure* grounds since a court may only uphold an agency decision on the basis articulated by the agency itself.[166] The only basis articulated by Commerce in respect of B.C.'s log export restrictions is *de jure* specificity, that is, specificity apparent on the face of the legislation.

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162 47 Fed. Reg. 42,422, at 42,424.

163 47 Fed. Reg. 39,332, at 39,335.

164 49 Fed. Reg. 47,284, at 47,287.

165 Panellists Weiler and Dearden agree with the remand order of the Panel majority, *infra*, however for different reasons, as set out at footnote 375, *infra*.

166 FPC v. Texaco, 417 U.S. 380, 397.

A review of the legislation referred to by Commerce in the *Final Determination*, however, reveals no such identification of program recipients. Section 135 of the British Columbia *Forest Act*[167] provides that, unless an exemption is obtained, timber harvested in the province must be either used in British Columbia or manufactured into either lumber, other sawn wood products, shakes, shingles, veneer, plywood, other wood-based panel products, pulp, newsprint, paper, poles, fence posts, Christmas trees, small sticks, ties, or mining timbers.

Exemptions to the log export restrictions may be granted by the Lieutenant Governor in Council (*i.e.*, the provincial cabinet) under section 136 for certain species or volumes of timber. Applications based on volume cannot exceed 15,000 cubic metres. Before granting the exemption, the Cabinet must first be satisfied that the timber or wood residue is either "surplus to requirements of timber processing facilities in the Province", cannot be processed economically or transported economically to a processing facility, or that an exemption would improve the utilization of timber cut from Crown land. Section 137 provides that exemptions may be made subject to certain fees and conditions.

Based on these provisions, Commerce concluded that "the BC log export restrictions, on their face, benefit only BC users of logs". As seen above, however, the legislation deals entirely with the forms in which timber may or may not be exported from the province, and the conditions under which an exemption might be obtained. The restrictions apply equally to all citizens, corporate and individual, of British Columbia. The only thing that is identified on the face of the legislation is timber products which, unless restricted therefrom under other legislation, may be freely exported by anyone in the province. Not only the producers of the manufactured products are subject to the regulations, but anyone who may wish to deal in logs for the export trade. Furthermore, there is nothing in the legislation to indicate the degree to which the export of raw logs will actually be restricted, as this depends upon the actual circumstances regarding the requirement for logs in the province, the

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[167] R.S.B.C. 1979, c. 140, as am.

location of processing facilities, transportation costs, and forestry practices on Crown lands, as well as on the exercise of cabinet discretion.

In the *Final Determination*, Commerce concluded that, "[t]he BC log export restrictions, on their face, benefit only BC users of logs".[168] Earlier, in its discussion of whether the log export restrictions constituted countervailable subsidies, however, Commerce said that:

> ... [b]ecause BC does not maintain direct control over the log prices through the imposition of its export restrictions, the Department determines that the BC export restriction scheme constitutes indirect, rather than direct, government action. Nonetheless, this indirect scheme, as demonstrated below, has the effect of reducing the production costs of BC softwood lumber manufacturers.[169]

Commerce itself realized, therefore, that the alleged benefits could only be conferred indirectly, through the functioning of the market, rather than as dictated by the legislation. If the program in fact was operated by the Lieutenant Governor in Council so as to significantly restrict the export of raw logs (a determination which itself requires looking at the degree to which government discretion affects the operation of the program), and in fact has the economic effect alleged (*i.e.*, that of increasing the supply of raw logs and therefore lowering their price in the B.C. market), then the users of such logs would in fact be the beneficiaries. Such a conclusion depends upon a *de facto* analysis, however, that the "subsidy ... in fact is provided to" a specific group of industries.

In this case, the referenced sections of the *Forest Act* do not explicitly confer any benefits at all. Without any apparent benefits, there can be no apparent beneficiaries. It is simply illogical, in the opinion of this Panel, for Commerce to argue, as it has, that a rule which operates only indirectly through market mechanisms to the benefit of certain market actors can be said to directly identify these same actors as program recipients.

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168 57 Fed. Reg. 22,570, at 22,610.

169 *Ibid.* at 22,609.

According to counsel for the Coalition,

> ... [w]hat you have here is on the face of the statute, you tell people you're not allowed to export logs. You have to produce them into these products. The Department does have to make an economic leap here, but it's a fairly minor leap, which is if these export restrictions act to keep the log price down, and that goes to causation and measurement, then the person who utilizes those laws, by definition of the statute will get the benefit. It's not much of a leap for *de jure* specificity.[170]

With all due respect to Commerce and the Coalition, the "minor" leap between a commodity export restriction which applies to every actor in the British Columbia economy and an economic impact[171] upon the group of enterprises which use that commodity as an input, is the very sort of effects analysis upon which *de facto* specificity is based. The programs benefits are not apparent on the face of the legislation. To say that the restrictions *de facto* operate to the benefit of the producers of timber products is far too great a leap for *de jure* specificity.

Even if we were of the opinion that the statute could reasonably support the conclusion reached by Commerce in this instance, we would be forced to remand this finding to the Department on the grounds that it has failed to provide a reasoned basis for its conclusions. There is no discussion or analysis of the legislation in either of the *Preliminary* or *Final Determinations*. Commerce merely asserts that the legislation supports the conclusions reached. As the Canadian Complainants' Joint Brief points out,[172] "[a]n ultimate finding in the statutory language is not enough

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170 Transcripts of Oral Hearing, (February 12, 1993) at 192-93.

171 The effects of the restriction depend upon the manner in which the Lieutenant Governor in Council exercises its discretion to grant exemptions. The restrictions may or may not be operated in such a way as to significantly restrict log experts, a point which is highlighted by the finding of Commerce in this case that the log export restrictions in Ontario, Québec and Alberta did not actually operate to significantly reduce the flow of exported logs from those provinces.

172 at IV.B-60.

in the absence of a basic finding to support it". In other words, a legal conclusion in the statutory language must be backed up by evidentiary conclusions in support.[173]

The only support given by Commerce for its legal conclusion of *de jure* specificity is the citation of its own finding of specificity in Leather from Argentina.[174] The sum total of the specificity analysis in that case consists, however, of the following passage:

> The embargo applies only to cattle hides, which are sold primarily, if not exclusively, to leather tanners. Thus, we determine that the embargo is limited to a specific industry and is, therefore, countervailable to the extent that it has caused hide prices to be lower than they would have been absent the embargo.[175]

The words "*de jure*" do not appear in this passage and the legislation is not so much as referred to. The preceding paragraph, discussing the background to the investigation, does reveal that the Resolution which implemented the embargo spoke of the need "to negotiate measures to maintain the volume of supply of raw materials adequate to the needs of the domestic market of the leather tanning and manufacturing sector". It is not clear from this, however, whether the embargo itself referred to leather tanners as the intended beneficiaries of the embargo. At best, whether the above finding of specificity was made on the basis of a *de jure* or a *de facto* analysis is unclear. At worst, this passage itself reflects the type of conclusory assertion, devoid of any analysis of the relevant legislation or the record evidence, that is evident in Commerce's *de jure* specificity analysis in this case.

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173 SCM Corp. v. United States, 487 F. Supp. 96, 104 (Cust. Ct. 1980).

174 55 Fed. Reg. 40,212 (1992).

175 *Ibid.* at 40,213.

(iii) Remand

The Panel was not persuaded that the record evidence met the requirement of *de jure* specificity and, therefore, the Panel remands the *Final Determination* to Commerce to review the record and establish whether the log export restrictions are *de jure* specific or *de facto* specific.

D. The Economic Theory of Log Export Restrictions as a Subsidy

Commerce based its determination that B.C.'s log export restrictions constitute a countervailable subsidy upon the economic theory that the restrictions enable B.C. softwood lumber producers to purchase logs at less than they would have to without the restrictions. British Columbia's log export restrictions consist of (1) restrictions of the quantity of logs that may be exported and (2) a tax on exported logs up to 100% of the difference between the export and domestic log price. B.C.'s log export restrictions are contained in Part XII of the *Forest Act*[176] and implementing regulations.[177]

Briefly, the economic theory relied on by Commerce holds that these restrictions segment the market for B.C. logs into two markets: a domestic market and an international market. Because the supply of B.C. logs to the international market is restricted, the price of logs in that market is higher than it would be in absence of the restrictions. Conversely, because the supply of B.C. logs in the domestic market contains logs that, in the absence of the restrictions, would be supplied to the international market, the price of logs in the domestic market is lower than it would be in the absence of the restrictions. In short, B.C. softwood lumber producers are able to purchase logs at a lower price than they would in the absence of the restrictions. Because the restrictions lower the cost to B.C. softwood lumber producers, they enable the B.C. softwood lumber producers to produce larger quantities at lower prices than they otherwise would.

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[176] R.S.B.C. 1979, c. 140, as am., ss. 135-37.

[177] B.C. Reg. 262/88.

It is clear from comments by a B.C. legislative committee, placed on the Administrative Record, that B.C.'s log export restrictions are intended to benefit B.C. softwood lumber producers. The B.C. Select Standing Committee on Forests and Lands has stated "[t]he reduced overall demand for logs resulting from arbitrarily restricting log exports provides the domestic processing sector with a lower log price."[178] Because Commerce is not required to demonstrate "intent" in order to impose a countervailing duty, these comments have limited legal relevance to the Panel's decision.[179] They do, however, support the argument that B.C.'s log export restrictions were intended to benefit B.C. softwood lumber producers.

Commerce stated in the *Final Determination*, "the B.C. export restrictions have been in place continuously since 1906."[180] The long history of B.C.'s log export restrictions, despite protests from Canadian economic actors who have felt themselves put at a competitive disadvantage by the programs, further attests to their efficacy.

E. Pre-Leather Interpretations of "Subsidy"

In the *Final Determination*, Commerce recognized that prior to "its final determination in [Argentine] Leather, the longstanding and consistent administrative practice of both the U.S. Department of Treasury (Treasury), the previous administrator of the U.S. countervailing duty law, and the Department was that border measures, such as export restrictions, generally did not constitute countervailable subsidies as a matter of law."[181] It will be useful to consider this previous administrative practice, as well as recent decisions in which Commerce, prior to issuing the *Final*

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178 "*Forest Act* - Part XII (Log Exports) and the Vancouver Log Market," Second Report of the British Columbia Select Standing Committee on Forests and Lands. 4th Sess., 34th Parl., Legislative Assembly of British Columbia (1991).

179 The relevance they do have is limited to Commerce's determination that B.C.'s log export restrictions were "specific" under the meaning of 19 U.S.C. § 1677(5)(A)(ii).

180 55 Fed. Reg. 22,570 at 22,610.

181 *Ibid.* at 22,606.

Determination, departed from this previous practice and adopted a new practice with respect to "border measures".

(i) Litharge from Mexico[182]

In Litharge from Mexico the Treasury Department refused to countervail a Mexican export-tax scheme that had the effect of reducing the price of [refined lead, the major input product] used in the manufacture of [litharge,] the final product under investigation."[183]

This determination was subsequently overturned in Hammond Lead Products, Inc. v. United States.[184] Hammond Lead was itself overturned by the U.S. Court of Customs and Patent Appeals[185] (the "CCPA") on the procedural ground that the statute as it then existed did not create a right to challenge negative countervailing duty determinations.

Congress reacted to this procedural ruling by the CCPA by "providing U.S. petitioners with the right to challenge negative final countervailing duty determinations in the *Trade Act of 1974*."[186] Simply because the procedural basis for the CCPA's decision overturning Hammond Lead was itself overturned by Congress does not, in itself, confirm that Congress endorsed the decision reached by the Customs Court in Hammond Lead. Congress expressed no view on the merits or demerits of the

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182 67 Treas. Dec. 142 (1967).

183 57 Fed. Reg., 22,570 at 22,607.

184 306 F. Supp. 460 (Cust. Ct. 1969).

185 Hammond Lead Products, Inc. v. United States, 440 F.2d 1024 (C.C.P.A. 1971), *cert. denied*, 404 U.S. 1005.

186 *Final Determination*, 57 Fed. Reg. 22,570 at 22,606; see Pub. L. 93-618, 88 Stat. 1978, 2041 (1975). codified at 19 U.S.C. § 1516; *see also* H.R. 15794, 92d Cong., 2d Sess. section (e) (1972).

Customs Court's decision overturning Treasury's determination in Litharge from Mexico.[187] Just as Congress's decision to overturn the CCPA did not necessarily constitute an endorsement of the decision of the Customs Court, the reversal on procedural grounds by the CCPA did not necessarily constitute an adjudication of the merits of the argument below.[188]

The fact that Congress offered no view on the merits of Litharge from Mexico and Hammond Lead means that the determination and the judicial and legislative events it stimulated offer little instruction in resolving the question of whether certain border measures such as export-tax schemes may constitute countervailable subsidies. If Congress's actions offer little guidance on the substance of the question, they are instructive on the manner in which the uncertainty is to be resolved. In this particular legislative context, congressional silence on the substantive question constitutes, in Commerce's view, an implicit delegation of authority to the administering agency to continue to construe the statute appropriately. Commerce believes that this is confirmed by the legislative history surrounding the *Trade Act of 1974*. As Commerce noted in the *Final Determination*,

> ... [i]n reporting an amended bill designed to overturn the CCPA's procedural ruling in Hammond Lead. [sic.] the Senate Finance Committee stated in pertinent part:
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> > "The Committee believes that American producers as well as importers should be permitted to have the right to judicial review in countervailing duty cases as a matter of basic equity and fairness, and as a means to secure

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187 *Final Determination*, 57 Fed. Reg. 22,570 at 22,606; see also H.R. 15794, 92d Cong., 2d Sess. section (e) (1972); S. Rep. No. 3964, 92d Cong, 2d Sess. section (e) (1972) (statement of sponsor Rep. Fulton); 118 Cong. Rec. 29,698 (1972) (statement of Sen. Fannin introducing a bill to overturn the procedural ruling in Hammond Lead.). In considering this legislative history, it is important to note, as Commerce did, that "[a]lthough the House-Senate conferees accepted the amended bill, the `bill was not brought to a vote in the House as an accommodation to the Secretary of the Treasury, with the understanding that the matter would be given attention in the context of trade legislation in the next Congress.' ASG Industries, Inc. v. United States, 467 F. Supp. 1200, 1229 (Cust. Ct. 1979 (citing H.R. Rep. 92-1583, 92d Cong., 2d Sess. (1972); S. Rep. 92-1298, 92d Cong., 2d Sess. (1972); 118 Cong. Rec. 37,098 (1972). `While the Executive Branch's trade legislation proposal of April 1973 contained no provision for judicial review of negative countervailing duty determinations, Congress provided one in the Trade Act of 1974." *Ibid.* (citing H.R. Rep. 93-571, 93d Cong., 1st Sess. 76 (1973); S. Rep. 93-1298, 93d Cong., 2d Sess. 183 (1974))." *Final Determination*, 57 Fed. Reg. 22,570 at 22,607-08, n.18.

188 Mutual Life Insurance Co. v. Hill, 193 U.S. 551, 553-554 (1904); *Final Determination*, 57 Fed. Reg. 22,570 at 22,606.

> administration of the law in keeping with the intent of Congress reflected in the broad, explicit and mandatory terms [*i.e.* `bounty or grant'] used in section 303."[189]

Thus, the determination in Litharge from Mexico stands for two propositions: (1) the previous practice of the Treasury Department had been to exclude border measures such as export-taxes from the definition of "subsidy" under 19 U.S.C. § 1677(5)(A); and (2) the legislative reaction to the Court of Customs and Patent appeals decision suggests that Congress preferred to leave the question of whether border measures such as export-tax schemes constituted "subsidies" to determination by the administering agency.

(ii) Anhydrous and Aqua Ammonia from Mexico[190]

In Anhydrous and Aqua Ammonia from Mexico, Commerce refused to countervail a Mexican export tax scheme in which natural gas was taxed but ammonia, a derivative of natural gas, was not. Petitioners argued that Commerce was bound by the decision of the Customs Court in Hammond Lead Products, Inc. v. United States.[191] Commerce rejected that argument.[192]

In the *Final Determination*, Commerce cited Anhydrous and Aqua Ammonia from Mexico for the propositions that "the long standing and consistent administrative practice... was that border

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189 *Final Determination*, 57 Fed. Reg. 22,570 at 22,608 (quoting S. Rep. No. 92-1221, 92d Cong., 2d Sess. 8 (1972) (emphasis added by Commerce)).

190 46 Fed. Reg. 28,522 (1963) at 28,524-25.

191 306 F. Supp. 460 (Cust. Ct. 1969), *rev'd on procedural grounds*, 440 F.2d 1024 (C.C.P.A.), *cert. denied*, 404 U.S. 1005 (1971).

192 Anhydrous and Aqua Ammonia from Mexico, 46 Fed. Reg. 28,522, 28,524-25 (1963).

measures... generally did not constitute countervailable subsidies as a matter of law,"[193] and that "pre-Leather determinations employ tautological reasoning."[194]

Anhydrous and Aqua Ammonia from Mexico is, indeed, an instance of Commerce refusing to countervail a border measure. Anhydrous and Aqua Ammonia from Mexico implies, however, that some border measures may be countervailable. Commerce found that the export tax program in this case was not countervailable because it was not specific and because there was no evidence that the program lowered the domestic price of natural gas, not simply because it was a "border measure."[195] If those variables had been otherwise, the determination, it seems, would have been different.

As for the second proposition, Anhydrous and Aqua Ammonia from Mexico rejects the reasoning of Hammond Lead as "untenable on its face, and unsupported by the Act and its legislative history."[196] Commerce reasoned that the "logic" of Hammond Lead:

> ... would lead us to conclude that the imposition or nonimposition of virtually any disadvantage is or may be [a] subsidy. Any time a government intervened at the border--such as with export taxes, import duties, or quantitative import or export restriction[s] on a product used as an input in further production--such action arguably could increase the quantities (and possibly lower the prices) of the domestically produced input product available in further production.[197]

Anhydrous and Aqua Ammonia from Mexico supports the second proposition only in the course of its discussion of Hammond Lead. Although Commerce was there critical of Hammond Lead, it

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193 57 Fed. Reg. 22,570 at 22,606.

194 *Ibid.* at 22,606, n.13.

195 Anhydrous and Aqua Ammonia from Mexico, 46 Fed. Reg. 28,522 at 28,525.

196 *Ibid.*

197 *Ibid.* at 28,524-25.

declined to follow Hammond Lead because it had been reversed.[198] The statement in Anhydrous and Aqua Ammonia from Mexico that the argument to include border measures within the definition of countervailable subsidy is "untenable on its face, and unsupported by the Act and its legislative history" may, therefore, be characterized as *obiter dictum*.

(iii) Non-Rubber Footwear from Argentina[199]

In Non-Rubber Footwear from Argentina Commerce determined that an export tax on hides did not constitute a countervailable benefit because Argentine purchasers of hides did not constitute a specific group of industries within the meaning of 19 U.S.C. § 1677(5)(A)(ii).[200] Commerce continued,

> ... even if we were to consider the users of leather to be a "specific group of enterprises or industries," we would still find the export tax not to be countervailable. The domestic parties' argument is based upon the assumption that the government caused the Argentine price of the input to the non-rubber footwear industry to drop through the use of the export tax (because less was exported, domestic supply increased and the per unit price fell). Actual prices, however, depend upon a complicated interaction of domestic and international supply and demand elasticities. Absent a showing of an actual reduction in the input price, we cannot conclude that the export tax has reduced the domestic price of hides.[201]

In the *Final Determination*, Commerce cites Non-Rubber Footwear from Argentina for the proposition that "the long standing and consistent administrative practice ... was that border measures ... generally did not constitute countervailable subsidies as a matter of law."[202] The use of the word

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198 *Ibid.* at 28,524.

199 49 Fed. Reg. 9,922 (March 16, 1984).

200 *Ibid.* at 9,923.

201 *Ibid.* at 9,923.

202 57 Fed. Reg. 22,570 at 22,606.

"generally" in the *Final Determination* implies that in some instances border measures may constitute countervailable subsidies. The Majority of the Panel believes that Non-Rubber Footwear from Argentina fairly supports this reading of the proposition. Specifically, Commerce found that the Argentine export tax was not countervailable because it was not specific, not because it was *per se* a "border measure."

(iv) Galvanized Carbon Steel Sheet from Australia[203]

In Galvanized Carbon Steel Sheet from Australia, Commerce announced the initiation of a countervailing duty investigation with respect to alleged subsidies of galvanized carbon steel sheet.[204] Commerce also announced that it would not initiate an investigation of allegations "that the government of Australia provides subsidies to the steel industry by limiting steel imports, thus artificially raising domestic steel prices."[205] Commerce reasoned that it would "be an extreme and erroneous position to conclude that governmental action which in any way restricts imports of competing products necessarily subsidizes domestic industries producing such products."[206] Commerce continued, "[t]o conclude even that petitioner has made a valid *prima facie* allegation would be tantamount to concluding that every time any government, including the U.S. government, through duties, quotas, or otherwise acts to restrict imports of a product competing with a domestically produced product, it necessarily subsidizes."[207]

In the *Final Determination*, Commerce also cites Galvanized Carbon Steel Sheet from Australia for the propositions that "the long standing and consistent administrative practice ... was

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203 49 Fed. Reg. 8,657 (March 8, 1984).

204 *Ibid.* "Galvanized carbon steel sheet" includes "hot- or cold-rolled carbon steel sheet which has been coated or plated with zinc."

205 *Ibid.* at 8,658.

206 *Ibid.*

207 *Ibid.*

that border measures ... generally did not constitute countervailable subsidies as a matter of law,"[208] and that "pre-Leather determinations employ tautological reasoning."[209] The conclusory language of Galvanized Carbon Steel Sheet from Australia can indeed be fairly read to support both propositions.

F. Post-Leather Interpretation of "Subsidy"

(i) Leather from Argentina[210]

In Leather from Argentina, Commerce determined that an embargo on cattle hide exports constituted a countervailable domestic subsidy "to manufacturers, producers, or exporters in Argentina of leather."[211] Commerce stated that "[t]he rationale underlying that determination was that (1) the embargo on raw hides `applie[d] only to [raw] cattle hides, which are sold primarily, if not exclusively to leather tanners [and, therefore,] ... [was] limited to a specific industry,' and (2) the export embargo `caused hide prices to be lower than they would have been absent the embargo' and, thereby enabled the leather tanners to sell the finished product, leather, at a lower price."[212]

With respect to the second rationale, Commerce "held petitioners to an extremely high standard of proof, requiring them to substantiate their claim that the embargo had a direct and discernible effect on hide prices in Argentina."[213] Petitioners met this standard by providing,

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[208] 57 Fed. Reg. 22,570 at 22,606.

[209] *Ibid.* at 22,606, n.13.

[210] 55 Fed. Reg. 40,212 (Oct. 2, 1990).

[211] *Ibid.*

[212] 57 Fed. Reg. 22,570 at 22,606 (quoting Leather from Argentina, 55 Fed. Reg. 40,212 at 40,213-214).

[213] Leather from Argentina, 55 Fed. Reg. 40,212 at 40,213.

> ... substantial source and secondary documentation, demonstrating the comparability of Argentine, United Kingdom (U.K.), and U.S. hide quality; documenting U.S., U.K. and Argentine hide prices over 30 years; and outlining their analysis of how the embargo is linked directly with the price differential between Argentine hide prices on the one hand, and U.S. and U.K. hide prices on the other.[214]

This high standard may have been required because of the normative innovation in this case, but not necessarily as a regular feature in each subsequent application. This point will become relevant in our subsequent discussion.

G. The Interpretation of "Subsidy" in Lumber III

The Canadian Complainants argue that Commerce "erred as a matter of law in determining that log export regulations constitute a countervailable subsidy."[215]

(i) Departure from Previous Interpretation of "Subsidy"

It was argued that Commerce's interpretation of "domestic subsidy" under the *Tariff Act of 1979* to include export restrictions was inconsistent with Commerce's previous practice. The Canadian Complainants argue that, with one exception, Commerce's interpretation departs from "over one hundred years of its own established practice."[216] In light of the review conducted above, that is an arguable point, but as Commerce recognized in the *Final Determination*, it is "authorized to depart from a long-standing and consistent practice--provided that [it] (1) offers a reasonable and rational explanation for doing so, and (2) demonstrates that the new practice is not inconsistent with the applicable statute."[217]

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214 *Ibid.*

215 Canadian Complainants' Joint Brief at D-19.

216 Canadian Complainants' Joint Brief at D-12.

217 57 Fed. Reg. 22,570 at 22,606.

(a) Rationale for Departure

To depart from a previous interpretation, Commerce must provide a reasonable rationale for the departure. Should the Panel find that Commerce failed to provide a reasonable rationale for the departure from previous determinations, the appropriate remedy is to remand the determination to Commerce for a full determination.

The Canadian Complainants contend that Commerce "offered no reasonable basis for departing from its past interpretation."[218] As explained in the next paragraph, Commerce and the Coalition dispute this claim. It was also pointed out that Commerce "has not claimed that its statutory reinterpretation is based on new Congressional pronouncements" or on "changed factual circumstances."[219] Although U.S. administrative law permits an agency to depart from a previous interpretation of a statute upon new congressional pronouncements or changed circumstances,[220] nothing in U.S. administrative law prohibits departure in the absence of new congressional pronouncements or changed circumstances. Thus, these are sufficient, but not necessary, conditions for a departure.

Commerce justified its departure on the basis of an improved understanding of the nature of certain border measures. Previous determinations, Commerce noted, were tautological in their reasoning. They simply assumed that border measures were not countervailable. Commerce's current interpretation reasons that some border measures may confer a countervailable domestic subsidy. In so doing, Commerce's current interpretation reflects an improved understanding of the nature or

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218 Canadian Complainants' Joint Brief at D-1.

219 Canadian Complainants' Joint Brief at D-20.

220 State of Michigan v. Thomas, 805 F.2d 176, 18 (6th Cir. 1986) (EPA had rational basis to depart from prior approval of Illinois and Wisconsin fugitive dust emission rules on basis of data not available at time rules were approved).

effect of border measures. Other determinations did not hold that border measures were *per se* non-countervailable. On the contrary, some previous determinations implicitly recognized that border measures that confer a benefit on a specific enterprise or industry or group of enterprises or industries would be countervailable.

Commerce and the Coalition, on the other hand, argue that Commerce met this burden in the *Final Determination*.

In the *Final Determination*, Commerce stated that in its view "the pre-Leather administrative determinations finding border measures in general to be *per se* noncountervailable pursuant to U.S. law were wrongly decided as contrary to Congressional intent."[221] Commerce noted that these determinations "employ[ed] tautological reasoning; these determinations assume as a premise the very conclusion they are seeking to prove--that is, border measures in general, including export restrictions, *per se* are not countervailable pursuant to U.S. law."[222] The Canadian Complainants defend the pre-Leather interpretations. Far from "mere tautologies" the Canadian Complainants find these interpretations to "reflect [Commerce's] careful consideration."[223] Careful examination of the pre-Leather determinations reveals that their discussion of border measures is often *obiter dictum* and, more importantly, reasonably characterized as tautological.

It was also argued that the emphatic statements found in previous determinations are emblematic not of tautological reasoning but of the absurdity that would result if Commerce were to depart from its previous, pre-Leather interpretation of "subsidy."[224] The Canadian Complainants

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221 57 Fed. Reg. 22,570 at 22,606.

222 57 Fed. Reg. 22,570 at 22,606 n.13; see, *e.g.*, Galvanized Steel from Australia, 49 Fed. Reg. 8,658 (stating that "the absurdity of such a proposition is self-evident"); Anhydrous and Aqua Ammonia from Mexico, 48 Fed. Reg. 28,525 (stating that "[t]he proposition that such governmental actions necessarily confer bounties or grants is untenable on its face").

223 Canadian Complainants' Joint Brief at D-69.

224 *Ibid.* at D-66 to D-69.

challenge the interpretation "[u]nder the fundamental axiom that the law may not be interpreted so as to produce absurd results."[225]

The alleged absurdity of interpreting "subsidy" to include a border measure turns on the unwarranted assumption that the interpretation renders all border measures subject to countervailing duties. The Canadian Complainants claim, for example, that under the new interpretation Commerce would be required to impose a duty on Canadian lumber imports if the "United States were to tighten its log export restrictions."[226] It would seem, however, that Commerce would have little difficulty discerning from the language of 19 U.S.C. § 1677(5)(A)(ii) an intent to limit the definition of subsidy to "domestic subsidies." That is, even if the United States were to "subsidize" Canadian producers, this subsidy would not be countervailable. Thus, the "absurd results" feared by the Canadian Complainants are unlikely to result from Commerce's interpretation "[t]aken to its logical conclusion."[227]

The specific determination at issue renders export restrictions, not border measures generally, subject to countervailing duties. What is more, the determination does not render export restrictions generally subject to countervailing duties. The restraints at issue here are restrictions on the export of a primary input. Rendering such restraint potentially countervailable does not necessarily and in itself produce absurd results.

It strikes one as reasonable for Commerce to depart from an administrative practice that was the product of tautological reasoning. This is especially true where, as is the case here, Congress has

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225 See Canadian Complainants' Joint Brief at 13; see also United States v. Brown, 333 U.S. 18, 27 (1948) ("[n]o rule of construction necessitates . . . acceptance of an interpretation resulting in patently absurd consequences"); Ambassador Div. of Florsheim Shoe v. United States, 748 F.2d 1560, 1563 (Fed. Cir. 1984) (reversing agency determination which "produces absurd results, results that were not and could not have been within the contemplation of Congress").

226 Canadian Complainants' Joint Brief at D-2 and D-67.

227 Canadian Complainants' Joint Brief at D-67.

expressed its intent that the term "subsidy" be construed broadly. Commerce's adoption of rules that exclude, *per se*, certain types of government programs (if, in fact, this was the ratio of the cases reviewed) seems inconsistent with the grant of authority to construe the definition of "subsidy" broadly and with flexibility.

Given that Congress granted Commerce authority to construe the term "subsidy" broadly, Commerce's decision to depart from previous determinations applying a tautological, *per se* rule is reasonable. As Commerce has clearly set forth this rationale in the *Final Determination*, remand to Commerce for further explanation of its departure from previous administrative rulings would not appear to be necessary.

(ii) Statutory Authority for Current Practice

To depart from previous administrative practice, Commerce must also demonstrate that its departure is not precluded by the statute. The Canadian Parties argue that Commerce is precluded by statute from defining the term "subsidy" to include export restrictions. Commerce and the Coalition argue, on the other hand, that Commerce demonstrated that it is not precluded by statute from defining "subsidy" to include restrictions on the export of a primary input.

(a) *Tariff Act of 1979*[228]

To demonstrate that its definition of "subsidy" was not precluded by statute, Commerce began, naturally enough, with an analysis of the text of the *Tariff Act of 1979*.[229]

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[228] *Tariff Act of 1930*, Pub. L. 71-361, 46 Stat. 590 ch. 497, Title VII, § 771, as added July 26, 1979, Pub. L. 96-39, Title I, § 101, 93 Stat. 176, and amended Aug. 23, 1988, Pub. L. 100-418, Title I, § 1312, 102 Stat. 1184.

[229] 57 Fed. Reg. 22,570 at 22,607-09; see also United States v. Esso Standard Oil Co., 42 CCPA 144, 151 C.A.D. 587 (1955) (the logical starting point for an analysis of the agency's interpretation of a statute is the language of the statute itself); Canadian Complainants' Joint Brief at D-31 (conceding that Commerce "correctly notes that the `logical starting point' for its analysis of the term `subsidy' is the statute itself").

Commerce determined that as the log export "restrictions affect the production of all softwood lumber, whether sold in the B.C. domestic market or export markets," the restrictions "fall within the purview of the domestic subsidy provisions" of 19 U.S.C. § 1677(5)(A)(ii), rather than the export subsidy provisions of 19 U.S.C. § 1677(5)(A)(i).[230] Section 1677(5)(A)(ii) provides in relevant part:

> (A) In General.--the term "subsidy" has the same meaning as the term "bounty or grant" as that term is used in section 303 [of the Act], and includes, but is not limited to, the following:
>
> . . .
>
> (ii) The following domestic subsidies, if provided or required by government action to a specific enterprise or industry, or group of enterprises or industries, whether publicly or privately owned and whether paid or bestowed directly or indirectly on the manufacture, production or export of any class or kind of merchandise:
>
> (I) The provision of capital, loans or loan guarantees on terms inconsistent with commercial considerations.
>
> (II) The provision of goods or services at preferential rates.
>
> (III) The grant of funds or forgiveness of debt to cover operating losses sustained by a specific industry.
>
> (IV) The assumption of any costs or expenses of manufacture, production or distribution.[231]

Section 303 of the *Act* uses the term "bounty or grant" as follows:

> [W]henever any country ... shall pay or bestow, directly or indirectly, any bounty or grant upon the manufacture or production or export of any article or merchandise produced in such country, then upon the importation of such article or merchandise

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230 *Ibid.* at 22,607.

231 19 U.S.C. § 1677(5)(A) (1991).

> into the United States, there shall be levied and paid, in all such cases, in addition to any duties otherwise imposed a duty equal to the net amount of such bounty or grant ....[232]

Having recited these provisions, Commerce noted that they do not provide operative definitions of the terms "subsidy", "bounty" or "grant".[233] Nor, in Commerce's view, can these provisions be said to expressly preclude Commerce from determining that restrictions on the export of a primary input constitute a subsidy.

Commerce argues that in specifically electing not to define these terms, Congress implicitly authorized Commerce to define "subsidy". Where Congress has left a gap for an administrative agency, courts are to be deferential toward the agency's efforts to fill in the gap. This deference is not absolute, however. Commerce must define "subsidy" in a manner that is consistent with the statute.

Nothing in the statute explicitly or implicitly precludes Commerce from defining "subsidy" to include benefits indirectly bestowed by the government. On the contrary, the statute expressly provides that government programs which indirectly bestow a benefit are potentially countervailable. Similarly, nothing in the statute explicitly or implicitly precludes Commerce from defining "subsidy" to include non-pecuniary benefits. On the contrary, the statute lists examples of non-pecuniary benefits that may constitute subsidies: "[t]he provision of goods or services at preferential rates."[234]

There is no requirement that a government program bestow benefits in the form of legal tender in order for that program to meet the definition of "subsidy". First, this alleged requirement conflicts with the plain language of the statute. The provision of goods or services at preferential

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[232] 19 U.S.C. § 1303 (1991).

[233] *Final Determination*, 57 Fed. Reg. 22,510 at 22,607.

[234] 19 U.S.C. § 1677(5)(A)(ii)(II).

rates does not result in a transfer of legal tender, yet is clearly within the definition of "domestic subsidy".[235] Second, the alleged requirement conflicts with previous administrative practice. Commerce has previously held countervailable government programs that did not entail a financial transfer from the government to the recipient.[236] Third, the alleged requirement would unduly limit the scope of the word "indirectly".

Similarly, nothing in the statute explicitly or implicitly precludes Commerce from defining "subsidy" to include programs that do not cause the government to forego revenue. As Commerce noted in the *Final Determination*, "to determine whether a program is countervailable, [Commerce] examines the benefit to the recipient and not the cost to the donor".[237]

Nor does the statute limit the definition of "subsidy" to the four types of programs enumerated at 19 U.S.C. § 1677(5)(A)(ii)(I)-(IV). On the contrary, the statute expressly provides that the term "subsidy" "includes, but is not limited to" the types of programs enumerated.[238] Commerce has demonstrated that the legislative history surrounding the statute indicates that Congress did not intend to limit the definition of "subsidy" to the four enumerated programs.[239] The House Report to the 1979 legislation states:

> The Committee does not intend for this to be a comprehensive, exclusive enumeration of domestic practices which will be considered subsidies. It is a minimum list, an

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235 19 U.S.C. § 1677(5)(A)(ii)(II).

236 Potassium Chloride from Spain, 49 Fed. Reg. 36,424-25 (1984) ("While there is no direct outlay of government funds, the benefits conferred on the companies are the result of a government-mandated program to promote exports.").

237 Certain Textile Mill Products from Mexico, 54 Fed. Reg. 36,841 (1989) at 36,843.

238 19 U.S.C. § 1677(5)(A).

239 See *Final Determination*, 57 Fed. Reg. 22,570 at 22,608.

> identification, for purposes of clarification, of those practices which are definitely subsidies.[240]

The Senate Report to the 1979 legislation states,

> The reference to specific subsidies in the definition is not all inclusive, but rather is illustrative of practices which are subsidies within the meaning of the word as used in the bill.[241]

The statutory language and legislative history clearly demonstrate that Congress implicitly delegated to Commerce authority to define "subsidy" beyond the four programs enumerated in the statute. As previously noted, where Commerce has delegated authority to construe a statute to the administrative agency, courts are to be deferential to agency constructions. As previously noted, this deference is not absolute, for the agency's construction must be consistent with the Act.[242]

Commerce has long interpreted the definition of subsidy to include programs not enumerated at 19 U.S.C. § 1677(5)(A)(ii)(I)-(IV). In the *Final Determination*, Commerce noted that it "routinely countervails certain domestic practices that are not included on the list, such as domestic grants and domestic tax subsidies."[243]

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240 H.R. No. 96-317, 96th Cong., 1st Sess. (1979).

241 S. Rep. 96-249, 96th Cong., 1st Sess. (1979).

242 See S. Rep. No. 249, 96th Cong., 1st Sess 84 (1979) ("The definition of `subsidy is ' intended to clarify that the term has the same meaning which administrative practice and the courts have ascribed to the term `bounty or grant' under section 303 of the *Tariff Act of 1930*, unless that practice or interpretation is inconsistent with the bill.") (emphasis added).

243 57 Fed. Reg. 22,570 at 22,608; see Proposed Regulations, at 23,366, 23,380, 23,382; Carbon Steel Wire Rod From Spain, 51 Fed. Reg. 36,579 (Oct. 14, 1986) ("The grants were provided to the firms in the Basque region . . ."); Industrial Phosphoric Acid From Israel, 52 Fed. Reg. 25,447 (July 7, 1987) (domestic grants); Stainless Steel Cooking Ware from Korea, 51 Fed. Reg. 42,867 (Nov. 26, 1988) ("[e]xemption from acquisition tax on purchase of land, buildings, and capital equipment for firms establishing factories in rural areas . . . .").

Having concluded that Congress did not intend the list of programs at 19 U.S.C. § 1677(5)(A)(ii)(I)-(IV) to be exhaustive, Commerce was faced with the problem of interpreting the term "subsidy" in light of the illustrative list. To aid in this problem of statutory construction, Commerce turned to the doctrine of *ejusdem generis*. The doctrine of *ejusdem generis* provides that "where general words follow an enumeration of ... things, by words of a particular and specific meaning, such general words are not to be construed in their widest extent, but are to be held as applying only to ... things of the same general kind or class as those specifically mentioned."[244]

Although in this instance the general words are followed by an enumeration of things by specific words, it seems reasonable for Commerce to have concluded that while Congress did not intend to limit "subsidy" to programs identical to those listed, Congress may have intended to limit Commerce to the same general kind or class as those listed.[245] The legislative history confirms this intention. As Commerce indicated, the House Report to the *Tariff Act of 1979* stated:

> ... to the extent [that] the [four illustrative] enumerations [of a domestic subsidy] under this provision might provide a basis for expanding the present standard [such expansion must be] consistent with the underlying principles implicit in these enumerations [and only] then [can] the standard ... be so altered.[246]

In light of this clearly expressed intention, Commerce concluded that, *ejusdem generis* "demands the conclusion that, in order for a domestic practice not expressly identified in the statute to be countervailable, the practice in question must be similar in nature to, or like, the four illustrative categories of domestic subsidies."[247]

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[244] *Black's Law Dictionary* (6th ed. 1990) at 517 (citing United States v. LaBrecque, 419 F. Supp. 430, 432 (D.C.N.J. 1976)).

[245] See *Sutherland Statutory Construction* § 47.717 (5th ed. 1992).

[246] H.R. Rep. No. 317, 96th cong., 1st Sess. 74 (1979); S. Rep. No. 249, 96th Cong., 1st Sess. 85 (1979).

[247] 57 Fed. Reg. 22,570 at 22,608.

Employing the doctrine of *ejusdem generis*, Commerce proceeded to determine if export restrictions on a primary input fell within the definition of "subsidy". To do this, Commerce considered two of the enumerated programs from the list, the "provision of goods or services at preferential rates" and the "assumption of any costs or expenses of manufacture, production or distribution."[248] Commerce also observed that under the express terms of the statute, such programs may operate directly or indirectly. Applying the doctrine of *ejusdem generis*, Commerce stated that any program which resembles the indirect provision of goods at preferential rates or the indirect assumption of any costs of production would meet the definition of "subsidy". Commerce then found that B.C.'s log export restrictions indirectly "reduc[ed] the production costs of B.C. softwood lumber manufacturers."[249] As such, Commerce reasoned, B.C.'s log export restrictions are like the programs enumerated at 19 U.S.C. § 1677(5)(A)(ii)(II) and, (IV),[250] and Commerce concluded, may constitute "domestic subsidies".[251]

Commerce's application of the doctrine of *ejusdem generis* has been criticized.[252] The Canadian Complainants argue that the proper inquiry is not whether a given governmental program

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248 19 U.S.C. § 1677(5)(A)(ii)(II) and (IV).

249 57 Fed. Reg. 22,570 at 22,609.

250 Commerce did not state that B.C.'s log export program resembles the indirect provision of a good or service at preferential rates or the indirect assumption of a cost of production. Rather, Commerce observed that B.C.'s log export restrictions are like the indirect provision of a good or service or the indirect assumption of a cost of production because all three have the effect of indirectly reducing production costs. In so doing, Commerce comes very close to implying that any program which indirectly reduces production costs is like the programs enumerated at 19 U.S.C. § 1677(5)(A)(ii)(I)-(IV). At first glance this line of argument seems at odds with Commerce's earlier statement that "it is well settled that not all foreign government actions that confer a benefit to particular products or industries constitute actionable subsidies pursuant to the Act. Zenith, 562 F.2d at 1209, aff'd, 437 U.S. at 443." (*Final Determination*, 57 Fed. Reg. 22,570 at 22,607). Whether this line of argument is at odds with the "well settled" rule articulated in Zenith depends on whether all "benefits" result in "cost savings". Export subsidies (as opposed to domestic subsidies) would not result in a costs savings, but these are not the type of benefits the court had in mind in Zenith (since the court stated that not all government benefits . . . are countervailable under the Act, which includes export subsidies). It is not clear why Commerce did not state that B.C.'s log export restrictions resembled the indirect provision of a good at a preferential rate.

251 57 Fed. Reg. 22,570 at 22,609.

252 Canadian Complainants' Joint Brief at D-43 to D-48.

has effects similar to the enumerated programs, but whether a given governmental program has characteristics similar to the enumerated programs. The cogency of this criticism turns, it seems, on the ability of the Canadian Complainants to maintain a rigorous distinction between a program's characteristics and its effects. It seems reasonable to consider a program's effects to be just another of its characteristics. But even if the Panel were to recognize a rigorous distinction between a program's characteristics and its effects, the Canadian Complainants criticism would still seem unwarranted. In applying the doctrine of *ejusdem generis*, Commerce likens the effects of B.C.'s log export restrictions to the effects of the indirect provision of goods at preferential rates or the indirect assumption of any costs of production. At other points in the *Final Determination*, however, Commerce states its view that B.C.'s log export restrictions effectively ensure the supply of logs to B.C. softwood lumber producers at preferential prices.[253] It seems clear, therefore, that Commerce could have likened the "characteristics" of the log export restrictions to the "characteristics" of the enumerated programs, namely the indirect provision of goods at preferential rates.

It was further argued that Commerce "relies upon the Customs Court decision in Hammond Lead ... for both its `substance' as judicial `precedent' and its `contribution' to the 1979 Act's legislative history."[254] It is far from clear that Commerce "relied" upon Hammond Lead as either "judicial precedent" or "legislative history", however. Commerce's discussion of Hammond Lead is limited to six paragraphs.[255] In these paragraphs, Commerce discusses Hammond Lead primarily to determine whether Congress, in overturning the CCPA's procedural ruling addressed the merits of the case.[256] Noting that "Congress did not either approve or disapprove the Customs Court's decision on the merits", Commerce went on to conclude that "any attempt to divine Congress's intent concerning the substantive issue presented here from the Hammond Lead controversy is highly

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253 57 Fed. Reg. 22,570 at 22,609-610.

254 Canadian Complainants' Joint Brief at D-33.

255 57 Fed. Reg. 22,570 at 22,606-609.

256 *Ibid.* at 22,606.

questionable."[257] Commerce then proceeded to analyze the language and legislative history of the countervailing duty law.[258]

Also challenged was Commerce's reliance on United States v. Zenith Radio Corp.,[259] and ASG Industries, Inc. v. United States.[260] The Canadian Complainants argue that Commerce's reliance on Zenith was "misleading and inappropriate" and that Commerce "misconstrue[d]" ASG.[261]

Commerce, it will be recalled, relied on Zenith to supplement "historical background" demonstrating that "Congress itself ... had ascribed a somewhat broad meaning to the statutory terms `bounty or grant'".[262] The Canadian Complainants appear to maintain, however, that Commerce relied on Zenith to support its reading of ASG. They then argue that Zenith and, particularly, the Supreme Court's affirmance, actually undermines Commerce's reading of ASG.

Careful examination of the *Final Determination* reveals, however, that Commerce relied on Zenith for little more than insight into the legislative history of the phrase "bounty or grant". The passage cited by Commerce reads as follows:

> Congress' intent to provide a wide latitude within which the [Secretary] may determine the existence or nonexistence of a bounty or grant is clear from the statute itself, and from the congressional refusal to define the words "bounty," [or] "grant" ... in the statute or anywhere else, for almost 80 years.[263]

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257 *Ibid.* at 22,606, 22,607.

258 *Ibid.* at 22,607.

259 562 F.2d 1209 (C.C.P.A. 1977), *aff'd sub nom.*, Zenith Radio Corp. v. United States, 437 U.S. 443 (1978),

260 467 F. Supp. 1200 (Cust. Ct. 1979).

261 Canadian Complainants' Joint Brief at D-39 and D-40.

262 57 Fed. Reg. 22,570 at 22,608.

263 Zenith, 562 F.2d 1209 at 1216.

Commerce's limited reliance on Zenith appears reasonable.

Similarly, Commerce relied on ASG as "historical background" demonstrating "that, by the time Congress was drafting the subsidy provisions of the Trade Agreements Act of 1979 ... the [Customs Court] had concluded that foreign government programs that indirectly reduce a foreign manufacturer's production costs constitute countervailable subsidies."[264] It was maintained, however, that ASG stands for the more limited proposition that foreign government programs falling within the "classic" definition of subsidy are countervailable regardless of their purpose, provided their effect is to reduce the production costs of foreign manufacturers.[265]

The Panel is faced, therefore, with two alternative readings of ASG. The Canadian Complainants' reading is only persuasive if the holding in ASG is fairly limitable to governmental measures that are by their "nature" within the "classic" definition of a countervailable "bounty or grant." Close examination of the passage cited by Commerce in the *Final Determination* does not support such a limitation. That passage reads as follows:

> Unquestionably, the effect of these programs has been to reduce [the respondent's] cost of producing float glass. And whether the reduction in cost is occasioned by direct cash payments, or by an act of government reducing labor cost, capital cost, or the cost of any other factor of production is of no consequence. For if a benefit or advantage is received in connection with the production of the merchandise, that benefit or advantage is a bounty or grant on production. And to the extent that such bountied [sic] merchandise is exported to the United States, it comes squarely within our countervailing duty law--section 303.[266]

Commerce's reading of ASG relies on no such limitation. Further, Commerce's reading relates the holding in ASG to the language of the countervailing duty law, casting light upon the phrase "directly

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[264] 57 Fed. Reg. 22,570 at 22,608.

[265] Canadian Complainants' Joint Brief at D-39 to D-40.

[266] 467 F. Supp. 1200 at 1213 (emphasis added).

or indirectly." The Canadian Complainants' reading, by contrast, would limit this phrase to the "purpose" of the government program, excluding government programs that by "nature" are indirect. Nothing in the language or the legislative history of the statute supports such a limitation. It appears, therefore, that Commerce did not "misconstrue" ASG.

(b) Section 301

The Canadian Complainants rely on section 301 of the *Trade Act of 1974* for two arguments. First, they argue that section 301 precludes Congress from defining subsidy to include export restraints because export restraints are exclusively remedied under section 301. Second, they argue that section 301 maintains a distinction between "subsidies" and "restrictions on access to supplies of ... raw materials" and that this distinction supports interpreting "subsidy" under the countervailing duty law so as to exclude export restraints from the category of countervailable subsidies.

It was argued that far from implicitly delegating authority to Commerce to define "bounty or grant", Congress has long precluded Commerce "from construing the term `subsidy' to include export regulations."[267] There are really two steps to this argument. First, the Canadian Complainants must argue that Congress has provided that border measures such as export restraints be remedied under a separate statute. Second, the Canadian Complainants must argue that Congress intended this remedy to be exclusive.

It has also been argued that since 1974, Congress has provided that border measures including export restraints be subject to "a separate legislative regime."[268] Specifically, the Canadian Complainants argue that:

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[267] Canadian Complainants' Joint Brief at D-50.

[268] *Ibid.* at D-56.

> Section 301 of the 1974 Act introduced a sweeping provision intended to confront a variety of foreign unfair trade practices, expressly including export restraints. The provision afforded U.S. industry an avenue to pursue legal action against such practices.[269]

Section 301 of the 1974 *Act* authorizes action against, *inter alia*, the imposition of "unjustifiable or unreasonable restrictions on access to ... raw materials."[270] But it is by no means clear, from the text or the context, that Congress intended "unjustifiable or unreasonable restrictions on access to ... raw materials" to include export restraints. It seems more likely that Congress had in mind, say, a stumpage program that excluded American companies from those eligible for stumpage rights. No argument or legislative history has been presented to demonstrate that B.C.'s log export restrictions qualify as "restrictions on access to raw materials" (our emphasis) and so fall within the express terms of section 301.

Even assuming, *arguendo*, that B.C.'s log export restrictions are "restrictions on access to raw materials" which are actionable pursuant to section 301, it does not follow that they are not also actionable under the countervailing duty laws. Nothing in the plain language of section 301 indicates that Congress intended that practices identified in section 301 may only be remedied pursuant to that statute. On the contrary, amongst the "unfair trade practices" actionable under section 301 are "subsidies" which are clearly also actionable under the countervailing duty law.

Furthermore, the legislative history strongly suggests that Congress did not intend the jurisdiction of section 301 and that of the U.S. countervailing duty law to be "mutually exclusive." Rather, the legislative history suggests that the jurisdiction of the two statutes is concurrent for certain government practices. When section 301 was enacted in 1974, the Senate Report stated:

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269 *Ibid.* at D-56.

270 *Trade Act of 1974*, § 301(a)(4), 88 Stat. 1978, 2041.

> [B]efore any action should be taken under section 301 on subsidies of products to the U.S. market, the following determinations would have to be made:
>
> (1) The Secretary of the Treasury must determine that the country provides subsidies or other incentives having the effect of a subsidy on its exports to the U.S.;
>
> (2) The U.S. International Trade Commission must find that the subsidized exports have the effect of substantially reducing the sales of competitive products made in the United States; and
>
> (3) The President must find that the remedies available under the Antidumping Act and under the countervailing duty law are inadequate to deter the subsidization practices.[271]

No legislative history has been cited to support the proposition that foreign government practices which may be remedied pursuant to section 301 may not be remedied through other measures.

Moreover, previous administrative practice demonstrates that the jurisdiction of section 301 over unfair trade practices is not exclusive. In particular, the history of the cattle hide export embargo at issue in Leather from Argentina[272] demonstrates that jurisdiction over unfair trade practices is not limited to section 301. In October, 1981 the United States Trade Representative ("USTR") initiated a section 301 investigation into Argentina's breach of a 1979 agreement with the United States. The USTR later dropped the investigation after deciding "that the issue was more appropriately pursued under section 125 of the *Trade Act of 1974*, which gave the President the authority to terminate the 1979 U.S.-Argentina Agreement."[273]

The Canadian Complainants also argue that section 301 maintains a distinction between "subsidies" and "restrictions on access to supplies of ... raw materials" and that this distinction

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271 Sen Rep. No. 93-1298, 7304 (1974); Commerce Response Brief at J-46.

272 55 Fed. Reg. 40,212 at 40,213

273 *Ibid.*

supports interpreting "subsidy" under the countervailing duty law so as to exclude export restraints from the category of countervailable subsidies.

This argument runs into substantial difficulties. First, it is not clear that the phrase "restrictions on access to supplies of raw materials" includes "export restrictions" of the type here at issue. It seems more likely that this phrase was meant to include something like a stumpage program that excluded American firms from bidding for stumpage rights. No evidence was adduced to demonstrate that B.C.'s log export restrictions are, in fact, restrictions on access to supplies of raw materials actionable under section 301.

Even assuming, *arguendo*, that Congress intended the phrase "restrictions on access to supplies of raw materials" to include export restrictions, the fact that section 301 draws a distinction between subsidies and restrictions on access to supplies of raw materials does not preclude Commerce from interpreting "subsidy" to include export restrictions under the countervailing duty law. As Canadian Complainants rightly note, section 301 is a "separate legal regime."[274] Section 301 and the countervailing duty law are administered by wholly separate agencies. There is no requirement, under U.S. administrative law, that one agency interpret a statute in a manner similar to the way another agency interprets a separate statute.

(c) Natural Resources Subsidy Proposal

The Canadian Complainants argue that Congress "rejected efforts to expand the term `subsidy' ... to include border measures, including export restraints" when it declined to adopt a proposed amendment to Title VII of the *Trade Agreements Act of 1979*.[275] It was further argued that Congress

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[274] Canadian Complainants' Joint Brief at D-57.

[275] *Ibid.* at D-22 to D-23 and *Tariff Act of 1930*, Pub. L. 71-361, 46 Stat. 590 ch. 497, Title VII, § 771, as added July 26, 1979, Pub. L. 96-39, Title I, § 101, 93 Stat. 176, and amended Aug. 23, 1988, Pub. L. 100-418, Title I, § 1312, 102 Stat. 1184.

"rejected the notion that the countervailing duty law covered border measures such as export regulations."[276]

Neither of these arguments is supported by the legislative history cited. The Canadian Complainants argue that the proposed amendment was designed to reverse Commerce's determination in Anhydrous and Aqua Ammonia from Mexico.[277] Careful analysis of this determination, however, reveals that the failure of Congress to reverse the determination in no way precludes Commerce from expanding the definition of subsidy to include border measures.

In Anhydrous and Aqua Ammonia from Mexico, Commerce refused to countervail a Mexican export tax scheme in which natural gas was taxed but ammonia, a derivative of natural gas, was not. The Petitioners argued that Commerce was bound by the decision of the Customs Court in Hammond Lead Products, Inc. v. United States.[278] Commerce rejected that argument.[279]

The Canadian Complainants argue that the proposed amendment, a "natural resource subsidy" proposal, was intended to reverse Anhydrous and Aqua Ammonia from Mexico."[280] Even if this were true, the failure of Congress to adopt the proposed amendment does not constitute a rejection of the notion that the term "subsidy" may include border measures. Although Anhydrous and Aqua Ammonia from Mexico is, indeed, an instance of Commerce refusing to countervail a border measure, the determination implies that some border measures may be countervailable. Specifically, Commerce found the export tax program in this case was not countervailable because it was not specific and because there was no evidence that the program lowered the domestic price of natural gas, not simply

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276 Canadian Complainants' Joint Brief at D-23.

277 46 Fed. Reg. 28,522 (1963).

278 306 F. Supp. 460 (Cust. Ct. 1969), *rev'd on procedural grounds*, 440 F.2d 1024 (C.C.P.A.), *cert. denied*, 404 U.S. 1005 (1971).

279 Anhydrous and Aqua Ammonia from Mexico, 46 Fed. Reg. 28,522 at 28,524-25 (1963).

280 Canadian Complainants' Joint Brief at D-23,

because it was a "border measure."[281] If those variables had been otherwise, the determination, it seems, would have been different. Thus, if Congress's rejection of the proposed amendment constitutes an endorsement of the result in Anhydrous and Aqua Ammonia from Mexico, it must also be considered an endorsement of Commerce's implied statement that border measures may, in certain circumstances, be countervailable domestic subsidies.[282]

(d) Export Targeting Subsidy Proposal

The Canadian Complainants also argue that a second proposed amendment would have placed border measures within the scope of the countervailing duty law by including them within the definition of "export targeting subsidies" and by rendering "export targeting subsidies" subject to countervailing duties.[283] Under the proposed amendment, "exporting targeting subsidies", would have included

> ... any government plan or scheme consisting of coordinated actions ... that are bestowed on a specific enterprise, industry, or group ... the effect of which is to assist the beneficiary to become more competitive in the export of a class or kind of merchandise.[284]

Canadian Complainants argue that "[a]mong the examples of such "targeting" practices included in the proposed amendment was any government action affording `special protection [to] the home

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[281] 48 Fed. Reg. 28,522 at 28,525.

[282] It is true that Commerce, in its discussion of Hammond Lead, stated that the reasoning of Hammond Lead is "untenable on its face, and unsupported by the Act and its legislative history." (Anhydrous and Aqua Ammonia from Mexico, 48 Fed. Reg. 28,522 at 28,525). It is worth noting, however, that Commerce declined to follow Hammond Lead because it had been reversed, not because Commerce disapproved of its reasoning. The statement in Anhydrous and Aqua Ammonia from Mexico that the argument to include border measures within the definition of countervailable subsidy is "untenable on its face, and unsupported by the Act and its legislative history" may, therefore, be characterized as *obiter dictum*.

[283] See Canadian Complainants' Joint Brief at D-24 to D-25.

[284] H.R. 4784, 98th Cong., 2d Sess. § 104.

market'" including border measures such as tariffs, import quotas, and other non-tariff barriers to trade.[285]

The Canadian Complainants argue that this proposed amendment was "intended to deal with indirect forms of government assistance that do not involve a cash transfer but nevertheless have a subsidizing effect".[286] It was argued further that this amendment was understood by Congress to remedy a limitation in countervailing duty law, namely:

> ... [c]urrent countervailing duty law specifically addresses only those subsidies which involve a cash transfer to the particular industry from the government treasury, such as grants, loans or certain tax benefits.[287]

In 1988, Congress made "export targeting" an actionable practice under section 301 of the *Trade Act of 1974*.[288]

The Canadian Complainants argue that the export targeting subsidies proposal "was opposed by numerous members of Congress on the ground that it would render the definition of subsidy `so broad that it covers legitimate forms of government behaviour, including many programs of the U.S. government'.[289] It is precisely the breadth of the export targeting proposal that Congress found objectionable. Further opposition, quoted by the Canadian Complainants, maintained that:

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285 Canadian Complainants' Joint Brief at D-25 (quoting H.R. 4784, 98th Cong., 2d Sess. § 104 and citing Foreign Industrial Targeting and Its Effects on U.S. Industries - Phase I: Japan, Inv. no. 332-162, U.S. ITC Pub. No. 1437, at 3, 19, 62-63 (October, 1983) (study undertaken at the request of Subcommittee on Trade of the House Ways and Means Committee)).

286 H.R. Rep. No. 725, 98th Cong., 2d Sess. 7 (1984); Canadian Complainants' Joint Brief at D-26.

287 H.R. Rep. No. 725, 98th Cong., 2d Sess. 28 (1984).

288 19 U.S.C. § 2411(d)(3)(B)(ii) (1988).

289 Canadian Complainants' Joint Brief at D-27 (quoting H.R. Rep. No. 725, at 89).

> ... [s]ome of the practices defined as targeting, such as protection of home markets ... clearly are not subsidies under the Subsidies Code and should not be addressed under the countervailing duty law.[290]

This statement contains an implicit recognition by Congress that some of the practices defined as targeting may be subsidies and might be addressed under the countervailing duty law. Thus, Congress's concern that the export targeting proposal was over-broad was not necessarily a rejection of the notion that certain border measures, particularly export restraints, may fall within the scope of the countervailing duty law.

(e) GATT

The 1979 *Trade Agreements Act* was intended to implement United States obligations under the *General Agreement on Tariffs and Trade* ("GATT") and the *Subsidies Code* negotiated in the Tokyo Round of Multilateral Trade Negotiations ("GATT *Subsidies Code*").[291] Article 407 of the *FTA*, entitled "Import and Export Restrictions," incorporates Article XI, ¶ 1 of the GATT in the following language at paragraph (1):

> Subject to the further rights and obligations of this Agreement, the Parties affirm their respective rights and obligations under the General Agreement on Tariffs and Trade (GATT) with respect to prohibitions or restrictions on bilateral trade in goods.

The GATT, the GATT *Subsidies Code*, and GATT practice are therefore important aids in interpreting United States countervailing duty law. Commerce argues that "a careful reading of the GATT text demonstrates that border measures, such as export taxes or restrictions, can constitute

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[290] H.R. Rep. No. 725, at 90 (cited by the Canadian Complainants in their Joint Brief at D-27) (emphasis added).

[291] *Trade Agreement Act of 1979*, Statements of Administrative Action, at 392, 1979 U.S.C.C.A.N. at 667.

a `subsidy' within the meaning of articles VI or XVI of the GATT."[292] The Canadian Complainants challenge this argument.[293]

The Canadian Complainants argue that "each of the articles of the GATT is dedicated to addressing a particular area of international trade."[294] They argue further that these articles create "separate and independent regime[s]" governing different aspects of international trade,[295] and continue that because Article XI is dedicated to addressing the "General Elimination of Quantitative Restrictions," quantitative restrictions may only be addressed through Article XI.[296] In contrast, the Canadian Complainants argue, Articles XVI and VI address subsidies and "contemplate unilateral remedial action in the form of countervailing duties."[297]

It is important to note that the Canadian Complainants do not contend that each article creates a "separate and independent regime." This is clear because the Canadian Complainants acknowledge that Articles VI, XVI, and XXIII jointly address the problem of subsidies and their remedies.[298] The Canadian Complainants argue that the GATT *Subsidies Code* "covers only subsidies, as regulated by

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[292] 57 Fed. Reg. 22,570 at 22,611.

[293] Canadian Complainants' Joint Brief at D-59 to D-66.

[294] Canadian Complainants' Joint Brief at D-59.

[295] Canadian Complainants' Joint Brief at D-59.

[296] Quantitative restrictions on exports are disfavored by the *GATT*. Article XI, ¶ 1 of the *GATT* provides:

> No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licenses or other measure, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.

[297] Canadian Complainants' Joint Brief at D-60.

[298] Canadian Complainants' Joint Brief at D-60 to D-61.

GATT Articles VI and XVI and the nullification or impairment of GATT benefits through subsidies, as proscribed by Article XXIII."[299]

In the *Final Determination*, Commerce recognized this argument, citing Article 19, ¶ 1 as a potential source of the Canadian Complainants' argument that export restrictions are remediable exclusively under Article XI. Article 19, ¶ 1 of the GATT *Subsidies Code* provides:

> No specific action against a subsidy of another signatory can be taken except in accordance with the provisions of the General Agreement, as interpreted by [the GATT *Subsidies Code*].

Commerce continued, however, to observe that footnote 38 to Article 19, ¶ 1 provides that Article 19, ¶ 1 "is not intended to preclude action under other relevant provisions of the General Agreement where appropriate."[300]

This footnote seems to recognize that a "subsidy" may also be remedied under another Article of the GATT. This appears to refute the Canadian Complainants contention that Articles VI and XVI create a "separate and independent regime." That is, a "subsidy" may, where appropriate, be remedied through Articles of the GATT other than VI and XVI. The Canadian Complainants dispute Commerce's interpretation of Article 19. They argue that the footnote in question "is intended to permit actions against subsidies which, although not violating the obligations of the Code, might nonetheless nullify or impair a party's rights under other provisions of the GATT."[301] But there is no basis in the text of the footnote or Article 19 of the GATT *Subsidies Code* for reading the parenthetical clause "although not violating the obligations of the Code" into the footnote.

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299 *Ibid.*

300 57 Fed. Reg. 22,570 at 22,611.

301 Canadian Complainants' Joint Brief at D-65.

Because neither the GATT nor the GATT *Subsidies Code* can be read to preclude defining "subsidy" to include certain export restrictions, Commerce's conclusion that "[n]either the GATT drafters nor the GATT *Subsidies Code* drafters squarely addressed the issue of whether export restrictions constitute an actionable `domestic subsidy' within the meaning of GATT seems reasonable.[302]

The question remains whether Commerce's interpretation under the GATT of the term "subsidy" to include export restrictions is reasonable.

Commerce noted that neither the GATT nor the GATT *Subsidies Code* expressly excludes export restrictions from the definition of countervailable subsidy.[303] This, Commerce argues, is telling because the GATT drafters clearly knew how to exclude:

> "... certain government measures from the coverage of the term `subsidy'. Specifically, Article VI of the GATT provides,
>
> > No product of the territory of any contracting party imported into the territory of any other contracting party shall be subject to anti-dumping or countervailing duty by reason of the exemption of such product from duties or taxes borne by the like product when destined for consumption in the country of origin or exportation, or by reason of the refund of such duties or taxes.[304]

To demonstrate the reasonableness of its interpretation, Commerce cites the non-exhaustive list of illustrative domestic subsidies set forth in the GATT *Subsidies Code*.[305] The GATT *Subsidies Code* there provides,

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302 Commerce's Response Brief at J-114.

303 Commerce's Response Brief at J-117 to J-118.

304 *GATT*, Art. VI, para. 4.

305 Commerce's Response Brief at J-115.

> Signatories recognize that the objectives mentioned in paragraph 1 above may be achieved, *inter alia*, by means of subsidies granted with the aim of giving an advantage to certain enterprises. Examples of possible forms of such subsidies are: government financing of commercial enterprises, including grants, loans or guarantees; government provision or government financed provision of utility, supply distribution and other operational or support services or facilities; government financing of research and development programmes; fiscal incentives; and government subscriptions to, or provision of, equity capital.[306]

Applying the doctrine of *ejusdem generis*, Commerce observed that "[t]he common or similar element shared by each of the five illustrative examples of domestic subsidies set forth in the Code is that foreign recipients enjoy a cost savings that they otherwise would not enjoy in the absence of government intervention in the free marketplace."[307] Commerce found that "B.C.'s log export restrictions share the same common element (i.e., cost savings) that generally characterizes the illustrative examples of domestic subsidies set forth in the GATT *Subsidies Code*."[308] This interpretation appears to be reasonable.

The Canadian Complainants argue that "a 1960 GATT panel established to review the operation of Article XVI of the GATT regarding disciplines on subsidies addressed the precise issue raised by [Commerce's] final determination--whether a quantitative restriction constitutes a `subsidy' within the meaning of the GATT."[309] In that report the panel discussed the operation of price support programs maintained through quantitative restrictions on imports. The panel stated that "[i]n such a case there would be no loss to the government, and the measure would be governed not by Article XVI, but by the other relevant Articles of the General Agreement."[310]

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306 *GATT Subsidies Code*, Art. 11, para. 3.

307 Commerce's Response Brief at J-116.

308 Commerce's Response Brief at J-117.

309 Canadian Complainants' Joint Brief at D-61; Review Pursuant to Article XVI:5, Report by the Panel adopted 24 May 1960, *GATT* Doc. L/1160, BISD 95/188 (1961) ("*GATT* Panel Report")

310 *Ibid.*

This statement does not preclude Commerce from defining "subsidy" to include export restrictions. First, the panel's statement was not essential to the holding. It was, therefore, *obiter dictum*, and of no binding effect. Second, the panel addressed the problem of an import restriction that raised the price of an input -- benefitting suppliers of the input at the expense of processors of the input. B.C.'s log export restrictions concern export restrictions that suppress the price of an input--benefitting processors of the input at the expense of suppliers. At first glance, it might appear that the reasoning of the GATT panel would apply to export restrictions as well as import restrictions. But it is not persuasive. The two situations may easily be distinguished in that a countervailing duty is designed to deprive a subsidized producer of a benefit. In the case of import restrictions, a countervailing duty would not deprive the recipient of the benefit. Rather, a countervailing duty would impose additional hardship on the processor of the price-supported input without depriving the supplier of the input of the benefit received by virtue of the price supports. By contrast, in the case of export restrictions, a countervailing duty would deprive the recipient of the benefit received by virtue of the suppressed price of the input.[311]

(iii) Application of Current Interpretation

(a) The Existence of a Subsidy

Commerce, "[h]aving established that the BC export restrictions can be considered a `domestic subsid[y]' practice within the meaning of the [Tariff Act of 1979]," sought to establish whether B.C.'s log export restrictions conferred a benefit on B.C. producers of softwood products.[312] According to Commerce, it sought "to determine whether there is a proximate causal relationship or correlation (i.e., regression analysis) between the BC export restrictions and the domestic price of BC

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311 Commerce's Response Brief at J-118 to J-119. There is a degree of unclarity here. Commerce did not, in its *Final Determination*, draw a distinction between import restrictions and export restrictions. Rather, Commerce simply discussed "border measures." There is no doubt that the *Final Determination* concerned export restrictions, however.

312 57 Fed. Reg. 22,570 at 22,609 (emphasis added).

logs."[313] Commerce then volunteered an alternative formulation: "In other words, we must ascertain whether these restrictions have a `direct and discernible effect' within the meaning of Leather upon the price of BC logs."[314]

This alternative formulation did not, unfortunately, aid in clarification. It has been the source of much disagreement.[315] By adopting the alternative "direct and discernible effect" formulation, throughout the remainder of the *Final Determination*, Commerce presumably sought to underscore a continuity between the *Final Determination* and Leather from Argentina. In offering the alternative formulation, Commerce seemed to imply (1) that "proximate causal relationship" would be satisfied by a showing of a "direct" effect; (2) that "correlation (*i.e.*, regression analysis) between the BC export restrictions and the domestic price of BC logs" would be satisfied by a showing of a "discernible" effect;[316] and, most importantly, (3) what may have been disjunctive requirements appear to have been transformed into conjunctive requirements.[317] In fact, Commerce's efforts at clarification engendered confusion.

Commerce seems to have been aware of this potential confusion. With respect to the first consequence of the alternative formulation, the equation of "proximate causal relationship" with "direct ... effect," Commerce seems to have been aware that use of the word "direct" seemed

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313 57 Fed. Reg. 22,570 at 22,609.

314 *Ibid.* at 22,609 (quoting Leather from Argentina, 55 Fed. Reg. 40,212 at 40,213).

315 Canadian Complainants' Joint Brief at D-74 to D-94.

316 Particularly as the existence of a discernible effect was demonstrated in Leather from Argentina through regression analysis. *Final Determination*, 57 Fed. Reg. 22,570 at 22,609 n.23 (discussing regression analysis employed in Leather from Argentina).

317 *Final Determination*, 57 Fed. Reg. 22,570 at 22,609 ("proximate causal relationship or correlation (*i.e.*, regression analysis) between the BC export restrictions and the domestic price of BC logs" (emphasis added) Leather from Argentina, 55 Fed. Reg. 40,212 at 40,213 ("direct and discernible effect" (emphasis added)).

inconsistent with the finding that export restrictions indirectly benefit B.C. softwood producers.[318] By acknowledging that the "direct and discernible effects" standard was used in Leather from Argentina to determine whether a program that provided indirect benefits was countervailable, Commerce seems to indicate that the meaning of "direct effects" expands to mean "indirect effects" when the program being investigated provides indirect benefits. This is not a legally satisfactory use of the language.

Confusion has also been created by the second and third consequences of the alternative formulation. By equating "discernible effects" with "correlation analysis (i.e., regression analysis)," and by transforming disjunctive requirements into conjunctive requirements, Commerce seems to have required demonstration through regression analysis that B.C.'s log export restrictions affect the price of B.C. logs.[319] This creates several problems. First, the study on which Commerce relies to demonstrate "discernible effects" contains no regression analysis which could demonstrate any causal link between any correlation.[320] Second, and more fundamental, where the program has been in place and relatively unchanged for a long period, regression analysis will not be possible.[321] If there has

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[318] 57 Fed. Reg. 22,570 at 22,609 n.23 ("The standard that we used in Leather--the `direct and discernible effect' standard--attempted to determine whether the border measure in that case, an export embargo, had a direct effect on the price of the input product, raw hides, even though we recognized that the effect upon the processed product under investigation was indirect" (Leather from Argentina, 55 Fed. Reg. 40,212 at 40,213-214)).

[319] Indeed, Canadian Complainants challenge Commerce on precisely this ground: Canadian Complainants Joint Brief at 13-14 ("[Commerce] failed to follow the essential test established in [Leather from Argentina]").

[320] All parties agree that the study by Margolick and Uhler, "The Economic Impact of Removing Log Export Restrictions In British Columbia" (April 1986) (the "Margolick-Uhler Study"), does not employ regression analysis. It is not clear exactly when all of the parties came to that realization, however. In particular, it is not clear that Commerce understood this at the time it issued the *Final Determination*. *Final Determination*, 57 Fed. Reg. 22,570 at 22,610 ("Based upon [the Margolick-Uhler] study, we determine that there is a relatively high or strong correlation between the BC log export restraints and the significant price differential between exported and domestically consumed logs."); *Ibid.* at 22,610 n.27 ("In contrast to our approach here, we did not use econometric studies in Leather.").

[321] Here, B.C.'s log export restrictions "have been in place since 1906." Canadian Complainants' Joint Brief at D-1.

been no significant change in B.C.'s log export restrictions, it will be impossible to demonstrate that changes in B.C. log prices have been correlated with changes in the restrictions.[322]

The Canadian Complainants have challenged Commerce's determination on the ground that it is "unsupported by substantial evidence."[323] They allege that "no study submitted by the Coalition and no analysis performed by the Department was designed to address" the issue of "whether British Columbia's log export regulations cause the price paid for logs by British Columbia lumber mills to be lower than otherwise would be the case."[324] The Canadian Complainants criticize the Margolick-Uhler study because, they allege, it assumes, but does not test for, a relationship between the log export restrictions and the price of logs.[325]

The Margolick-Uhler Study was also challenged on the ground that it "was based on 1983 data and modeled a log market vastly different in several respects from the current structure of the British Columbia, United States, and Pacific Rim log markets."[326] In response to this challenge, Commerce and the Coalition make two arguments. First, they argue that any analysis of the effects of the log export restrictions must predate the *Memorandum of Understanding*, in order to account for the effects of the log export restrictions in the absence of the *MOU*. Second, they argue that the analysis of the Margolick-Uhler Study was updated to reflect more recent prices by the Newport Study.[327]

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322 The impression that Commerce required proof of a "discernible effect" may have had its source in Commerce's notice of self-initiation in which it stated that it required "evidence demonstrating that the restrictions had a measurable downward effect on domestic log prices." *Self-Initiation*, 56 Fed. Reg. 56,055 at 56,057.

323 Canadian Complainants' Joint Brief at D-3.

324 *Ibid.* at D-3.

325 *Ibid.* at D-3.

326 *Ibid.* at D-15.

327 Carl Newport, "Review and Update of the Economic impact of Remaining Log Restrictions in British Columbia," (April 1992), Coalition's Pre-Hearing Brief, Pub. Doc. No. 484, Exhibit 44 (Apr. 21, 1992) ("Newport Study").

The Canadian Complainants offered evidence[328] purporting to show "that there was no connection between British Columbia's log export restrictions and domestic log prices."[329]

Although the Panel may believe that Commerce did not mean to introduce a requirement that it demonstrate "discernible effects" through regression analysis before finding a subsidy to be countervailable, the role of the Panel is not to rewrite the determination replacing "correlation analysis" and "regression analysis" with "probability based economic theory" or some such phrase. Rather, the appropriate remedy should be remand for clarification as to whether the "direct and discernible" effects test requires the performance of a regression analysis.

Should Commerce determine upon remand that regression analysis is not required, it should then clarify what it meant by "direct and discernible effects." Specifically, Commerce should clarify whether it meant to equate the phrase "proximate causal relationship or correlation (i.e., regression analysis)" with the phrase "direct and discernible effects." If it did not, if the phrases represent two different standards, Commerce should clarify which standard governs and why. Commerce should then clarify whether the applicable standard is met by substantial evidence on the record. Given the confusing exposition of the "direct and discernible effects" standard, however, it is impossible for the Panel to determine whether the Margolick-Uhler Study and the Newport Study constitute substantial evidence supporting the existence of either a "proximate causal relationship" or "direct and discernible effects."

The Canadian Complainants' objection to the filing of the Newport Study is dealt with, *supra*.

328 Kalt Study I, at 25-27; Dr. William F. Finan, "Evaluation of Relationship between Log Exports and Prices in British Columbia," Pub. Doc. No. 501, Tab 4, Attachment A (April 27, 1992), ("Finan Study").

329 Canadian Complainants' Joint Brief at D-16.

(iv) Remand

The Panel remands the *Final Determination* to Commerce for clarification of the meaning of the applicable legal standard and demonstration that the standard was met by substantial evidence on the record.

H. Calculation Issues[330]

In the previous two subsections, the Panel remanded 1) Commerce's determination that British Columbia's log export restrictions were *de jure* specific and 2) Commerce's determination that British Columbia's log export restrictions constituted a subsidy for clarification of the "direct and discernible effects standard" and whether that standard was met by substantial evidence on the record. On reconsideration, Commerce may reverse itself. But it is also possible that upon remand Commerce may find that British Columbia's log export restrictions constitute a countervailable subsidy. We consider, as a contingency, the calculation issues addressed by Commerce in its *Final Determination*.

To facilitate a clear exposition of the calculation issues, it is necessary to explain the administrative demarcation of British Columbia's forests. The Ministry of Forests ("MOF") divides British Columbia into two areas: the coast and the interior. During verification, the Canadian respondents divided the interior into three smaller areas: the tidewater interior, the border interior and the north/central interior. Thus, there are four areas: the coast, the tidewater interior, the border interior and the north/central interior.

Commerce found that the "geographic characteristics and the costs of transporting logs from [the north/central interior], both under current market conditions and under conditions that would prevail absent the restrictions" would prevent logs from the north/central interior from exhibiting "any

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[330] Panellists Weiler and Dearden take no position as to these calculation issues in light of their dissent, *infra*; see footnote 403, *infra*.

significant level of exports even without the [log export] restrictions."[331] Commerce therefore excluded north/central interior logs from its calculation of the amount of the subsidy. None of the parties challenged Commerce's exclusion of these logs.

Commerce included logs from the remaining three areas (the coast, the tidewater interior and the border interior) in its calculation of subsidy[332]. The inclusion of logs from the border interior has proved controversial.[333] The Canadian Complainants contended that Commerce erred in its conclusion that logs from this area benefit from the subsidy conferred from the log export restrictions. They argued that logs from this area do not have access to the export market. Therefore, their argument continued, the log export restrictions have no practical effect. If the restrictions were to be removed, the Canadian Complainants claimed, the quantity and price of logs on the border interior domestic market would be unchanged.

Commerce disagreed. Citing the study by Professor Kalt, Commerce adopted "an outer limit of 100 miles" for use "to conservatively define the likely area of potential exports from the interior."[334] Commerce then found that "due to the proximity to export markets in the United States" of the border interior, tenure holders in the border interior would likely export logs if there were no export restrictions."[335]

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331 Final Determination, 57 Fed. Reg. 22,570, at 22,612.

332 *Ibid.* at 22,612.

333 Respondents do not assert that the tidewater interior is affected by "geographic and economic constraints that Respondents attribute to the rest of the administrative interior." *Final Determination*, 57 Fed. Reg. 22,570, at 22,614.

334 *Ibid.* at 22,614 (internal quotations omitted).

335 *Ibid.* at 22,615.

Affidavits on the Record cited by the Coalition, the Flynn/Cox Study, the Percy Study, the volume of log exports from 1981 to 1990, and the existence of a price gap all provide substantial evidence that a demand for timber felled in the "border interior" exists in the U.S.

The Panel finds that this determination is supported by substantial evidence on the Record. Accordingly, the Panel affirms the determination of Commerce with respect to the inclusion of tenure holders in the border interior in the calculation of the subsidy conferred by British Columbia's log export restrictions. Commerce properly included the volume of logs produced in the border interior in its calculation of British Columbia's log export regulations subsidy.

The question remains, however, whether Commerce erroneously excluded areas of British Columbia from the calculation of the benefit. The Panel remands the determination to Commerce for consideration of the Coalition's claim that the areas included should be expanded.

Commerce proceeded to calculate the amount of the subsidy by examining "the difference between the current domestic log price and the price that would exist if the restrictions were not in place."[336] To determine this difference, Commerce examined the following: domestic price, species/grade adjustment, export price, economic adjustment and export costs. The Panel will now consider each of these in turn.

(i) Domestic Price

Commerce "calculated a domestic log price based on price information from the Vancouver log market for the coast, observed log prices in the tidewater interior, and 1989 Statistics Canada log valuation data, adjusted for inflation for the border interior."[337] In adjusting these prices for inflation, Commerce used the Purchase Price Index ("PPI") for all goods rather than the log PPI. The Panel

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[336] *Ibid.* at 22,615.

[337] *Ibid.* at 22,616.

remands the determination for recalculation of the domestic price of logs from the border interior using the log PPI.

Commerce weighted these prices by the percentage of the harvest from each area included in the benefit as follows: 64% for the coast, 10% for the tidewater interior, and 26% for the border interior.[338] With these data and weights, Commerce derived an average domestic price with which to calculate the benefit. Although the Canadian Complainants have challenged various aspects of this derivation, the Panel finds that the average price so derived is supported by substantial evidence on the record and that the method of derivation is both consistent with established agency practice and reasonable.

(ii) Species/Grade Adjustment

Because export logs tend to be of higher quality than domestic logs, it is necessary to adjust the differential between the domestic price and the export price by the species/grade adjustment. In calculating the species/grade adjustment for the interior, Commerce applied the same adjustment used on the coast. This procedure was objected to by both the Canadian Complainants and the Coalition.

The Panel agrees with both the Canadian Complainants and the Coalition. Having included logs from the tidewater and border interiors, Commerce proceeded to "recognize that quality differences do exist between logs from the coast and those from the interior."[339] Notwithstanding these recognized quality differences, Commerce "applied the coastal species/grade adjustment to the interior as the best information available."[340]

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338 *Ibid.* at 22,616.

339 *Ibid.* at 22,616.

340 *Ibid.* at 22,616.

Commerce itself agrees with the Canadian Complainants and the Coalition and has requested remand to determine an interior species adjustment.

The Panel remands the determination so that Commerce may ascertain a species/grade adjustment supported by substantial evidence on the record.

(iii) Export Price

Commerce based its calculation of export price on data taken from Statistics Canada. Because (1) these data were themselves "based on empirically observed prices taken from customs records,"[341](2) Commerce determined that it was not appropriate to use cross-border prices as suggested by the Coalition when intra-province data were available, and (3) Commerce found that the Statistics Canada data "originate primarily from the tidewater interior and the coast, not simply the coast" and also include a small portion of exports from the border interior,[342] the Panel finds that the derivation of export price was based on substantial evidence on the record.

(iv) Economic Adjustment

In calculating the benefit conferred by the log export restrictions, Commerce also "adjusted the export price downward by a price equilibrium factor to account for the decrease in the British Columbia export price that would result from lifting the log export restrictions."[343] In deriving this adjustment, Commerce relied on the Margolick-Uhler study and the Newport update. This resulted

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341 *Ibid.* at 22,616.

342 *Ibid.* at 22,617.

343 *Ibid.* at 22,617.

in a downward adjustment of the export price of 18% and an upward adjustment of the domestic price of 27%.[344]

The Canadian Complainants heavily criticize this derivation of the "price equilibrium factor". First, the Canadian Complainants argue that Commerce could not rely on an economic model to derive the price equilibrium factor because in Leather From Argentina they relied on regression analysis. Commerce was quite explicit, however, in stipulating that differences between British Columbia's log export restrictions and the Argentine leather restrictions preclude the use of a regression analysis. The Panel finds the use of a study such as the Margolick-Uhler study and Newport update instead of regression analysis reasonable under the circumstances described by Commerce.[345]

Second, the Canadian Complainants claim that the calculation of the subsidy is flawed because Commerce failed to account for structural changes in the market since the Margolick-Uhler study in 1983. The Canadian Complainants contend, and the Coalition concedes, that the Newport study did not revisit Margolick and Uhler's determination of elasticities of supply and demand. The Canadian Complainants maintain that, for example, changes in British Columbia's log export policies, the tightening of the U.S.'s log export policies, and changes in the structure of the former Soviet Union warrant remand for assessment of the effects of these changes on the supply and demand elasticities and the "equilibrium adjustment" for subsidy measurement. The Margolick-Uhler study used a range of assumptions about elasticities of supply and demand to predict the effect of the removal of the log export restrictions on the supply and demand of logs. The Newport update did not update these assumptions. Instead, the Newport study examined the assumptions and pronounced them "reasonable." Accordingly, the Panel remands the determination to Commerce for express consideration of which of the Margolick-Uhler elasticities assumptions for supply and demand they adopt.

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344 *Ibid.* at 22,618.

345 *Ibid.* at 22,617.

In addition, the Panel grants Commerce's request for remand of the determination to Commerce for reconsideration of the economic adjustment made to export price.

(v) Export Costs

Commerce adjusted the average log export price for dry land sorting and lost volume, and for export transportation costs. The Panel finds that each of these adjustments was supported by substantial evidence on the record.

In its *Final Determination*, Commerce declined to adjust for falldown sort costs, the "costs" associated with the reduced value of the logs left in a boom after the top quality logs have been removed for export. The Canadian Complainants contend that the diminished value of the falldown sort is an export cost and should be included in the adjustment of the average log export price. Alternatively, the Canadian Complainants contend that the diminished value of the falldown sort results from variations within grade.

Commerce concedes that "a falldown sort may result when an export sort is removed from a camp-run sort."[346] Commerce, however, declined to adopt a "within grade adjustment." In so doing, Commerce cited the absence of evidence "of a within-grade average difference between exported and domestic logs" and the fact that Commerce had "no reason to believe that the species/grade adjustment we made does not account for within-grade differences."[347]

The Panel finds that neither Commerce's decision to include the diminished value of the falldown sort as an export cost nor its decision not to adjust for within-grade differences is supported by substantial evidence on the record. The determination is therefore remanded to Commerce for

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346 *Ibid.* at 22,620.

347 *Ibid.* at 22,620.

either recalculation of the export cost adjustment to include the diminished value of the falldown sort or adoption of a within-grade adjustment.

Finally, the Panel finds that Commerce's decision to calculate the subsidy based on the value, rather than the volume, is supported by substantial evidence on the record. Given the wide variance in the density of different lumber products, and the general inverse correlation between density and value, Commerce's decision to calculate the subsidy on a value basis seems reasonable and should not be remanded.

(vi) Remands

To summarize this subsection on calculation issues, the Panel remands:

1) the determination to Commerce for express consideration of the Coalitions's claim that Commerce erred in limiting its calculation of the benefit to certain areas of British Columbia;

2) the determination to Commerce for recalculation of the domestic price of logs from the border interior using the log PPI;

3) the determination so that Commerce may ascertain a species/grade adjustment supported by substantial evidence on the record for logs from the interior;

4) the determination to Commerce for express consideration of which of the Margolick-Uhler elasticities assumptions for supply and demand they adopted in calculating the equilibrium price factor;

5) the determination to Commerce for reconsideration of the economic adjustment made to export price; and

6) the determination to Commerce for either recalculation of the export cost adjustment to include the diminished value of the falldown sort or adoption of a within-grade adjustment.

VII. OTHER ISSUES

A. Introduction

Although the Panel does not need to specifically render reasons for every issue raised by the Parties in light of the above mentioned findings, the Panel believes it important nevertheless to briefly address certain issues that warrant comment:

1. company exclusion requests;
2. provincial exclusion requests; and
3. Dr. Lange's participation on the Commerce verification team.

B. Company Exclusion Requests

Commerce received 334 company-specific requests for exclusion. Commerce determined it impracticable to investigate all 334 requests from its investigation. Instead, Commerce limited its investigation to those companies that produced softwood lumber solely or primarily from U.S. origin logs. Three issues arise in the regard.

First, the Canadian Complainants allege that Commerce's decision not to investigate the vast majority of requests on the ground that it was impracticable was not in accordance with law. Secondly, an individual company MacMillan Bloedel, claimed that Commerce's decision not to investigate its exclusion request constituted an abuse of its discretion to limit its investigation on grounds of practicability, contrary to law. Thirdly, the Canadian and Québec governments and the QLMA argue that Commerce's refusal to investigate two Québec companies which fulfil Commerce's exclusion criteria constituted an error for which remand was justified.

(i) Commerce's Investigation

Contrary to the assertions of the Canadian Complainants, 19 § C.F.R. 355.14 of the Department's *Regulations* accords Commerce a discretion with regard to company-specific requests for exclusion from a cvd investigation. While producers or exporters are entitled by the *Regulations* to submit a written application for exclusion, section 355.14(c) states that the "Secretary will investigate requests for exclusion to the extent practicable in each investigation"; it neither requires exclusion nor does it even specify any procedure or criteria applicable to requests for exclusion.

Similarly, no provision in the GATT *Subsidies Code* requires a Signatory to grant company-specific exclusions from countervailing duty orders. When read in context, it is reasonable for Commerce to interpret Article 4.2 of the *Subsidies Code* as requiring only that a Signatory's exporters be assessed a duty no greater than the subsidy found for the class or kind of merchandise found to be subsidized. The investigating authority is not obliged to ensure that it does not levy a duty beyond the subsidy actually received by each company which may be affected by a cvd order.

Commerce's discretion is illustrated by its past investigatory practice when faced with numerous producers and/or exporters. Commerce either aggregates data from the government or it investigates specific companies that represent at least 60% of the exports of the subject merchandise. Thereafter, the cvd statute requires that Commerce determine whether a country provides an injurious subsidy with respect to a class or kind of merchandise imported into the U.S., and if it does, a countervailing duty is imposed on the merchandise equal to the amount of the country's net subsidy, not the amount of the subsidy in fact received by the company (see, for example, Commerce's investigations in Live Swine from Canada).[348] The net subsidy is applied to the merchandise unless Commerce investigates and, in fact, finds that there is a significant differential between the benefit received by certain companies from the countervailable program.[349] Commerce

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[348] 56 Fed. Reg. 28, 561 (1991).

[349] 19 U.S.C. § 1671e(a).

is not, however, directed to make this determination and thus the application of a differential rate is mandated only if such determination is in fact made.

The Panel notes that in Ceramic Tile from Mexico,[350] the Court of International Trade upheld Commerce's country-wide rate. In Certain Fresh-Cut Flowers from Canada,[351] Commerce investigated only two enterprises which accounted for more than 60% of the exports of the subject merchandise, and applied the rate received by these two companies to all exports of the subject merchandise from Canada. By definition, an average subsidy rate subjects some producers and exporters to duties in excess of the subsidies they in fact receive.

In its Brief,[352] Commerce stated: "[w]hile Commerce conducts company-specific countervailing duty investigations where practicable, investigations of 334 companies is beyond any conceivable realm of possibility and is not even close to the average number of companies (5) or the most companies (57) Commerce or Treasury has ever investigated or reviewed." Ample foundation for Commerce's decision that it was impracticable to investigate the bulk of the company exclusion requests is found in a memorandum to A.M. Dunn, then Assistant Secretary for Import Administration, from J.S. Spetrini, Deputy Assistant Secretary for Compliance.[353]

This Panel is precluded from remanding Commerce's decision regarding exclusions unless the Canadian Complainants establish that Commerce has interpreted its discretion unreasonably, in effect in a manner that no reasonable agency could in the circumstances. On the evidence before it, the Panel finds that Commerce's exercise of discretion not to investigate all company-specific exclusion requests in the circumstances of this case did not go beyond the bounds of "reasonableness".

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350 49 Fed. Reg. 9,919 (1984).

351 52 Fed. Reg. 2,134 (1987)

352 at I-7.

353 Pub. Doc. No. 162 (January 17, 1992).

(ii) MacMillan Bloedel

Commerce justified its decision to limit the investigation of company exclusion requests to companies producing softwood lumber solely from (later revised to "primarily from") U.S. origin logs, as follows:

> "One category of companies seeking exclusion would not pose an extraordinary administrative burden. Companies that produce lumber entirely from U.S. origin logs cannot benefit from any federal or provincial stumpage programs. We recommend accepting the exclusion requests from these companies as long as they have submitted proper certifications. We have identified only 11 companies that have properly certified that they produce lumber entirely from U.S. origin logs.
>
> Drafting and sending questionnaires to these 11 companies will not create an administrative burden because there is only one fact that need be established: the source of the timber used by the companies to produce lumber. In addition, verification will be relatively straightforward matter, and there will be no need to calculate benefits."[354]

While Commerce chose a criterion to limit its investigation - a "bright" line - which was clearly not the only criterion available, the Panel may not substitute its own "bright line" for that chosen by the investigating authority so long as the line chosen is reasonable. In the Panel's view, the submissions of MacMillan Bloedel did not establish that Commerce acted unreasonably in making that choice.

MacMillan Bloedel's claim assumes Commerce's discretion but argues that having decided to investigate those companies that produce lumber primarily from U.S. origin logs on the basis that investigation of this sub-group was "practicable" within the meaning of its *Regulations*, Commerce had a duty to consider the exclusion requests of all other identifiable sub-categories of companies

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[354] Pub. Doc. No. 162, at 2.

which could "practicably" be investigated. MacMillan Bloedel claims that it, alone, forms such a sub-category.

MacMillan Bloedel argues that this Panel may remand Commerce's decision if it determines that Commerce "abused" its discretion not to investigate; abuse is said to amount to a finding that Commerce's decision in this regard was "unsupported by substantial evidence on the record"[355] or that Commerce did not otherwise act "in accordance with law".[356]

MacMillan Bloedel's argument is simple and at first glance has some `common sense' merit. MacMillan Bloedel argues that if Commerce found it practicable to investigate 24 exclusion requests, there is no reason why it could not practicably investigate the request of one more company in a readily-identifiable and discrete category. The discrete category is defined on the basis of three characteristics:

1. MacMillan Bloedel harvested more private timber than any other softwood lumber company in B.C.;

2. MacMillan Bloedel had a higher proportion of private timber in its harvest than any other major softwood lumber company in B.C. holding Crown timber; and,

3. MacMillan Bloedel had a higher proportion of the total harvest of private timber than any other softwood lumber company in B.C.

In the end, however, MacMillan Bloedel's argument does not meet the standard required to overturn the exercise of Commerce's discretion as to whether to investigate company exclusion requests on the grounds of practicability. Commerce exercised its discretion by drawing a "bright line" that allowed it to investigate companies producing softwood lumber solely or primarily from

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[355] citing in support China National Arts and Crafts Import and Export Corporation v. U.S., 771 F. Supp. 407, 413 (CIT, 1991.

[356] citing in support Tai Yang Metal Industrial Co. Ltd. v. U.S., 712 F. Supp. 973, 974 and 978 (CIT, 1989).

U.S. origin logs. MacMillan Bloedel simply argues that Commerce should have exercised its discretion to draw another arbitrary line which included it, as a company that produces a significant proportion of lumber from unsubsidized private timber.[357]

The Panel is left with the practical problem as to how, if it is to accede to MacMillan Bloedel's reasoning, a reviewing panel should direct Commerce to draw a new line? For example, is Commerce bound, if it investigates MacMillan Bloedel's exclusion request, to consider excluding Canadian Pacific Forest Products because, like MacMillan Bloedel, over 40% of that company's total harvest came from private timber? Or, would Commerce be required to exclude Fletcher Challenge and Doman Forest Products of B.C. because those companies represent companies having over 20% of their total harvest from private timber?

While, in fact, only six companies that originally requested exclusion obtained over 10% of their total harvest from private timber, the question before us is whether it is the Panel's role to make such a decision for Commerce? The Panel rules that it cannot play such a role. Commerce's decision does not amount to an "abuse of discretion", within the meaning accorded that phrase in the authorities referred to the Panel by MacMillan Bloedel, nor can it be said to be a decision no reasonable agency could have made in the circumstances.

(iii) Commerce's Refusal to Exclude Two Québec Companies That Met The Exclusion Criteria

Commerce refused to consider the applications of two of the QMLA companies for exclusion from the investigation: Les Industries Maibec and Matériaux Blanchet. These companies produced lumber almost exclusively from U.S. origin logs during the period of investigation and received only

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[357] Commerce wisely stressed during oral argument that MacMillan Bloedel was not before the Panel claiming that a *de minimis* amount of the logs it used to produce softwood lumber came from Crown land. In fact, over 50% of MacMillan Bloedel's harvest came from lands found by Commerce to be subsidized.

de minimis benefits. It is not disputed that these two companies fulfilled Commerce's exclusion criteria.

Commerce refused to exclude these two companies because they filed their responses to Commerce's first questionnaire after the deadline of January 31, 1992. These two companies did not learn about the existence of the first questionnaire until the deadline of January 31, 1992 had expired and promptly responded to that questionnaire once they learned of its existence (*i.e.* on February 21, 1992).

On February 24, 1992, Commerce distributed its second questionnaire to companies that produced lumber from U.S. origin logs. Les Industries Maibec and Matériaux Blanchet responded to the second questionnaire in a timely fashion. The Administrative Record does not reveal whether these responses were solicited by the Department of Commerce. The Panel assumes that Commerce did not solicit these responses. Neither of the responses by these two companies to the two questionnaires were rejected by Commerce or returned to the two companies. Commerce did not, as its *Regulations* require, return to the submitter (with written notice stating the reasons for return of the document) any untimely or unsolicited questionnaire response rejected by the Department, nor did Commerce inform the two companies that it considered the deadline for the first questionnaire critical. Indeed, at no point did Commerce provide any written and reasoned explanation as to why it rejected the applications. The two companies did not learn of the rejection until the *Final Determination*, which provided no explanation as to the critical nature of the first questionnaire deadline to Commerce's methodology.

(iv) Remand

The Panel finds that having fulfilled all of the criteria required for exclusion, Commerce should have excluded these companies. As a result, the Panel remands this matter to Commerce for consideration and pronouncement upon the exclusion requests of Les Industries Maibec and Matériaux Blanchet.

C. Provincial Exclusion Requests

The Canadian Complainants assert that Commerce erred in failing to exempt (or exclude) certain provinces from the investigation, or alternatively from the imposition of cvd duties.

First, Québec argues that it should have been exempt from Commerce's investigation at the initiation stage, or alternatively at the conclusion of the investigation, because its provincial stumpage system is "market-based" and thus analogous to the systems in the Maritime provinces exempt from the investigation. Second, British Columbia asserts that because it, like the Maritime provinces, was exempt from application of the export charges set out in the *MOU*, Commerce did not have the "special circumstances" upon which to self-initiate an investigation involving British Columbia. Québec effectively adopts this assertion. Finally, Québec argues that Commerce erred in applying a country-wide (average) subsidy rate to Québec's exports, *i.e.* Québec should be exempt because Commerce's investigation of Québec found a 0.01% (*de minimis*) subsidy. Alberta effectively adopts this position, alleging that absent calculation errors it too would have a *de minimis* subsidy rate mandating exemption.

(i) "Market-Based" Stumpage Systems

Québec asserts that Commerce, apprised of the `market--oriented' nature of its stumpage system, was bound to exempt Québec from its self-initiated investigation. Stated simply, Québec argues that because the Maritimes were exempt from the *MOU* on the basis of their market-oriented stumpage systems and hence from Commerce's investigation because of an absence of `special circumstances', Québec merits the same treatment.

Québec adds *inter alia* that Commerce relied upon inaccurate and outdated data in self-initiating an investigation of Québec, and further that none of the three bases upon which Commerce

self-initiated its investigation of Québec survived the *Preliminary Determination*.[358] Québec also argues that in the only previous self-initiated investigation, Commerce relied on a more stringent standard, and substantially greater evidence.[359]

Even if the similarity between Québec's stumpage system and the exempt Maritime Provinces is an insufficient basis for exemption, Québec argues alternatively that on investigation and confirmation that Québec's stumpage rates are based on private market survey data similar to the Maritimes, Commerce was obliged to exempt Québec from any cvd order. Exclusion in these circumstances is said to be mandated by basic principles of administrative law which require that agencies act consistently, applying the same basic standards to all parties before them, *e.g.* disparate treatment of similarly situate parties is at law "inherently unreasonable". Commerce's own *Regulations* which "[e]xcludes from the application of [a cvd] order any producer or exporter that the secretary finds did not receive directly or indirectly...any net subsidy..." is said to mandate the exemption of a province found not to receive a subsidy. In effect, Québec argues, if all the producers or exporters in the province should be excluded, so must the province.

Commerce's response to these arguments is simple, and in the end, persuasive. Commerce states that its acknowledgement of the "dominance of market determined stumpage rates" as the basis for the *MOU*'s exemption of the Maritime provinces does not require that it delve into this rationale at the stage of self-initiation. Commerce correctly notes that its *Final Determination* does not rely

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[358] Québec argued that:

(a) Commerce reversed its own determination in Lumber I that cross-border comparison was too arbitrary;
(b) Commerce recycled outdated data gathered during Lumber II, which did not reflect Québec's amendments to its stumpage system; and
(c) Commerce selected and relied upon isolated current information.

[359] Commerce's previous self-initiation came in response to the steel Trigger Price Mechanism ("TPM") in effect from 1978 to 1983. The TPM established, by regulation, certain presumptions regarding the existence of countervailable subsidies and material injury when import prices for specified steel products dropped below a certain level. In such circumstances, Commerce was required to self-initiate a countervailing duty investigation. Québec argues that the TPM embodied a clear and discernible standard upon which to self-initiate in sharp contrast to that at instance.

on this factor but only on the simple fact that the Maritime provinces were expressly exempt from the application of the export charges under the *MOU* and the other provinces were not.

Commerce further argues that Québec cannot stand in the guise of a "producer" or an "exporter" (a company) in claiming an exemption, because its statute clearly provides for exemptions of grantees of subsidies, not grantors. As Commerce was unable to investigate all companies in Québec, it could only find an average (*de minimis*) margin. Some companies may have received higher subsidies while others received no subsidy at all. In such a situation, Commerce states that it cannot exclude the exporters of an entire province.

A reading of Commerce's Reasons on Self-Initiation, its *Preliminary Determination* and its *Final Determination*, indicates that Commerce's exemption of the Maritime provinces was based on the express exemption of these provinces in the *Amendment to the MOU*, and its belief that such exemption removed its jurisdiction over these provinces.

Québec was not expressly exempt from the *MOU* and in fact, was subject to export charges at the time of self-initiation. Thus, at the self-initiation stage, it was reasonable for Commerce to refrain from inquiring into the similarity between the stumpage systems in the provinces expressly exempt by the *MOU* and the systems in the other (non-exempt) provinces. The `special circumstances' threshold for self-initiation in the GATT *Subsidies Code* is broad. Indeed, Congress appears to have generally favoured the initiation of investigations so long as the bases are not frivolous - the more stringent standard is reserved for the stages of preliminary and final determination.

In the absence of explicit guidance as to the appropriate standard of self-initiation, Commerce is only required to consider reasonably how Congress intended the standard apply had it expressly spoken on the subject. Commerce's decision at the stage of self-initiation cannot therefore be said to be unreasonable, and neither can Commerce's decision not to exempt Québec upon investigating its stumpage system. Commerce was not required, in the Panel's view, to exempt any province on

the basis of the similarity of their stumpage system to the system in a Maritime province. Commerce did not exempt the Maritime provinces under the *MOU* nor did it undertake an assessment of the market-orientation of those systems.

(ii) Exemption from the *MOU*'s Export Charge

British Columbia and Québec claim that Commerce's failure to exempt it from the self-initiated investigation was inconsistent with Commerce's exemption of the Maritime provinces and therefore not in accordance with law. Commerce addressed B.C.'s repeated requests for exemption only in the *Final Determination*, stating simply at p. 22,622:

> Although the export tax for B.C. under the *MOU* was reduced to zero, B.C. was not exempt from the *MOU*. Despite the zero rate, B.C.'s operation of replacement measures was still subject to consultations with the United States and monitoring by both governments. Although B.C.'s export tax rate was zero, a decrease in its replacement measures would have resulted in the reimposition of some or all of the 15% export tax. This was not the case for the Maritime Provinces. The Maritime Provinces were exempt from the export charge; no reimposition of the export charge was possible during the lifetime of the *MOU*.

B.C.'s argument may be summarized as follows. In its Reasons for Self-Initiation, Commerce stated that "Canada's unilateral termination of the *MOU*" constituted "special circumstances" within the meaning of Article 2 of the GATT *Subsidies Code* and therefore justified self-initiation. Commerce expressly recognized that the Maritime provinces were "exempted from payment of the export charge under the *MOU*, and therefore excluded these provinces from the self-initiated investigation". Because of its replacement measures (measures which continue in existence to date), B.C. was also exempt from payment of the export charge under the *MOU*.[360] As both B.C. and the Maritimes are exempt, Commerce must apply its own logic and exclude B.C. from the self-initiated investigation as they did the Maritimes.

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[360] B.C. also relies on the practical argument that with its replacement measures, B.C. timber can no longer be said to be subsidized, thus countervail is unwarranted. Similarly situate parties are required, it is said, to be treated equally under U.S. law.

B.C. adds that the Maritimes have never been exempt from the operation of the *MOU*. The Maritimes were subject to an export charge during the first year of the *MOU*. Although the Maritimes were exempt from the export charge by the *Amendment to the MOU* (1987), Commerce is said to have continued to monitor the Maritimes, which remain subjected to export procedures, to filing return requirements, as well as to the consultation requirement in para. 8(e) of *Amendment to the MOU* so long as the *MOU* was in force.

While Québec relies on basically the same arguments, it is noteworthy that at the time of the self-initiation of investigation, Québec was still subject to a 3.6% export charge.

Commerce's response to these claims is primarily based on three observations. First, the Maritime Provinces, unlike the other provinces, were expressly exempt by paragraph 3 of the *Amendment to the MOU* from the *MOU*'s export charges. Commerce goes so far as to claim that the Maritimes were freed in perpetuity from the collection of export charges short of a new amendment. Second, neither B.C. nor Québec was "exempt" from the export charges; they were only allowed to replace these charges. Finally, the Government of Canada was required to reimpose export charges unilaterally upon B.C. or Québec if either failed to administer the replacement measures; the Maritimes were not subject to the unilateral implementation of export charges.

As regards the Maritimes' consultation obligations, Commerce noted that the *MOU* simply required that on a rapid and substantial increase in exports from the Maritimes the Parties were to consult, a mechanism Commerce asserts was imposed to protect against the circumvention of the *MOU* by transhipment of logs from a non-exempt province through one of the Maritime provinces.

In the Panel's view, the exemption claims of B.C. and Québec face a number of hurdles, the greatest of which is the inescapable fact that B.C. and Québec's status under the *MOU* and its *Amendment* are manifestly distinguishable from that of the Maritimes. B.C. and Québec were required to enact replacement measures to represent the value of the export charge, while the Maritimes were expressly exempt from having to enact any replacement measures. B.C. and Québec

could be subject to the unilateral imposition of an export charge by the Canadian Government; the Maritimes could not.

While the Panel recognizes what might be termed the `practical injustice' of the imposition of cvd duties in conjunction with the continuing application of replacement measures, it is important to remember that with the termination of the *MOU*, B.C. and Québec were entitled to withdraw the replacement measures. Additionally, Commerce is correct in its claim that, at the time of self-initiation, it was not Commerce's function (nor were they able) to determine whether the replacement measures completely offset any subsidy, a determination implicitly required by the Canadian parties' submissions on this issue.

Fundamentally, Commerce's decision to exempt the Maritimes from this investigation was based on its belief that due to the *MOU*'s express terms, it lacked the requisite jurisdiction to initiate against the Maritimes. In its oral submissions, Commerce stated that absent such express terms, it would have initiated the investigation against the entire country. In the end, the Panel is not prepared, on the applicable standard of review, to find that Commerce's interpretation of its obligations on self-initiation constituted an unreasonable construction of the law, the express terms of the *MOU* and the *Amendment to the MOU*, and the requirements of the GATT *Subsidies Code*. Absent such a finding, the Panel must defer to the investigating authority's interpretation of its function in these circumstances.

(iii) Commerce's Refusal to Apply a Province-Specific Rate

One of the most interesting questions before the Panel arises from Québec's claim (adopted by Alberta) that Commerce erred in applying a country-wide (average) subsidy rate. Québec argues that, in the particular circumstances of this investigation, Commerce is required to assess and apply a province-specific countervail duty. Because of the unique nature of this argument, it is necessary to outline the Parties' submissions on this issue in some detail.

Québec makes the following points of import. In recent matters involving imports of softwood lumber from Canada, the U.S. has consistently calculated province-specific rates -notably under the *MOU* and under its section 301 investigation of softwood lumber. In other areas such as beer, the U.S.T.R. has focused on the practices of specific provinces and fashioned retaliation against such provinces. Such a focus is, according to Québec, consistent with the GATT *Subsidies Code,* and thus U.S. law, being to curb and adjust unfair trade policies and practices of a government or governments. Given such purpose, Québec argues that the application of a country-wide rate in this instance is inappropriate because only the provincial government may "curb or adjust the stumpage practices considered to be countervailable". Commerce is said to have recognized this reality by investigating provincial stumpage systems, by relying on provincial data in the verification of responses, and by finding a subsidy margin for each province and for each programme under review (stumpage and log export restrictions).

The focus of Québec's legal argument is 19 U.S.C. § 1677(3) which defines "country" to include "... a political sub-division, dependant territory....". This definition, Québec argues, was adopted in 1979 to subsume then-existing 19 U.S.C. § 1303 which made cvd orders applicable to "any country, dependency, colony, province or other political subdivision...". Commerce's codified practice in 19 U.S.C. § 1677(3) is said to reflect Article 4 of the GATT *Subsidies Code* which states that "no countervailing duty shall be levied on any imported product in excess of the amount of the subsidy found to exist, calculated in terms of subsidization per unit of the subsidized and exported product". Québec notes, as well, 19 C.F.R. § 355.20(d)(3)(i) and (ii) of Commerce's *Regulations* which require that Commerce publish and apply individual net subsidy rates when a "significant differential" is identified between a country-wide rate and an individual company rate. Québec argues that this too is indicative of a legislative intent not to impose countervail duties in excess of the benefit actually received. In effect, Québec argues that the provinces in this instance stand in the stead of individual companies. Québec submits that Commerce's decision to investigate on a provincial, rather than a company-specific basis, should not be allowed to defeat the policy underlying its codified practice of applying specific rates where significant differentials exist.

As a practical consideration, Québec's position is persuasive. Québec was found to have a 0.01% (*de minimis*) subsidy margin. As a result of Commerce's application of a country-wide subsidy rate however, Québec exporters face a 6.1% cvd duty, roughly half of which results from Commerce's finding that B.C.'s log export restrictions are countervailable while most of the remainder results from the finding that stumpage systems in other provinces confer a countervailable subsidy.

Alberta's claim for exemption is somewhat more complicated than Québec's, relying on two basic premises: first, that the Alberta tenure systems are competitive and non-distortive; and second, that on correction of certain errors in establishing the benchmark for Alberta's Quota Tenure System and for its CTP Tenure System, as well as a number of calculation errors, Commerce would have found a maximum subsidy of 0.48% *(de minimis).* In such an event, Alberta would be excluded from any cvd order like the Maritimes (*supra*), or alternatively, as a "political subdivision", it may be subject only to province-specific duties.

For its part, Commerce characterizes its procedure in Lumber III as exemplary of an ordinary aggregate case. Commerce states that, pursuant to 19 U.S.C. § 1677, a cvd investigation may proceed in one of two ways:

(1) where there are only a few foreign producers or exporters, Commerce first calculates company-specific rates, then averages all subsidies received by the companies to create an average net subsidy rate which will apply to all exports of the subject merchandise unless it has evidence before it that there is a significant differential in the subsidy received by one or more of the companies, as defined in 19 C.F.R. § 355.20(d)(3)(i) and (ii); or

(2) where the number of individual producers or exporters is too large to calculate the subsidy received by each, Commerce relies on data from government records to determine the aggregate amount of subsidy provided by the government for each countervailable program, then it averages the subsidies provided under all the programs to all exports of each class or kind of the subject merchandise from the country. Thereafter, Commerce derives a net benefit for that subsidy.

As a result of the number of producers involved, Commerce applied the latter aggregate methodology here, as it purportedly did in Lumber I,[361] Live Swine from Canada,[362] Fresh Chilled and Frozen Pork Products from Canada,[363] and Lamb Meat from New Zealand.[364]

As to Québec's claim that 19 U.S.C. § 1677(3) requires that a political subdivision such as Québec be considered a "country" for purposes of the applying a cvd duty, Commerce asserts that its enabling legislation mandates a bi-partite process for arriving at a cvd order which process involves different definitions at different stages. In establishing whether a subsidy exists, Commerce states that a "country" for purposes of 19 U.S.C. § 1671(A) routinely mandates the investigation of a state, provincial, or local program, and the necessary calculation of the subsidy conferred by that program. However, the assessment (or calculation) of the subsidy rate, mandated by § 1671e(a)(2), demands that all subsidies be averaged into a net benefit and be applied to a class or kind of merchandise in the country investigated. In this latter stage of the analysis, "country" is limited to the ordinary meaning attributed that word. In essence, Commerce claims that the statute requires that it fashion its investigation into the existence of a countervailable program in accordance with the particular federal, provincial or local program(s) at issue in order to avoid being precluded from countervailing non-federal programs, but that the remedy is to be applied to the entire "geo-political boundary" that Commerce investigates and not to geo-political subdivisions.

To carry Québec's argument to its logical conclusion Commerce submits, would require, for example, that Commerce exempt municipalities able to prove that producers within their boundaries receive *de minimis* subsidies. Such an interpretation would be unadministerable in Commerce's view.

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361 48 Fed. Reg. 24,159 (1983).

362 *e.g.* 56 Fed. Reg. 28,531 (1991).

363 *e.g.* 54 Fed. Reg. 30,774 (1989).

364 *e.g.* 54 Fed. Reg. 1,402 (1989).

As outlined above, it is Commerce's position that the provinces cannot stand in the stead of individual companies. The express language of Commerce's *Regulations* refers to a significant differential in the subsidy received by "producers" or "exporters", and thus Québec's claim that provinces must receive the benefit of 19 C.F.R. § 355.20(d)(3)(i) and (ii) runs contrary to the express text of the *Regulation*. Commerce is bound to apply Congress's express intent.

For Québec and Alberta to succeed on this argument, they must establish that Commerce's interpretation of its statute and regulations, including its understanding of its mandate to investigate countervailable programs and to assess aggregate duties on a country-wide basis, is an interpretation that no reasonable agency could have made. Commerce's interpretation need not be the only interpretation nor need it be the most consistent or the fairest interpretation. Where Congress has not expressly pronounced on the issue, leeway is given to the authority's interpretation of its enabling legislation within certain boundaries. It is sufficient therefore if Commerce's interpretation of 19 U.S.C. § 1671(A) and 1671e is within the bounds of reason.

Commerce is clearly able to investigate provincial programs and apply a province-specific subsidy rate if desired. The Panel agrees that it is arguable that the application of a Canada-wide rate to vastly different programs administered by distinct political sub-divisions in Canada may not accord with a "purposive" interpretation of the U.S. cvd law and the GATT *Subsidies Code*. Nonetheless, the Panel must also recognize the burden facing Québec and Alberta. These provinces must establish that no reasonable agency could have interpreted its enabling legislation and its regulations as written to arrive at the result here. While there may be better interpretations, or fairer interpretations, the Panel cannot find that Commerce has interpreted these provisions as no reasonable agency could.

D. Participation of Former Coalition Employee on Verification Team

The Panel invited counsel for all Parties to address in oral argument the propriety of the placement of Dr. William Lange, a former employee of the Coalition for Fair Lumber Imports, on Commerce's verification team. During oral argument, the Panel also invited counsel to file written

submissions regarding this matter which were subsequently filed by the Canadian Complainants, the Department of Commerce and the Coalition.

In 1986, Dr. Lange was employed by the Coalition in Lumber II which involved many of the same issues raised in this proceeding. Since 1987, Dr. Lange has been employed by the U.S. Forest Service and was selected by Commerce from approximately 140 U.S. Forest Service economists in order to provide technical assistance to Commerce in Lumber III.

Three documents in the Administrative Record address the issue of bias as a result of Dr. Lange's prior employment with the Coalition and his involvement in Lumber III:

1. letter from Robert C. Cassidy, Jr. to the Honourable Alan M. Dunn (March 3, 1992) - Pub. Doc. No. 332;

2. letter from Leonard M. Shambon to the Honourable Alan M. Dunn (March 12, 1992) - Pub. Doc. No. 382; and

3. letter from Barbara Fredericks, Assistant General Counsel for Administration, Department of Commerce, to Robert C. Cassidy, Jr. (March 19, 1992) - Pub. Doc. No. 549.

(i) Public Statements By Dr. Lange On Behalf of The Coalition

The public documents in the Administrative Record disclose that Dr. Lange made numerous public statements on behalf of the Coalition regarding the softwood lumber trade dispute with Canada. These public statements were made in the following fora or documents:

1. Dr. Lange assisted in gathering evidence to support the Coalition's petition;

2. Dr. Lange appeared as a witness for the Coalition during the International Trade Commission's Public Conference held on June 10, 1986 regarding Softwood Lumber from Canada;

3. Dr. Lange made statements to the media in support of the Coalition's countervail petition in Lumber II;

4. Dr. Lange issued Press Releases on behalf of the Coalition;

5. Dr. Lange represented the Coalition at a conference at Lakehead University in Thunder Bay; and

6. Dr. Lange worked with the Administration to better understand the applicability of U.S. trade laws and to understand how and when to use U.S. trade laws.

The above documents reveal that Dr. Lange made statements such as:

1. Lange said the subsidy comes in the form of cheaper stumpage fees.
(Pub. Doc. No. 332 - October 22, 1985);

2. Lange called the 1983 Commerce Department ruling that the Canadian practice did not amount to a subsidy a "legalistic interpretation" that he said the industry hopes could be overturned under legislation now in Congress.
(Pub. Doc. No. 332 - October 22, 1985)

3. "The more you look at the Canadian system the more subsidies you find" he said. "We feel confident that the verification process will move the duty number closer and closer to what we allege".
(Pub. Doc. No. 332 - *Vancouver Sun,* October 17, 1986)

4. According to Lange, the information he and his colleagues are after will add to what is collected from Canada through the questionnaire.
(Pub. Doc. No. 332 - *Vancouver Sun,* July 15, 1986)

5. Imports will "wipe out the whole industry", he said.
(Pub. Doc. No. 332 - *Forest Industry* - July, 1986)

Remarks made by Dr. Lange as a representative of the Coalition at a 1986 Conference at Lakehead University in Thunder Bay dealing with "Tariffs and the Canadian Forest Industry" include:

1. "the provinces achieve [maximum timber industry employment] by virtually giving away their timber at prices totally unrelated to market values" (p.47);

2. "Canadian lumber producers pay little or nothing for their timber raw material" (p.53);

3. "...the basic issue boils down to the raw materials value. Canadian lumber producers enjoy a heavily subsidized price, and U.S. producers pay a fair market price for timber, a disadvantage they cannot make up in the marketplace" (p.58);

4. Paul Tufford to Dr. Lange: "Dr. Lange, first of all I'd like just a yes or no answer to this: a countervailing duty - the idea of that is to bring the price of Canadian lumber up to what you term fair market price in the U.S."
Lange: "Yes" (p.76).

5. Addressing the point of assisting U.S. exporters to reach new markets: "Unfortunately, every time we open up a new market to our exporters, you Canadians come in and take it from us. (If you can steal markets from us in our own back yard, certainly you will be able to steal them anywhere else)" (p.78).

6. "In terms of log exports from Canada to the U.S., the U.S. can't get at your stumpage until first having those logs declared surplus, which sometimes occurs with insect damage....The problem is log export restrictions....The point is we don't have the level of those types of subsidies that are available across the board to you" (p.79-80).[365]

(ii) Rule 7

The Department of Commerce argues that because the Canadian Complainants did not cite in their complaints Dr. Lange's involvement as an error of fact or law, the Panel lacks authority to reverse the *Final Determination* on this basis, even if it found that the evidence warranted it. Rule 7 of the *Rules of Procedure for Article 1904 Binational Panel Reviews* states:

Panel reviews shall be limited to

(a) the allegations of error of fact or law, including the jurisdiction of the investigating authority, that are set out in the complaints filed in the Panel Review; and

(b) procedural and substantive defences raised in the panel review.

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[365] Pub. Doc. No. 332.

The Canadian Complainants did not specifically raise the issue of Dr. Lange's bias in their complaints. The matter however was raised in Part II (Statement of the Case) of the Canadian Complainants' Joint Brief filed pursuant to Rule 60(1). The Complaint submitted on behalf of the Government of Canada claims *inter alia* that:

> ... in its investigations into Canadian timber programs, the ITA has applied numerous, mutually inconsistent standards and methodologies that demonstrate an absence of both controlling legal principles and any coherent methodology for evaluating factual data, and frustrate any efforts by Canada to avoid or eliminate known risks of countervailing duty actions (para. 32) (emphasis added)

The Complaint also states:

> The ITA's arbitrary refusal to apply clear and consistent rules and methodologies in its investigation of Canadian timber programs is unsupported by substantial evidence, and otherwise not in accordance with law (para. 33) (emphasis added)

Commerce argues that the Canadian Complainants never raised Dr. Lange's involvement in this case to the level of an "error of fact or law" within the meaning of Rule 7(a). The Department therefore argues that under Rule 7(a) the Panel lacks authority to reverse the *Final Determination* due to Dr. Lange's involvement.

The Panel has taken a purposive approach to interpreting Rule 7(a) as was done by the Panel in New Steel Rail, except Light Rail, from Canada which held that Rule 7(a) was:

> ... designed to assure that when a major procedural or substantive issue was brought before the Panel, the other parties will have a timely opportunity to respond in such a manner as to assure that the Panel has before it all necessary information to make an informed decision.[366]

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[366] U.S.A. 89-1904-07 at 21.

In Certain Dumped Integral Horsepower Induction Motors,[367] the Panel, although mindful of the strict wording of Rule 7, dismissed a motion to prevent a complainant from raising an issue before the Panel that was not expressly set out in its complaint. The Panel held that the complaint, viewed broadly, adequately anticipated the issue raised. The Panel found no prejudice to the Respondent resulting from any deficiency in the wording of the complaint.

In Replacement Parts for Self Propelled Bituminous Paving Equipment from Canada,[368] the Panel noted that Rule 7 limits the Panel's scope of review and stated that objections to ITA's determination that the parties failed to articulate in their complaints are beyond the Panel's authority to adjudicate.

While this Panel is not bound by previous binational panel decisions, it may be guided by such decisions. In the case at bar, the purpose of Rule 7(a) has been fulfilled - all parties have had a timely opportunity to respond in such a manner as to assure that the Panel has before it all necessary information to make an informed decision. Firstly, Commerce was notified of the Canadian Complainants objections to Dr. Lange's involvement in the investigation as soon as the Canadian Complainants learned of his involvement and Commerce responded to the objections.[369] Secondly, during a pre-hearing conference call, the Panel invited counsel for all parties to address the issue of bias during oral argument. At the oral hearing, the Panel invited and subsequently received written submissions from the parties on this issue.

As was the case in Induction Motors, this Panel takes a broad view of the Government of Canada's Complaint and finds that the issue of bias can be subsumed in the claims made in paragraphs 32 and 33. Most importantly, however, the Panel finds that the Department of Commerce was in no way prejudiced by any deficiency in the Complaint of the Government of Canada. The purpose of

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[367] CDA-90-1904-01 at 8-9.

[368] U.S.A.-90-1904-01 at 18.

[369] see Pub. Doc. No. 332; Pub. Doc. No. 382; and, Pub. Doc. No. 549.

Rule 7(a) has been fulfilled in this case and the Canadian Complainants are not prohibited from raising this issue before the Panel.

(iii) Bias

The Panel must review the *Final Determination* in this case in accordance with the general legal principles that the Court of International Trade would apply. These general legal principles include due process.

The appearance of bias or prejudgment in an administrative proceeding is sufficient to constitute a violation of due process - "it is fundamental that both unfairness and the appearance of unfairness should be avoided".[370]

Public statements by agency officials concerning the facts and issues involved in a proceeding can be sufficient evidence of prejudgment to constitute a denial of due process.[371] A speech by a Commissioner participating in a Securities and Exchange Commission proceeding criticizing a securities `violator' and indicating that the violator should be permanently barred from employment in the securities business resulted in the nullification of the proceedings in which Commissioner participated after his speech.[372] There is no way to know how the influence of one upon the others can be quantitatively measured.[373]

Several of the statements cited above, made by Dr. Lange on behalf of the Coalition, are conclusory of specific adjudicative facts relevant to the Lumber III investigation.

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370 In re. Murchinson, 349 U.S. 136; American Cyanamid Co. v. FTL, 363 F.2d 757, 767 (6th Cir. 1966).

371 Antoniu v. SEC, 877 F.2d 721, 724-26 (8th Cir. 1989), *cert. denied*, 494 U.S. 1004 (1990).

372 Stanton v. Mayes, 552 F.2d 908, (10th Cir. 1977), *cert. denied*, 434 U.S. 907 (1977).

373 American Cynamid, 363 F.2d at 767.

It is evident from the Administrative Record that Dr. Lange was more than merely the chief spokesperson for the Coalition in Lumber II - he participated in gathering evidence for the petition, he appeared as a witness before the ITC, and worked with the Administration on trade remedies for U.S. producers. It is also evident from the Administrative Record that Dr. Lange held very definite preconceived opinions about Canadian stumpage practices and log export restrictions.[374] These opinions go beyond general views of law or policy relevant to the issues addressed in the *Final Determination* and go beyond an "underlying philosophy" regarding this investigation.

(iv) Remand

The Panel has serious concerns that Dr. Lange's participation in the investigations in British Columbia and Québec may have been inappropriate and may have tainted the *Final Determination*. However, the Panel does not know from the Record before it the exact role played by Dr. Lange during the investigation, nor his role in the formulation of the *Preliminary* and *Final Determinations*. Because there exists a definite possibility of an appearance of bias, the Panel requests that Commerce provide details to the Panel (including documentation) of Dr. Lange's specific role in this investigation at all stages and of any input Dr. Lange may have had in the formulation of the *Preliminary* or *Final Determination.* Specifically, the Panel requests information regarding (1) the extent of Dr. Lange's participation in the decision-making process, (2) actions by Dr. Lange during the investigation that may have prejudiced the Canadian Complainants, and (3) the letter Ms. Anderson attempted to introduce to the Panel regarding this issue during the oral argument.

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[374] Pub. Doc. No. 332.

VIII. CONCLUSION

For the reasons stated above, the *Final Determination* is affirmed in part and remanded in part.

The results of this remand shall be provided by Commerce to the Panel within 90 days of this decision.

Date: _____
Richard G. Dearden (Chair)
(dissenting in part)

Date: _____
Lawson A.W. Hunter, Q.C.

Date: _____
Morton Pomeranz

Date: _____
Michael Reisman

Date: _____
Paul Weiler
(dissenting in part)

IX. LOG EXPORT RESTRICTIONS (DISSENT OF WEILER AND DEARDEN)

A. Introduction

In the principal opinion in the Lumber III proceedings, a majority of the Panel has remanded Commerce's *Final Determination* to countervail British Columbia's log export restrictions. The remand order instructs Commerce to reconsider its judgment about two subsidiary issues in that Determination -- regarding the "specificity" and the "direct and discernible effect" of these export restraints. It is possible that Commerce will reach precisely the same judgment as before regarding these two issues, albeit rephrased in the terms suggested by the Panel. If so, that will leave standing the major premise to Commerce's ruling -- that the fact a government measure generates some cost savings for a specific industry makes this measure a countervailable subsidy. We believe that Commerce's decision thereby to revise its decades-old policy to the contrary was a legally unjustified interpretation of the *Tariff Act*. Thus we must dissent from our colleagues' acquiescence in Commerce's unwarranted expansion of the scope of its authority.

Before delving into the legal issues, we will synopsize the economic theory relied on by Commerce. For nearly a century, British Columbia law has required that raw logs harvested from Crown land (or from land previously granted by the Crown) shall be used or manufactured within the province. Such logs can be exported only if the government determines that these logs are surplus to domestic need or unless exports would improve utilization of the timber stand. With respect to those logs that are exported, a "fee-in-lieu of manufacturing" must be paid, ranging up to 100% of the difference between the export price and the average domestic price of the logs in question. The evident aim of this government policy is to encourage log processing inside the province by guaranteeing local mills preferred access to all the logs they need in their operations. Commerce concluded that another effect of the policy was to reduce the log price paid by domestic processors by insulating these firms from foreign competition for British Columbia logs. The result of this government "distortion" of the log market was to artificially increase the output and to lower the

price of softwood lumber products manufactured in British Columbia, thence subjecting United States producers to an unfair competitive disadvantage.

That economic analysis posed to Commerce the further problem of determining the price that British Columbia producers would have paid for logs had these export restraints not been in place. Commerce's answer was that the free market price was the one paid in the Pacific Rim export market for the same species and grade of logs, adjusted downwards to take account of an expected reduction in the export price if B.C. logs were freely added to the available supply in the export market (and adjusted further for additional transportation costs in the sale of logs to foreign rather than local processors). Measured against that benchmark, the lower prices observed in the British Columbia log market were found to constitute a countervailable subsidy.[375]

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[375] As part of that ruling, Commerce found that these lower domestic log prices conferred their benefits on a specific group of industries and firms. The Panel decision has remanded this part of the *Final Determination* back to Commerce for reconsideration. We agree with the need for remand on the specificity issue, but on the following basis. In its cryptic analysis of this point, Commerce found that log export specificity was *de jure*, rather than *de facto*, in nature. The Panel majority correctly points out that Commerce's finding about whether there was a benefit from log export restraints in the form of lower domestic log prices is a matter of fact. But it does not necessarily follow that those who are the beneficiaries of these lower prices cannot be determined *de jure*, rather than *de facto* -- *i.e.*, gleaned from the face of the legislation rather than through factual investigation of which potential beneficiaries of an administrative program (such as stumpage) actually take advantage of it.

When one looks at the wording of the B.C. *Forest Act*, s. 135 says that logs that are harvested from (present or past) Crown lands are primarily reserved for use or manufacture in the province, with exports strictly limited by the government under terms stated in s. 136 of the *Act*. If as a matter of fact these export restraints produce lower domestic log prices, and if as a matter of law such cost savings can be deemed a subsidy, then it seems clear from the face of the British Columbia statute that the parties who will benefit from this program are those who use or manufacture such logs in the province. In any event, given the deferential attitude exhibited by our Panel colleagues towards Commerce's adoption of the "cost-savings" test for log exports, we believe that they should have found that Commerce's use of the *de jure* test had at least a reasonable footing.

The reason why we agree with the remand on this issue is that like the Panel majority, Commerce concentrated only on the question whether the true source of specificity among beneficiaries of this law was *de jure* or *de facto*, and thereby missed the key question of whether the scope of these beneficiaries was narrow enough to be specific in the first place. And as to this crucial question, the answer surely must be the same for log exports as it is for stumpage programs, which the entire Panel has remanded for further consideration on this point. If Commerce concludes on remand that the category of softwood lumber producers is -- or is not -- specific enough to warrant possible countervailability of provincial stumpage programs, then the category is - or is not -- specific enough for possible countervailability of British Columbia's log export restraints.

B. Cost Savings Test

Unlike the natural resource market for the right to harvest standing timber (analyzed, *supra*), there is no doubt that government policies can distort the market for raw logs and thereby influence the output and price of downstream softwood lumber markets. The Canadian Complainants took serious issue with the methodology used by Commerce to identify and measure the actual economic impact of B.C.'s log export restraints. However, their principal ground for attack on Commerce's ruling was the major expansion in countervailing duty law implied by adoption of a "cost savings" test for subsidy. The significance of this change in administrative direction is exhibited by the fact that even though B.C.'s log export restraints have been in existence throughout this century (and have been the target of a number of other U.S. government measures), there was no suggestion in either Lumber I or Lumber II that this particular B.C. policy amounted to a countervailable subsidy under the *Tariff Act*.

Administrative agencies are entitled, of course, to adopt new and different interpretations of their governing legislation if these are permissible readings of the statutory language and intent.[376] Here the immediately relevant wording is found in 19 U.S.C. § 1677 (5):

> A) In General. The term "subsidy" has the same meaning as the term "bounty or grant" as that term is used in section 303 [of the Act], and includes, but is not limited to, the following:
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>
> (ii) The following domestic subsidies, if provided or required by government action to a specific enterprise or industry, or group of enterprises or industries, whether publicly or privately owned and whether paid or bestowed directly or indirectly on the manufacture, production or export of any class or kind of merchandise:

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[376] See Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984), and Rust v. Sullivan, 111 S. Ct. 2524 (1991).

> (I) The provision of capital, loans or loan guarantees on terms inconsistent with commercial considerations.
> (II) The provision of goods or services at preferential rates.
> (III) The grant of funds or forgiveness of debt to cover operating losses sustained by a specific industry.
> (IV) The assumption of any costs or expenses of manufacture, production or distribution.

In turn, section 303 of the *Act* (19 U.S.C. § 1303) reads:

> [W]henever any country ... shall pay or bestow, directly or indirectly, any bounty or grant upon the manufacture or production or export of any article or merchandise produced in such country ... then upon the importation of such article or merchandise into the United States ... there shall be levied and paid, in all such cases, in addition to any duties otherwise imposed, a duty equal to the net amount of such bounty or grant ....

This legislative language makes clear that the list of illustrative government practices does not exhaust the meaning and scope of subsidy. For example, Commerce has regularly found that various government tax rebates constitute countervailable subsidies because of the resemblance of such measures to those explicitly listed in the statute.[377]

The Canadian Complainants argued at length that Commerce's reading of § 1303 and § 1677 produced an unwarranted overlap with section 301 of the *Trade Act of 1974* (modified at 19 U.S.C. § 2411), a provision that targets a host of unfair trade practices -- including "unjustifiable or unreasonable restrictions on access to ... raw materials." The historical evolution of both § 1301 and 1303 traced by the Canadian Complainants in their briefs does indicate that Commerce assumed that the principal weapon for combating foreign border measures would be "unfair trade practice" law rather than "countervailing duty" law. Certainly, the availability of this statutory recourse under § 1301 is a sufficient answer to any argument that expansive interpretation of § 1303 and § 1677 is

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[377] *e.g.*, Potassium Chloride from Spain, 49 Fed. Reg. 36,424 (1984), and Non-Rubber Footwear from Argentina, 49 Fed. Reg. 9,922 (1984).

indispensable for the U.S. government to be able to deal with such practices that may be having an adverse impact on U.S. producers.

Still, as Commerce points out, on its face the *Tariff Act* does not preclude the application of both § 1301 and § 1303 (or § 1677) to the same foreign government practices. In addition, such an overlap between the two statutory measures may well have been judged by Congress to be a reasonable way of allowing each provision to be deployed against the different trade consequences of the same border measures adopted by foreign governments. For example, in this case § 1667 would allow imposition of a countervailing duty on B.C. softwood lumber products that might otherwise enjoy a competitive advantage against U.S. producers in the U.S. market. However, unfair trade practice penalties would be required to press British Columbia to give U.S. producers access to B.C. logs and thereby enable them to compete better with B.C. producers in softwood lumber product sales in the Japanese market.[378]

C. Scope of The Definition of Subsidy

The more fundamental problem posed by Commerce's *Final Determination* is not just its use of § 1677 against a border measure, but its underlying rationale that any foreign government measure that generates any cost savings for a specific industry group is a countervailable subsidy.[379] This interpretation of the term "subsidy" -- which was explicitly announced for the first time in this case --

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[378] Another important theme in the Canadian Complainant's argument was that even if British Columbia's log export policy did reduce log prices paid by domestic producers, the B.C. government was simply correcting the market malfunction effected by Japan which limited import of softwood products and thence artificially enhanced the demand for and price of B.C. logs. That argument might be a good practical reason why the U.S. government might not use section 301 unfair trade practice penalties to force B.C. to relax its log export restraints. It is not, however, a good legal reason for denying the possible "subsidy" quality to the B.C. government's intervention in an admittedly imperfect, but still competitive, Pacific Rim log market (see ASG Industries v. United States, 467 F. Supp. 1200 (1979)).

[379] Indeed, when one reads the Panel majority decision on this issue, it is evident that almost all the majority's attention was focused on the question of whether use of subsidy law against border measures squared with other provisions of United States trade law or with its international trade obligations under *GATT*. With all due respect to our colleagues, the result is that the majority decision never seriously addresses the more fundamental legal problems that are posed by Commerce's adoption of its "cost savings" test as the general principle governing countervailability of any type of government law or program.

constitutes a qualitative expansion of the natural meaning of the statutory wording and a sharp break with a century of administrative practice. In addition, the severe difficulties encountered by Commerce in identifying and measuring any such cost savings actually conferred by B.C.'s log export restraints exemplifies the reasons why both Congress and prior Administrations have judged the narrower interpretation to be the more sensible one.

In enacting § 1677(5) containing the new term "subsidy" and its four statutory examples, Congress directed that "to the extent [that] the [four illustrative] enumerations [of a domestic subsidy] under this provision might provide a basis for expanding the present standard," such expansion of the list must be "consistent with the underlying principles implicit in these enumerations" and only "then [can] the standard ... be so altered.".[380] When one looks closely at the illustrative list of subsidies, the key family resemblance among them seems clear: each measure involves a government paying or bestowing some kind of monetary benefit upon the producers in question.

1. Providing capital, loans, or loan guarantees at prices that are lower or on terms that are better than those dictated by normal commercial considerations;[381]

2. Providing goods or services at preferential rates (i.e. cheaper prices) than those observed in benchmark markets;[382]

3. Granting funds or forgiving debts to cover a firm's operating losses;[383]

4. Assuming a firm's costs or expenses of either manufacture, production, or distribution.[384]

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380 H.R. Rep. No. 317, 96th Cong. 1st Sess. 74 (1979) (as quoted in Lumber III).

381 see, *e.g.*, Industrial Phosphoric Acid from Israel, 52 Fed. Reg. 25,447 (1987).

382 see, *e.g.*, Carbon Black from Mexico, 51 Fed. Reg. 30,385 (1986).

383 see, *e.g.*, Stainless Steel Sheet, Strip and Plate from the United Kingdom, 48 Fed. Reg. 19,048 (1984).

384 see, *e.g.*, Certain Steel Products from the Federal Republic of Germany, 47 Fed. Reg. 39,345 (1982).

That same characteristic is shared by the principal examples of unlisted measures deemed countervailable subsidies -- direct grants to favored domestic producers,[385] or favorable tax treatment or tax rebates conferred upon the industry in question.[386] And precisely the same common theme runs through the illustrative list provided in the GATT *Subsidies Code* (pursuant to which the current version of section 677 was enacted in the *Trade Agreements Act of 1979*):

> Examples of possible forms of such subsidies are: government financing of commercial enterprises, including grants, loans or guarantees; government provision or government financed provision of utility, supply distribution and other operational or support services or facilities; government financing of research and development programmes, fiscal incentives; and government subscriptions to, or provision of, equity capital.[387]

In every one of these cases in which it is said that the government is paying or bestowing a subsidy, bounty, or grant upon a producer, some kind of identifiable financial transaction takes place between the two; the government either makes a grant or loan to, or pays an expense of, the producer, or the government foregoes the full rate that it might have charged for provision of capital, goods, or services, or in collection of taxes owed. In that respect, the statutory list and administrative history of subsidy determinations are qualitatively different from the governmental measure at issue here -- a B.C. law that gives domestic softwood lumber producers first call on all the B.C. logs they might need, thereby allegedly reducing the market price these producers pay private logging firms to purchase the logs.[388]

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385 see, *e.g.*, Industrial Phosphoric Acid from Israel, 52 Fed. Reg. 25,447 (1987).

386 see, *e.g.*, Stainless Steel Cooking Ware from Korea, 51 Fed. Reg. 42,867 (1988).

387 Article 11, Par. 3.

388 Commerce and our majority Panel colleagues did cite language in a Customs Court ruling in ASG Industries v. United States, 467 F.Supp. 1200 (1979), to the effect that "whether the reduction in cost is occasioned by direct cash payment, or by an act of government reducing labor cost, capital cost, or the cost of any other factor of production is of no consequence [in finding a] bounty or grant on production." However, the Italian government action at issue in that case involved investment grants, low-interest rate financing, and reduction of normal contributions to state welfare organizations -- precisely the kinds of subsidies now listed in § 1677. The focus of the judicial ruling in ASG Industries was on whether such

For textual support of this much broader "cost savings" reading of § 1677 and § 1303, Commerce pointed to the phrase "whether paid or bestowed directly or indirectly." As the Canadian Complainants highlight in their submissions, "... the phrase `directly or indirectly' in the statute relates to the method of conferring a subsidy, not to the existence of a subsidy in the first place".[389] In fact, that particular phrase has historically been used only to cover cases in which rather than confer the benefit itself, the foreign government arranges with a private firm (typically, a bank) to act as the intermediary in providing the subsidy (usually low interest loans) to the producers favored by government policy.[390] The actual assistance provided by the intermediary in question still took the form of a financial transaction with the favored firms at less than benchmark rates.

D. Leather From Argentina

Prior to the Leather From Argentina determination in 1990 (which did not advert to this underlying issue of legal principle), no prior Administration had ever applied this century-old countervailing duty legislation to find that a government measure not involving a financial transaction was a subsidy on the grounds simply that it saved costs of production for domestic firms. Indeed, in a number of cases involving export measures such an interpretation had been explicitly rejected.

The first such reported case was Litharge from Mexico,[391] in which the Treasury Department (which was then responsible for administering this law) rejected a claim that a Mexican tax on the export of lead was a countervailable program on the grounds that it reduced the domestic price of lead that was the major input in the manufacture of litharge. While a lower court judge disagreed

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financial assistance by the government was countervailable even if the Italian government's motive was to offset higher costs experienced by firms locating in underdeveloped and less prosperous regions.

389 Canadian Complainants' Joint Brief, at D-49.

390 see, *e.g.*, Potassium Chloride from Spain, 49 Fed. Reg. 36,424 (1984); Oil Country Tubular Goods from Korea, 49 Fed. Reg. 46,776 (1984); Certain Granite Products from Spain, 53 Fed. Reg. 24,340 (1988); and Rice from Thailand, 51 Fed. Reg. 12,356 (1986).

391 67 Treas. Dec. 142 (1967).

with that administrative determination,[392] his ruling was itself reversed by the U.S. Court of Custom and Patent Appeals on the jurisdictional ground that negative countervailing duty determinations were not reviewable in the courts.[393] Several years later, in the *Trade Act of 1974*, Congress amended the statute to give the same right of judicial review to American producers denied a favorable administrative ruling as had hitherto been enjoyed by importers who had been subjected to a countervailing duty. In enacting that legislation Congress expressed no view, one way or the other, about the substantive merits of the question presented in Litharge from Mexico.

As a result of the 1979 *Trade Agreements Act*, the Commerce Department assumed principal responsibility for administration of the *Tariff Act*. In a trilogy of Determinations in the mid-1980s, Commerce reconfirmed the position that border measures were not countervailable subsidies.[394] In these rulings Commerce made a variety of observations about why none of these programs were countervailable. However, the common theme in each determination was that the petitions asked for an unwarranted expansion of the scope of countervailing duty law. As Commerce stated in response to the petition about Australian limits on steel imports:

> We will not investigate these allegations because we do not view such practices to be subsidies ... Here, the allegations are not that the government has provided some specific monetary benefit upon the product in question (or something equivalent thereto) but that the product has been subsidized by government restrictions ... While it may be true that in an abstract economic sense such import restrictions, in lessening competition in the domestic marketplace, do provide some benefits of at least a temporary nature to the domestic producers of the product, that is far from saying that such restrictions properly can be viewed as conferring a subsidy within the meaning of the countervailing duty law. To conclude even that the petitioner has made a valid prima facie allegation would be tantamount to concluding that every time any government, including the U.S. government, through duties, quotas, or otherwise acts to restrict imports of a product competing with a domestically produced product,

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392 Hammond Lead Products Inc. v. United States, 306 F. Supp. 460 (Cus. Ct. 1969).

393 Hammond Lead Products Inc. v. United States, 440 F.2d 1024 (C.C.P.A. 1971).

394 see Anhydrous and Aqua Ammonia from Mexico, 48 Fed. Reg. 28,522 (1983) (export tax on petrochemicals); Galvanized Carbon Steel Sheet from Australia, 49 Fed. Reg. 3,687 (1984) (limitations on steel imports); and Non-Rubber Footwear from Argentina, 49 Fed. Reg. 9,922 (1984) (export tax on hides).

> it necessarily subsidizes. If so, all governments subsidize most products most of the time. Totally apart from the virtually impossible task of attempting to quantify such a benefit for countervailing duty purposes, the absurdity of such a proposition is self-evident and necessarily beyond the intent of Congress in enacting the countervailing duty law.[395]

Given this long-established and recently re-confirmed understanding of the scope of countervailing duty law, it is not surprising that no suggestion was made in either Lumber I or Lumber II that British Columbia's century-old log export restraints were countervailable. It was not until Leather from Argentina[396] that the first-ever administrative determination was made that a border measure was countervailable. As we noted above, the administrative authors of that ruling did not seem to realize the fundamental change in statutory direction they were taking. Instead, after finding that the embargo upon export of capital hides benefited a single "specific" industry, leather tanning, Commerce simply stated that it would hold petitioners "to an extremely high standard of proof, requiring them to substantiate their claim that the embargo had a direct and discernible effect on hide prices in Argentina,"[397] (a burden that Commerce then found was satisfied in the particular circumstance of that case). Thus, while Leather from Argentina led Commerce to invite consideration of the status of B.C.'s log export restraints, it was in Lumber III that the issue was first seriously

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395 49 Fed. Reg. at 8,658. Commerce made much the same observations about the petition regarding Mexico's export tax on petrochemicals in Anhydrous and Aqua Ammonia from Mexico:

> Although the imposition or removal of a disadvantage may affect production of a particular good and thus its trade flow, a bounty or grant does not necessarily result. Such logic would lead us to conclude that the imposition or non-imposition of virtually any disadvantage is or may be a subsidy. Any time a government intervened at the border -- such as with export taxes, import duties, or quantitative import or export restrictions on a product used as an input in further production -- such action arguably could increase the quantities (and possibly lower the prices) of the domestically produced input product available in further production. The proposition that such governmental action necessarily confers bounties or grants is untenable on its face, and unsupported by the Act and its legislative history. (See 49 Fed. Reg. 28,522 at 28,524-525).

396 55 Fed. Reg. 40,212 (1990).

397 *Ibid.*, at 40,213.

joined about whether such a reversal of administrative policy was compatible with the governing legislation.[398]

In our view, the new interpretation proffered by Commerce in this case is not a legally permissible interpretation of the relevant wording of the *Tariff Act*. Our principal reason for that judgment is that the open-ended "cost savings" test is not the natural and ordinary reading of the phrase "subsidy [or bounty or grant] paid or bestowed by the government" (even paid or bestowed indirectly, through an intermediary), as illustrated by the four examples then enumerated in the statute. We are also cognizant of the severe practical problems that would flow from such a qualitative expansion of the scope of this legislative provision -- problems that have uniformly persuaded prior Administrations not to pursue the path taken by Commerce here.

The first problem is that there is absolutely no intrinsic limitation to the scope of government actions that can be alleged to be subsidies to the extent they generate cost savings for specific groups of industries. This case happens to involve an export restraint that is believed to lower the price paid by domestic producers for a manufacturing input. Exactly the same kind of attack could be made against a foreign government that reduced the tariffs or other barriers to importation of such an input. Ironically, then, if the United States government were to negotiate with Canada a reduction in barriers to entry of American goods and services that helped reduce the cost of production of certain Canadian manufacturers, Lumber III would entitle American competitors of these Canadian manufacturers to seek the imposition of countervailing duties against exports by the latter firms into this country.

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[398] In its reasons for decision, the Panel majority downplays this statutory history by pointing to arguable factual distinctions and verbal qualifications in the prior cases. However, the key events in that history are undisputed: no prior Administration had ever accepted the invitation to interpret the term "subsidy" (or "bounty" or "grant") as encompassing pure "cost saving" measures; the Reagan Commerce Department consciously and explicitly rejected this statutory reading for reasons of both law and policy; and the reversal of direction by the Bush Commerce Department in Leather from Argentina occurred without Commerce even adverting -- at least openly -- to the broader significance of the step it was taking. And contrary to what the majority Panel states in its decision, that the log export restrictions examination was "[a]s result of a petition filed by the Coalition" (see p. 61), in fact it was Commerce in its Reasons for Self-Initiation in Lumber III that raised for the first time the question whether Canada's long-standing log export restraints might be countervailable.

Indeed, the "cost savings" principle cannot be confined to border measures, but instead is potentially applicable to every law, regulation, or other measure adopted by a government. An illustration that emerged at the hearing of this appeal was the action taken by the U.S. government in 1986 to adopt a no-fault vaccine injury compensation program designed to relieve manufacturers of the spiralling cost of tort litigation. The oft-cited Chevron case provides another apt example: a government that adopts a "bubble" (or broader "emissions rights") program to give its businesses greater flexibility in meeting environmental standards at lower cost. The tacit assumption of Commerce's Lumber III ruling is that any such sensible "cost savings" measure adopted by a foreign government would constitute a countervailable subsidy for purposes of the *Tariff Act*.

Commerce's response to those concerns is that there are other limitations upon countervailability than the concept of subsidy. However, a prior section of this Panel decision has demonstrated the difficulties inherent to Commerce's approach to the principal statutory constraint -- "specificity". Commerce's Determination in Lumber III also demonstrated how illusory is the other apparent constraint articulated in Leather from Argentina -- that petitioners must satisfy "an extremely high standard of proof" that the government action had "a direct and discernible effect" on production costs.

A crucial difference between the narrower "financial transactions" and the open-ended "cost savings" test of subsidy is that the former provides some kind of monetary benchmark against which Commerce can reliably identify and measure the supposed cost savings to producers in order to assess a countervailing duty against their products.[399] While economic theory predicts that one would

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[399] The Panel majority acknowledged -- as did Commerce in its *Final Determination* -- that the *ejusdem generis* principle requires that "where general words follow an enumeration of ... things by words of a particular and specific meaning, such general words are not to be construed in their widest extent, but are to be held as applying only to ... things of the same general kind or class as those specifically mentioned" (see *supra*). However, we respectfully disagree with the majority Panel that the only alternative to an open-ended "cost savings" test was an extremely narrow "legal tender" test: *i.e.*, governments can only provide benefits by paying cash to, or forgoing revenue from, domestic producers. Since this "legal tender" test is obviously incompatible with some of the listed examples of "subsidy", the majority may have felt driven to ratify Commerce's choice of a "cost savings" test that sweeps under this statutory shadow every imaginable form of government measure that helps reduce domestic costs of production in any specific group of industries. The majority of the Panel does not even allude to, let alone try to refute, the intermediate "financial transactions" test which, as we have shown in the text of this dissent, more

normally find some reduction in price from a government measure that excludes some potential sources of demand for the product in question, it is a challenging task to verify that this has happened in any concrete case,[400] and if so, to what extent.[401]

That problem appeared relatively manageable in Leather from Argentina because for the prior two decades the government of Argentina had regularly imposed and then removed its export restraints. Thus Commerce could observe how these government actions produced "direct and discernible" divergence, and then convergence, in Argentina and United States hide prices (the latter being taken as the market benchmark). Two major problems stood in the way of Commerce making such calculations in the case of B.C.'s log export restraints. One was the fact that the much higher cost of shipping raw logs rather than processed lumber tends to produce segmented log markets that pair timber stands and nearby mills; these markets display a considerable range of log prices, even without any legal obstacles to log shipments, from one market to the other (as exhibited, for example, within and between states in the Pacific Northwest). The other reason is that since British Columbia log export restraints had been in existence throughout this century, Commerce could not follow the example of Leather from Argentina and simply observe what had been the apparent price effect of lifting the restraints entirely.

Just as was true for stumpage rates, the only direct evidence prepared for and offered in these proceedings about the apparent price effect of B.C.'s log export restraints came from the Canadians -- in the form of empirical studies conducted by Drs. Joseph Kalt and William Finan. These studies examined the consequences of the sharp hike in British Columbia's fee-in-lieu of manufacture from

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aptly captures the wording of and prior history of the statute. And as we will explain *infra*, drawing the subsidy boundary (as have all previous Administrations) in terms of financial transactions rather than cost savings avoids the huge practical problems that Commerce tried -- unsuccessfully -- to deal with in Lumber III itself.

400 The Canadian Complainants trace Commerce's recognition of their measurement difficulties in previous determinations in their Joint Brief, at D-71.

401 An important comparative virtue of section 301's unfair trade practices provision is that the government there does not have to quantify the precise competitive advantage gained by producers in the foreign country in order to adopt trade measures that prod their government to remove the offending measure.

1986 to 1989, a government decision that in turn cut by two-thirds (from 3% to 1%) the export share of B.C.'s total log harvests. Neither Drs. Kalt nor Finan found any effect from these changes in government policy or export volume upon the ratio of export to domestic log prices that the petition assumed must result from B.C.'s log export restraints.

Commerce rejected this direct evidence on the grounds that B.C.'s log exports constituted too small a share of the Pacific Rim log market to make it likely that one would observe any price effect from these modest changes in the policy and the volume (though no specific documentation was offered for these reasons for rejection).[402] Commerce relied, instead, on a paper written in 1986 by Drs. Margolick and Uhler on The Economic Impact of Removing Log Export Restrictions in British Columbia. The Canadian Complainants detailed at length the major problems[403] in Commerce's reliance upon this document for its purposes (neither Drs. Margolick nor Uhler were asked to comment on the relevance of their economics paper to these legal proceedings):

1. Though Commerce appeared to assume that Drs. Margolick and Uhler had conducted a "correlation analysis (*i.e.*, regression analysis)" these two authors did not themselves undertake any empirical investigation of whether in fact there was the kind of interplay between domestic and export log markets that was the key predicate for Commerce's Determination. Instead, operating on the assumption that such a relationship existed (and borrowing supply and demand elasticities from earlier studies that had been done for different purposes), Drs. Margolick and Uhler sought only to simulate what would be the various effects upon the B.C. economy if the government were to remove direct log export restraints and rely simply on the export tax.

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[402] For example, the fact that log exports are a tiny share (whether 3% or 1%) of B.C.'s total harvest does not imply that present log exports from B.C. are a tiny share of the Pacific Rim log export market, such that a sharp drop in the B.C. log export share could have no observable impact on prices. Commerce offered no evidence on that latter point. In addition, Commerce was itself mistaken in reading (and rejecting) Kalt's analysis as based on what would have been an incorrect assumption that all of the log exports from B.C. were subject to a 100% fee-in-lieu-of-manufacture.

[403] Our colleagues address some of these problems in the section of their decision dealing with calculation issues (at pp.118-125). We have serious reservations about the majority's comments about some of these issues -- *eg.*, the empirical value of the Margolick-Uhler and Newport studies. In view of our judgment that log export restraints are non-countervailable as a matter of law, we do not take any position about the proper disposition of the calculation issues raised by all parties.

2. A review and update by C. A. Newport of the Margolick-Uhler paper simply offered the author's personal opinion that the elasticities relied upon by Drs. Margolick and Uhler were still valid, without addressing the question of whether significant changes that had occurred throughout the 1980s in the structure of the Pacific Rim log market might have altered the earlier economic relationships.

3. Doctors Margolick and Uhler had relied for their calculation upon 1983 log prices, grades, and quantities for the B.C. Coastal log market. While the Newport update incorporated 1989 Coastal data, neither Margolick-Uhler nor Newport offered Commerce any evidentiary basis for estimating a possible effect of restraints on the export of logs from the B.C. Interior (in particular, from the Border Interior for which Commerce found a subsidy effect in its Determination).

4. Most important, the Margolick-Uhler Study, and Newport Study totally ignored the implications of the "derived demand" effect that had been detailed by Drs. Kalt and Finan in their submissions to Commerce. Without elaborating in detail on this well-established economic concept, it is sufficient to state that if a relaxation of B.C.'s log export policy produced greater foreign demand for B.C. logs, it would also reduce the foreign demand for the softwood products domestically processed from these logs. Thus, while increased demand from foreign processors would tend by itself to raise the price of B.C. logs, the coincident reduction in demand for logs by domestic processors would tend to decrease the price. It is an empirical question whether or not these two contrasting price tendencies would be precisely offsetting; this would depend on the actual levels of and complex relationships between foreign and domestic demand for both B.C. logs and softwood lumber.[404] However, having rejected the negative evidence from Drs. Kalt and Finan, Commerce had absolutely no positive evidence upon which to determine that B.C.'s log export restraints were not only encouraging processing of logs in the province, but were also reducing the price of this input in the production of softwood lumber products destined for the U.S. market. [405]

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[404] Indeed, Commerce itself made precisely the same point in Non-Rubber Footwear from Argentina, 49 Fed. Reg. 9,922 (1984) at 9,923, in rejecting a cvd petition against an export tax which alleged that this government measure was reducing domestic prices and production costs, stating: "Actual prices, however, depend upon a complicated interaction of domestic and international supply and demand elasticities."

[405] We should make clear that consideration of the "derived demand" effect is entirely different from calculating a "net economic effect" of the government measure on a firm's production and pricing decisions. For example, if a government provides an admitted subsidy (e.g., low interest loans) to firms to locate in an economically depressed region, Commerce is correct in stating (at 57 Fed. Reg. 22,804-05) that it is not required to trace through the net effect of this subsidy by offsetting the additional expenses incurred by the firm in this high-cost region. But in the case of log export restraints, what is precisely at issue is whether B.C.'s log export policy provided any (and then how much) subsidy, under Commerce's new "cost savings" definition of that term. In its investigation of the impact of B.C.'s policy, Commerce cannot focus simply on one economic tendency of elimination of log export restraints -- increasing export demand -- and turn a blind eye to another corresponding tendency -- reduction in domestic

Throughout its Determinations and its briefs for this appeal, Commerce contended that a legal requirement that the Department undertake a systematic empirical demonstration of what actually would be the domestic price of B.C. logs (to both Interior as well as Coastal producers) absent log export restraints imposed too rigorous a barrier to the application of its new concept of countervailable subsidy. As quoted earlier, that is precisely the reason why previous Administrations had refused to stretch the statutory term and illustrations of subsidy (or bounty and grant) beyond their natural connotations, and embark on the guesswork of determining whether and how much cost savings might be generated for specific producers by the innumerable measures taken by foreign governments.

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demand. Only if the overall result of these two tendencies is to generate some increase in B.C. log prices can Commerce find that this crucial factual predicate of its legal interpretation has been satisfied.

E. Conclusion

Lumber III presented two crucial questions about the scope and limits of U.S. countervailing duty law. One question was whether some kind of distortion in the operation of free competitive markets is a necessary predicate to finding that a particular government measure -- here, pricing of a natural resource -- is a countervailable subsidy. The second question was whether the bare fact that a government measure generates some cost savings for specific groups of private producers is sufficient to make that measure -- here, restriction of log exports -- countervailable.

In turn, this case presented important questions about the appropriate scope and limits of judicial review of decisions made by administrative agencies. The teaching of the U.S. Supreme Court in Chevron, U.S.A. Inc. v. Natural Resources Defense Council,[406] is that administrative agencies must be given the latitude to adopt reasonable interpretations of their governing statutes. But as the Supreme Court has itself made clear since Chevron, affected parties also have the right to expect that reviewing courts will exercise their responsibility to ensure that agencies respect the key boundaries established by Congress around regulatory programs.[407] By reason of the *Free Trade Agreement* between the United States and Canada, that judicial responsibility was entrusted here to a binational panel, the principal body for scrutinizing the legal judgments made by a Commerce Department that invited, investigated, and adjudicated this trade dispute between the two nations.

In coming to these conclusions, we have followed the same approach to judicial review of the *Final Determination* regarding both the stumpage-preferentiality part of the decision and the part of

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406 467 U.S. 837 (1984).

407 An apt analogy for this case is Board of Governors of the Federal Reserve System v. Dimension Financial Corp., 474 U.S. 361 (1986), in which the Court rejected an effort to expand the scope of statutorily-regulated "banks" in order to encompass institutions which were providing financial services that were the functional equivalent of those denominated on the face of the legislation (e.g., NOW accounts that in practice closely resemble accounts where the depositor has a legal entitlement to withdraw funds on demand). Comparable recent decisions include Public Employees Retirement System v. Betts, 492 U.S. 158 (1989), and EEOC v. Arabian Am. Oil Co., 111 S. Ct. 1227 (1991).

the decision concerning log export restrictions. After close analysis of the statutory wording, the administrative history, and the economic realities, we concluded that Commerce had gone beyond the letter and spirit of the *Tariff Act* both in rejecting the "market distortion" criterion and in adopting the "cost savings" criteria for subsidy decisions.

The tack taken by the Panel majority in the log export part of this decision is markedly different. The majority decision recites and dismisses a long list of arguable legal flaws, asserted by the Canadian Complainants, in Commerce's *Final Determination*. As noted earlier in this dissent, we agree that with respect to a number of these objections (for example, the overlap of cvd and unfair trade practice law in dealing with border measures), Commerce's position is legally reasonable, whether or not practically sound. But the majority's approach meant that they did not really focus on the key issue in this case -- the legal significance of Commerce's expansion of U.S. trade law through the adoption of its new "cost-savings" test of countervailable subsidy.

Under the *Free Trade Agreement* and the *Tariff Act*, this Panel's responsibility is to ensure that Commerce complies with Congress' statutory wording and intent. For that reason, we dissent.