

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

**AB-2003-6**

*Report of the Appellate Body*



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<i>Brazil – Aircraft</i>	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/AB/R, adopted 20 August 1999, DSR 1999:III, 1161.
<i>Brazil – Aircraft (Article 21.5 – Canada II)</i>	Panel Report, <i>Brazil – Export Financing Programme for Aircraft, Second Recourse by Canada to Article 21.5 of the DSU ("Brazil – Aircraft (Article 21.5 – Canada II) ")</i> , WT/DS46/RW/2, adopted 23 August 2001.
<i>Brazil – Desiccated Coconut</i>	Appellate Body Report, <i>Brazil – Measures Affecting Desiccated Coconut</i> , WT/DS22/AB/R, adopted 20 March 1997, DSR 1997:I, 167.
<i>Canada – Aircraft</i>	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377.
<i>Canada – Dairy</i>	Appellate Body Report, <i>Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products</i> , WT/DS103/AB/R, WT/DS113/AB/R and Corr.1, adopted 27 October 1999, DSR 1999:V, 2057.
<i>Canada – Dairy (Article 21.5 – New Zealand and US)</i>	Appellate Body Report, <i>Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products, Recourse to Article 21.5 of the DSU by New Zealand and the United States</i> , WT/DS103/AB/RW, WT/DS113/AB/RW, adopted 18 December 2001.
<i>EC – Asbestos</i>	Appellate Body Report, <i>European Communities – Measures Affecting Asbestos and Asbestos-Containing Products</i> , WT/DS135/AB/R, adopted 5 April 2001.
<i>EC – Bananas III</i>	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591.
<i>EC – Bed Linen (Article 21.5 – India )</i>	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India, Recourse to Article 21.5 of the DSU by India</i> , WT/DS141/AB/RW, adopted 24 April 2003.
<i>India – Patents (US)</i>	Appellate Body Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products</i> , WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9.
<i>US – Canadian Pork</i>	GATT Panel Report, <i>United States – Countervailing Duties on Fresh, Chilled and Frozen Pork from Canada</i> , adopted 11 July 1991, BISD 38S/30.
<i>US – Carbon Steel</i>	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002.
<i>US – Corrosion-Resistant Steel Sunset Review</i>	Appellate Body Report, <i>United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan</i> , WT/DS244/AB/R, adopted 9 January 2004.
<i>US – Countervailing Measures on Certain EC Products</i>	Appellate Body Report, <i>United States – Countervailing Measures Concerning Certain Products from the European Communities</i> , WT/DS212/AB/R, adopted 8 January 2003.
<i>US – Countervailing Measures on Certain EC Products</i>	Panel Report, <i>United States – Countervailing Measures Concerning Certain Products from the European Communities</i> , WT/DS212/R, adopted 8 January 2003, as modified by the Appellate Body Report, WT/DS212/AB/R.
<i>US – Export Restraints</i>	Panel Report, <i>United States – Measures Treating Exports Restraints as Subsidies</i> , WT/DS194/R and Corr.2, adopted 23 August 2001.

Short Title	Full Case Title and Citation of Case
<i>US – FSC</i>	Appellate Body Report, <i>United States – Tax Treatment for "Foreign Sales Corporations"</i> , WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, 1619.
<i>US – Section 211 Appropriations Act</i>	Appellate Body Report, <i>United States – Section 211 Omnibus Appropriations Act of 1998</i> , WT/DS176/AB/R, adopted 1 February 2002.
<i>US – Softwood Lumber III</i>	Panel Report, <i>United States – Preliminary Determinations with Respect to Certain Softwood Lumber from Canada</i> , WT/DS236/R, adopted 1 November 2002.
<i>US – Softwood Lumber IV</i>	Panel Report, <i>United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada</i> , WT/DS257/R and Corr.1, 29 August 2003.

WORLD TRADE ORGANIZATION  
APPELLATE BODY

**United States – Final Countervailing Duty  
Determination with Respect to Certain  
Softwood Lumber from Canada**

United States, *Appellant/Appellee*  
Canada, *Appellant/Appellee*

European Communities, *Third Participant*  
India, *Third Participant*  
Japan, *Third Participant*

AB-2003-6

Present:

Baptista, Presiding Member  
Lockhart, Member  
Sacerdoti, Member

## **I. Introduction**

1. The United States and Canada each appeals certain issues of law and legal interpretation in the Panel Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* (the "Panel Report").<sup>1</sup> The Panel was established to consider a complaint by Canada concerning countervailing duties imposed by the United States against imports of certain softwood lumber products from Canada ("softwood lumber"). Before the Panel, Canada challenged a number of aspects of the final determination by the United States Department of Commerce ("USDOC") that led to the imposition of the duties.

2. On 22 May 2002, USDOC published in the United States Federal Register a countervailing duty order in respect of softwood lumber from Canada.<sup>2</sup> The countervailing duty order followed a final countervailing duty determination by USDOC on 21 March 2002.<sup>3</sup> In that determination, USDOC found that softwood lumber benefited from countervailable subsidies attributable to a

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<sup>1</sup>WT/DS257/R, 29 August 2003.

<sup>2</sup>Panel Report, para. 2.4. See also "Notice of Amended Final Affirmative Countervailing Duty Determination and Notice of Countervailing Duty Order: Certain Softwood Lumber Products From Canada", United States Federal Register, 22 May 2002 (volume 67, number 99), p. 36070.

<sup>3</sup>Panel Report, para. 2.1. USDOC's final countervailing duty determination was published in the United States Federal Register as: "Notice of Final Affirmative Countervailing Duty Determination and Final Negative Critical Circumstances Determination: Certain Softwood Lumber Products from Canada" (the "Final Determination"), United States Federal Register, 2 April 2002 (volume 67, number 63), p. 15545. The United States Federal Register notice made reference to a further document entitled "Issues and Decision Memorandum: Final Results of the Countervailing Duty Investigation of Certain Softwood Lumber Products from Canada" (the "*Decision Memorandum*"), (unpublished, Exhibit CDA-1 submitted by Canada to the Panel), which was generally referred to in the Panel Report as the "USDOC Final Determination".

number of Canadian government programs. USDOC found that, by conferring a right to harvest timber through stumpage programs, certain provincial governments provided goods to lumber producers.<sup>4</sup> According to USDOC, these goods were provided at less than adequate remuneration, thereby conferring a benefit.<sup>5</sup> USDOC also found that the subsidies conferred through the stumpage programs were specific to an industry or group of industries.<sup>6</sup>

3. Canada argued before the Panel that USDOC's final countervailing duty determination was inconsistent with the United States' obligations under Articles 1.2, 2.1, 2.4, 10, 12, 14, 14(d), 19.1, 19.4 and 32.1 of the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement") and Article VI:3 of the General Agreement on Tariffs and Trade 1994 (the "GATT 1994").

4. The Panel Report was circulated to Members of the World Trade Organization ("WTO") on 29 August 2003. In the Panel Report, the Panel concluded, at paragraph 8.1:

- (a) that the USDOC's determination that provision of stumpage constituted a financial contribution in the form of the provision of a good or service was not inconsistent with Article 1.1 (a) (1) (iii) [of the] SCM Agreement, and we therefore *reject* Canada's claim that the United States' imposition of countervailing duties on the basis of that determination was inconsistent with Articles 10, 19.1, 19.4 and 32.1 [of the] SCM Agreement, and Article VI:3 of GATT 1994;
- (b) that the USDOC's determination of the existence and amount of benefit to the producers of the subject merchandise was inconsistent with Articles 14 and 14(d) [of the] SCM Agreement, and we therefore *uphold* Canada's claim that the United States' imposition of countervailing duties on the basis of that determination was inconsistent with Articles 14, 14(d), 10 and 32.1 [of the] SCM Agreement; ...<sup>7</sup>

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<sup>4</sup>*Decision Memorandum, supra*, footnote 3, pp. 29–30.

<sup>5</sup>*Ibid.*, p. 45.

<sup>6</sup>*Ibid.*, p. 52.

<sup>7</sup>Having reached this conclusion with respect to Canada's claim regarding the existence and amount of a benefit, the Panel declined to rule on Canada's additional allegation that USDOC's flawed benefit analysis meant that the United States imposed countervailing duties in a manner inconsistent with Articles 19.1 and 19.4 of the *SCM Agreement*.



- (c) that the USDOC's failure to conduct a pass-through analysis in respect of upstream transactions for log and lumber inputs between unrelated entities was inconsistent with Article 10 [of the] SCM Agreement and Article VI:3 of GATT 1994, and we therefore *uphold* Canada's claim that the United States' imposition of countervailing duties in respect of such transactions was inconsistent with Articles 10 and 32.1 [of the] SCM Agreement and Article VI:3 of GATT 1994; ...<sup>8</sup> (original italics)

5. The Panel also found that USDOC's determination that provincial stumpage programs provide *specific* subsidies within the meaning of Article 2.1 was not inconsistent with the *SCM Agreement*.<sup>9</sup> The Panel declined to rule on Canada's claims regarding the methodology used by USDOC to calculate the subsidy rate and USDOC's conduct of the investigation.<sup>10</sup> The Panel concluded that, to the extent the United States acted inconsistently with the provisions of the *SCM Agreement* and the GATT 1994, the United States had nullified or impaired benefits accruing to Canada under those Agreements. The Panel therefore recommended that the Dispute Settlement Body (the "DSB") request the United States to bring its measure into conformity with its obligations under the *SCM Agreement* and the GATT 1994.<sup>11</sup>

6. On 2 October 2003, the United States notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*").<sup>12</sup> On 3 October 2003, for scheduling reasons, the United States withdrew its Notice of Appeal pursuant to Rule 30 of the *Working Procedures*, conditional on its right to re-file the Notice of Appeal at a later date.<sup>13</sup> On 21 October 2003, the United States re-filed a substantively identical Notice of Appeal pursuant to

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<sup>8</sup>Having reached this conclusion with respect to Canada's claim regarding the need for a pass-through analysis, the Panel declined to rule on Canada's additional allegation that USDOC's failure to complete a pass-through analysis meant that the United States imposed countervailing duties in a manner inconsistent with Articles 19.1 and 19.4 of the *SCM Agreement*.

<sup>9</sup>Panel Report, para. 8.1(d). (This finding of the Panel is not appealed)

<sup>10</sup>*Ibid.*, para. 8.2. (This finding of the Panel is not appealed)

<sup>11</sup>*Ibid.*, para. 8.4.

<sup>12</sup>WT/DS257/6, 6 October 2003.

<sup>13</sup>WT/DS257/7, 7 October 2003.

Rule 20 of the *Working Procedures*.<sup>14</sup> On that same day, the United States filed its appellant's submission in accordance with the *Working Schedule* drawn up by the Division for this appeal.<sup>15</sup>

7. On 23 October 2003, the European Communities, a third participant in these proceedings, requested the Appellate Body to modify the *Working Schedule*.<sup>16</sup> On 24 October 2003, the Appellate Body declined the European Communities' request, noting that extending the date for the filing of third participants' submissions would significantly reduce the time available for the Division to consider carefully the arguments raised therein as well as the time available to the participants to respond to those arguments.<sup>17</sup> The Division also observed that the new Notice of Appeal filed by the United States on 21 October 2003 was, in all relevant respects, identical to the one submitted on 2 October 2003, and that the critical time-period for third participants and appellees to prepare their responses to arguments raised by appellants and other appellants is the period between the receipt of the appellant's or other appellant's submissions, which contains the appellants' arguments, and the due date for the filing of the third participants' submissions. The Division noted that the time-period between the receipt of the appellant's submission and the due date for third participants' submissions in this case was the same as it would have been, had the Notice of Appeal of 21 October 2003 been filed 10 days before the date of the appellant's submission, as normally occurs.

8. On 27 October 2003, Canada filed an other appellant's submission.<sup>18</sup> On 5 November 2003, Canada and the United States each filed an appellee's submission.<sup>19</sup> On that same day, the European Communities and Japan filed third participants' submissions.<sup>20</sup> On 27 October 2003, pursuant to Rule 24(2) of the *Working Procedures*, India notified the Appellate Body Secretariat that it would not be filing a third participant's submission, but that it intended to make a statement at the oral hearing.

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<sup>14</sup>WT/DS257/8, 24 October 2003.

<sup>15</sup>Pursuant to Rule 21(1) of the *Working Procedures*.

<sup>16</sup>In a letter from the Permanent Delegation of the European Commission dated 23 October 2003, the European Communities argued that the time-period within which it had to file its third participant's submission was contrary to Rule 24(1) of the *Working Procedures* because it was less than 25 days from the date of the re-filing of the Notice of Appeal.

<sup>17</sup>Letter from the Director of the Appellate Body Secretariat dated 24 October 2003.

<sup>18</sup>Pursuant to Rule 23(1) of the *Working Procedures*.

<sup>19</sup>Pursuant to Rule 22(1) and Rule 23(3) of the *Working Procedures*.

<sup>20</sup>Pursuant to Rule 24(1) of the *Working Procedures*.

9. The Appellate Body received two *amicus curiae* briefs during the course of these proceedings. The first, dated 21 October 2003, was received from the Indigenous Network on Economies and Trade (based in Vancouver, British Columbia, Canada).<sup>21</sup> The second, dated 7 November 2003, was a joint brief filed by Defenders of Wildlife (based in Washington, D.C., United States), Natural Resources Defense Council (based in Washington, D.C., United States) and Northwest Ecosystem Alliance (based in Bellingham, state of Washington, United States).<sup>22</sup> These briefs dealt with some questions not addressed in the submissions of the participants or third participants. No participant or third participant adopted the arguments made in these briefs.<sup>23</sup> Ultimately, in this appeal, the Division did not find it necessary to take the two *amicus curiae* briefs into account in rendering its decision.

10. In a letter dated 12 November 2003, the Director of the Appellate Body Secretariat informed the participants and third participants that, in accordance with Rule 13 of the *Working Procedures*, the Appellate Body had selected Mr. Giorgio Sacerdoti to replace Mr. A.V. Ganesan as a Member of the Division hearing this appeal because the latter was prevented from continuing to serve on the Division for serious personal reasons.

11. The oral hearing was held on 20 November 2003. The participants and third participants each presented oral arguments and responded to questions put to them by the Members of the Division hearing the appeal.

## II. Arguments of the Participants and the Third Participants

### A. *Claims of Error by the United States – Appellant*

#### 1. Calculation of Benefit

12. The United States requests the Appellate Body to reverse the Panel's finding that Article 14(d) of the *SCM Agreement* required the United States to determine the adequacy of remuneration for government-provided timber based on any observed non-government prices for timber in Canada, even when such prices are substantially influenced, or even effectively determined, by the government's financial contribution.

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<sup>21</sup>This brief purported to add an indigenous dimension to the issues raised by this appeal.

<sup>22</sup>The organizations filing this brief commented on the environmental implications of the issues raised by this appeal.

<sup>23</sup>Responses to questioning at the oral hearing.

13. The United States argues that the guidelines for the calculation of benefit in Article 14(d) must be interpreted in a manner consistent with the term "benefit" as it is used in Article 1.1(b) of the *SCM Agreement*. The United States refers to the Appellate Body's interpretation of the term "benefit" in Article 1.1(b) in *Canada – Aircraft* and recalls that a government financial contribution confers a benefit if the "'financial contribution' makes the recipient 'better off' than it would otherwise have been absent that contribution", and that the marketplace provides the appropriate basis for comparison.<sup>24</sup> The United States criticizes the Panel's interpretation because it does not permit identification of the trade-distorting potential of a financial contribution. Rather, it requires a circular analysis in which government prices are compared to other prices that simply reflect the government's participation in the market.

14. The United States contends that the term "market conditions" as used in Article 14(d) can only mean "commercial" market conditions that are not determined or substantially influenced by the government's financial contribution. The United States agrees with the Panel that "prevailing" market conditions are market conditions as they exist or which are predominant, but argues that the Panel incorrectly interpreted the phrase "prevailing market conditions" as the "prevailing conditions of sale for the good in question", without inquiring whether the prevailing conditions are "market" conditions.<sup>25</sup> The United States submits that not all prevailing conditions are market conditions within the meaning of Article 14(d). The United States further argues that the designation in the chapeau to Article 14 of the provisions of that article as "guidelines" signifies that they are guides or principles, not rigid rules that purport to contemplate every conceivable circumstance. This interpretation is supported, according to the United States, by the use of the broad phrase "in relation to" before "prevailing market conditions" in the text of Article 14(d).

15. The United States thus takes issue with the Panel's finding that the United States was required to use private timber prices in Canada in assessing the adequacy of remuneration for government stumpage. Although the Panel acknowledged that, if the government were the sole supplier of the goods in question, the conditions prevailing would not be "market conditions", the Panel failed to consider that, in Canada, provincial governments control the vast majority of timber and are therefore the predominant suppliers. According to the United States, the conclusion should have been the same regardless of whether the government was the sole or predominant supplier. The United States accordingly contends that it was appropriate for it to conduct its analysis of the adequacy of remuneration for government stumpage in Canada using proxies other than private Canadian timber prices.

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<sup>24</sup>Appellate Body Report, *Canada – Aircraft*, para. 157.

<sup>25</sup>United States' appellant's submission, para. 20.

2. Pass-Through Analysis

16. The United States requests the Appellate Body to reverse the Panel's finding that, in failing to carry out a pass-through analysis, the United States acted inconsistently with Article 10 of the *SCM Agreement* and Article VI:3 of the GATT 1994, and, consequently, that the United States' imposition of countervailing duties was inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.<sup>26</sup> Although the United States accepts that the *SCM Agreement* requires that countervailing duties not be imposed in an amount exceeding the "subsidy found to exist", it contends that the Panel erred in finding that a pass-through analysis is required in respect of sales of *logs* from tenure-holding sawmills producing softwood lumber to unrelated sawmills, and for sales of *lumber* by tenure-holding sawmills to unrelated lumber remanufacturers. The United States does not appeal the Panel's finding that, where a subsidy is received by an independent timber harvester, a pass-through analysis is required in respect of sales to unrelated sawmills or unrelated remanufacturers.<sup>27</sup>

17. The United States contends that the *SCM Agreement* does not require investigating authorities to determine the "subsidy found to exist" on a company-specific or transaction-specific basis before imposing countervailing duties. Rather, according to the United States, the *SCM Agreement* expressly contemplates that, in an investigation, a Member may adopt an aggregate methodology that may subject individual exporters or producers to countervailing duties without individually investigating whether those exporters or producers actually received a subsidy.

18. With this in mind, the United States argues that a pass-through analysis is required only where the subsidy is bestowed *indirectly*. Thus, if a subsidy is received directly by someone *other than* a producer of the product under investigation, an investigation is required to determine whether some or all of that subsidy is passed through to enterprises that *do* produce the product under investigation. Because USDOC's investigation with respect to softwood lumber from Canada involved subsidies that were granted directly to Canadian producers of softwood lumber and were not received by someone other than a producer of softwood lumber, the United States argues that no pass-through analysis was required. The United States recalls that the product under investigation—softwood lumber—includes both primary lumber and remanufactured lumber. The United States contends that there is no basis in the *SCM Agreement*, or the GATT 1994, for the Panel's finding that "what constitutes the 'product' for which subsidies are being measured depends in part on what happens to the product after it is produced."<sup>28</sup> There is also no basis for the Panel's finding that the

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<sup>26</sup>Panel Report, paras. 7.99 and 8.1(c).

<sup>27</sup>United States appellant's submission, footnote 7 to para. 5.

<sup>28</sup>*Ibid.*, para. 42.

United States was required to reduce the "subsidy found to exist" by the amount of subsidies attributable to certain lumber products sold domestically, unless it could establish that those subsidies passed through to an exported product.

19. The United States argues that the Panel erred in requiring a pass-through analysis to determine what, if any, portion of the total subsidies could be specifically traced to products entering the United States that were produced by companies that purchase logs or lumber from unrelated entities. Article 19.3 of the *SCM Agreement* explicitly recognizes that exporters who are "not actually investigated" may be "subject to" countervailing duties.<sup>29</sup> There is thus no requirement, in an aggregate investigation, to investigate whether individual exporters receive subsidies. Article 19.3 simply requires that expedited reviews be available to enterprises that were not individually investigated. The United States argues that, in finding that a pass-through analysis was required in this case, the Panel expanded the obligation to determine the subsidy granted to production of a product, to include an obligation to determine the subsidy granted to specific producers of that product.

B. *Arguments of Canada – Appellee*

1. Calculation of Benefit

20. Canada requests the Appellate Body to uphold the Panel's finding that the United States' determination of the existence and amount of benefit was inconsistent with Article 14 and Article 14(d) of the *SCM Agreement* and, therefore, that the United States' imposition of countervailing duties on the basis of that determination was inconsistent with Articles 14, 14(d), 10, and 32.1 of the *SCM Agreement*.

21. Canada observes that Article 14(d) requires the adequacy of remuneration to be determined "in relation to the prevailing market conditions ... in the country of provision", and submits that the ordinary meaning of Article 14(d) of the *SCM Agreement* requires Members to use prevailing market conditions in the country of provision as the benchmark against which to determine the adequacy of remuneration. Canada contends that "in the country of provision" can only mean "in the country of provision", and nothing in the context, object and purpose, or negotiating history of Article 14 permits an alternative reading. In particular, according to Canada, the use of the term "in relation to" does not give discretion to Members to reject in-country benchmarks for comparison.

22. Canada also argues that the Panel's interpretation of the phrase "prevailing market conditions" is consistent with the ordinary meaning of these terms as used in Article 14(d). Canada disagrees with

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<sup>29</sup>United States appellant's submission, para. 46. (italics omitted)

the approach taken by the United States, which, it contends, interprets the word "market" in Article 14(d) in isolation from the qualifying term "prevailing" and the phrase "in the country of provision". Canada claims that the United States mischaracterized the Panel's findings as to when in-country prices would not govern the determination of adequate remuneration, and that the Panel was correct in finding that in only two situations it would not be possible to use in-country prices. The first situation is where the government is the only supplier of the relevant goods, and the second situation is where the government administratively controls all the prices for those goods. The Panel found that the facts before it did not fall within either one of these situations. Canada asserts, moreover, that the United States' attempt to equate the government's position as a dominant supplier of goods with formal government price-setting is untenable because it would permit investigating authorities to avoid the in-country comparisons required by Article 14(d).

23. In addition, Canada submits that the Panel's interpretation of Article 14(d) is entirely consistent with WTO jurisprudence relating to the term "benefit" in Article 1.1(b) of the *SCM Agreement*. The Panel did not dismiss the Appellate Body's statements in *Canada – Aircraft* as irrelevant to the interpretation of Article 14(d). Rather, the Panel concluded, consistent with that Appellate Body decision, that the marketplace provided the appropriate basis in which to compare transactions. Canada distinguishes the report of the panel in *Brazil – Aircraft (Article 21.5 – Canada II)*, which dealt with a different type of financial contribution.

24. Canada asserts that the Panel's interpretation of Article 14(d) is supported by the context of that provision. In particular, Canada submits that, even though the chapeau of Article 14 refers to the paragraphs that follow as "guidelines", it is clear from the use of the mandatory term "shall" that the calculation of benefit by an investigating authority must be consistent with those provisions. As a result, the "guidelines" cannot be referred to as "general principles" because they *mandate* the type of evidence that must be employed to determine and measure any benefit conferred. Similar contextual support is provided by paragraphs (b) and (c) of Article 14, which do not mention the country of provision or the territory of the Member. According to Canada, this indicates that, if the drafters of Article 14 had intended to allow reference to be made to the countries other than the country of provision, they would have done so explicitly.

25. Finally, Canada argues that the Panel's interpretation is supported by economic logic. It points out that there are inherent economic problems with cross-border comparisons, as well as a broad range of other considerations that also affect the comparability of forestry resources.

2. Pass-Through Analysis

26. Canada requests that the Appellate Body uphold the Panel's interpretation that Article 10 of the *SCM Agreement* and Article VI:3 of the GATT 1994 required USDOC to conduct a pass-through analysis in its countervailing duty investigation of softwood lumber from Canada.

27. Canada contends that, by not appealing the Panel's finding that a pass-through analysis is required where subsidies are received by independent harvesters of timber, the United States has accepted that a pass-through analysis is required in instances of alleged *indirect* subsidization. According to Canada, the United States thus concedes that when a Member wishes to impose countervailing duties on the products of producer A, that Member must demonstrate that a subsidy bestowed upon producer B is passed through producer B's arm's-length sale of an input to producer A. For Canada, this is an acceptance of the fundamental principle reflected in the *SCM Agreement*, and of the GATT 1994, that a Member may not presume the existence of a subsidy.

28. Canada submits that the requirement for a pass-through analysis applies equally to arm's-length sales of log inputs between sawmills, and to arm's-length purchases of lumber inputs from sawmills by lumber remanufacturers. In Canada's view, the fact that the United States chose to undertake its countervailing duty investigation on an aggregate, country-wide basis does not exempt the United States from the requirement to make such a pass-through determination. Canada argues that Article 19.3 of the *SCM Agreement*, which the United States invokes, does not permit a Member to simply presume subsidization. According to Canada, in order to impose countervailing duties on a product, a Member must first determine that there is a subsidy to a recipient, in the sense of Article 1.1 of the *SCM Agreement*, which relates to the manufacture, production or export of that product. The United States' decision to conduct its investigation on an aggregate basis cannot absolve it of the fundamental requirement to establish the existence of a subsidy in respect of the products of sawmills and lumber remanufacturers who purchase their log or lumber inputs at arm's length. According to Canada, the Panel's findings follow consistent GATT and WTO jurisprudence on impermissible presumptions of subsidization, including the findings of the panel in *US – Softwood Lumber III*.

29. In Canada's view, the United States' arguments to the contrary impermissibly reduce to inutility the obligation in Article 10 of the *SCM Agreement* to "take all necessary steps" to determine subsidization in accordance with Article VI of the GATT 1994 and the *SCM Agreement*. Canada argues that any presumption of subsidization, especially in the face of evidence establishing no subsidy, fails to ensure that countervailing measures offset actual subsidization. Canada contends, further, that the United States' arguments reverse the burden of proving subsidization from the



investigating authority to the producers on whose products a countervailing duty is imposed. Canada dismisses as unsatisfactory the United States' argument that affected companies may request a *post facto* expedited review at which they may seek to "disprove Commerce's presumed pass-through of the alleged subsidy".<sup>30</sup>

C. *Claims of Error by Canada – Appellant*

1. Financial Contribution

30. Canada asks the Appellate Body to reverse the Panel's finding with respect to the existence of a "financial contribution". Canada contends that the Panel made several errors of law in developing legal interpretations related to what constitutes a "financial contribution" within the meaning of Article 1.1(a) of the *SCM Agreement*.

31. First, the Panel erred in interpreting the word "goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement*. Canada argues that the Panel misinterpreted the text of Article 1.1(a)(1)(iii), in its context, in finding that the word "goods" referred to tangible or movable personal property other than money. Although Canada agrees that the Panel's definition reflects the ordinary meaning of the term, Canada argues that, in the context of Article 1.1(a)(1)(iii) of the *SCM Agreement*, the term "goods" is limited to "tradable items with an actual or potential tariff classification".<sup>31</sup> In support of this view, Canada observes that Article 3.1(b) of the *SCM Agreement* refers to measures that favour "domestic over imported goods", and argues that the term "imported" in this context means that goods must be tradable. Canada reasons that this means the "goods" referred to in Article 1.1(a)(1)(iii) must also be tradable. In addition, Canada observes that the terms "goods" and "products" are synonymous and are used at various points in the Multilateral Agreements on Trade in Goods (Annex 1A of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*")) to refer to items that are traded or imported or exported. It follows, for Canada, that all "goods" and "products" must be tradable and must be capable of bearing a tariff classification. Further, even if it is accepted that the term "goods" encompasses tangible or movable personal property other than money, Canada argues that the Panel erred in its legal characterization of the facts before it. According to Canada, the Panel found that unidentified trees, with roots firmly in the ground, constitute tangible or movable personal property. Canada submits that the Panel erred because standing timber is not personal property.

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<sup>30</sup>Canada's appellee's submission, para. 79.

<sup>31</sup>Canada's other appellant's submission, para. 25.

32. Finally, Canada contends that the Panel erred in finding that Canadian provincial governments "provide" standing timber through stumpage programmes. In Canada's view, the Panel erred in giving the word "provides" the broad interpretation "to make available". This was inappropriate, according to Canada, because, throughout the *WTO Agreement*, the meaning of the term "provides" is limited to "supplying" or "giving". Canada argues that the only thing provided by provincial governments under stumpage programmes is an intangible right to harvest. This right to harvest cannot be equated with providing standing trees, without effectively making the intangible right of exploitation "goods".

33. Canada requests the Appellate Body, should it reverse the findings of the Panel with respect to the existence of a financial contribution, to recommend that the DSB request the United States to bring its measures into conformity with the *SCM Agreement*, *inter alia*, by revoking the countervailing duties on softwood lumber and refunding deposits paid.

D. *Arguments of the United States – Appellee*

1. Financial Contribution

34. The United States argues that, by finding that standing timber constitutes "goods" within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*, the Panel interpreted the term "goods" consistently with its ordinary meaning and context, and in the light of the object and purpose of the *SCM Agreement*. The United States agrees with the Panel that the ordinary meaning of the term "goods" includes things to be severed from real property, such as standing timber. Nothing in the language or context of the term "goods" in Article 1.1(a)(1)(iii) suggests any limitation of the term to tradable products. Nor does the object and purpose of the *SCM Agreement* support Canada's position. In particular, the United States argues that the use of the term "imported goods" in Article 3.1(b) of the *SCM Agreement*, and similar terminology in other agreements, cannot be read to imply that the term "goods" in Article 1.1(a)(1)(iii) can only mean goods capable of being imported or traded. The United States points to the lack of a qualifier such as "imported" in Article 1.1(a)(1)(iii). In addition, the United States argues that Canada's interpretation of "goods" would render superfluous the explicit exception in Article 1.1(a)(1)(iii) for "general infrastructure", because that provision could never encompass any infrastructure if "goods" were interpreted in such a narrow manner. If that were the case, then there would be no need for the explicit exception. The United States also contends that Canada's argument regarding whether standing timber is "personal property" is inapposite. According to the United States, the Panel rightly did not attempt to interpret property laws, nor was it required to do so in considering whether standing timber was goods within the meaning of Article 1.1(a)(1)(iii).

35. The United States further argues that, by finding that the provincial governments provided standing timber to Canadian tenure holders, the Panel interpreted the term "provides" in Article 1.1(a)(1)(iii) of the *SCM Agreement* consistently with its ordinary meaning and context and in the light of the object and purpose of the *SCM Agreement*. According to the United States, Canada elevates form over substance by arguing that the only thing provided by the provincial governments is an intangible right to harvest, and that the granting of such a right is not the provision of goods. Noting that the definition of "provide" includes to "make available" and to "supply or furnish for use", the United States contends that it is beyond dispute that when a government transfers ownership of goods by giving a company the right to take them, the government is providing those goods within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*.

36. Finally, the United States argues that, in the event the Appellate Body finds that the United States has not acted in conformity with its obligations under the *SCM Agreement* or the GATT 1994, the Appellate Body should refrain from making any recommendation regarding the specific manner in which such findings should be implemented.

E. *Arguments of the Third Participants*

1. European Communities

(a) Financial Contribution

37. The European Communities disagrees with Canada that the term "goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement* should be limited to "tradable items with an actual or potential tariff classification". The European Communities argues that the ordinary meaning of the word "goods" includes many forms of property, and is not limited to movable property. It finds support for the view that the term "goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement* encompasses immovable property in the French and Spanish versions of the *SCM Agreement*. This understanding is further corroborated by the immediate context of the term "goods" in Article 1.1(a)(1)(iii), which refers to the provision of goods or services "other than general infrastructure". Only where such goods are "general" infrastructure are they excluded from the coverage of that provision. The European Communities also points to the object and purpose of the *SCM Agreement* and argues that the broad phrase "goods and services other than general infrastructure" is intended to cover any in-kind transfer of resources. The European Communities notes that subsidies may take the form of complex bundles of rights involving, for example, rights to movable or immovable goods, services or intellectual property. According to the European Communities, if such complex economic transactions were not covered by the disciplines of the *SCM Agreement*, there would be considerable room for circumvention.

(b) Calculation of Benefit

38. The European Communities agrees with the Panel that Article 14(d) of the *SCM Agreement* obliges WTO Members to use market prices in the country of provision to determine whether government-provided goods confer a benefit. The term "prevailing" clarifies that the benchmark is not a hypothetical market free from any government intervention, but, instead, it is the existing market, even if it is affected by the government's presence in the market. Therefore, private prices in the country of provision may not be disregarded as a benchmark based only on the government's presence in the market.

39. The European Communities asserts that, in exceptional situations where all domestic prices are effectively determined by the government or the government is the only suitable supplier available, there would be no market conditions within the meaning of Article 14(d). In such situations, other benchmarks would need to be used, as the Panel itself acknowledged. The decision as to whether market conditions exist must be made on a case-by-case basis. In this case, however, USDOC was not entitled to use cross-border prices instead of Canadian market prices on the basis of a mere assertion—without further explanation—that private Canadian prices are driven by prices of government-provided timber.

(c) Pass-through Analysis

40. The European Communities agrees with the general principle that investigating authorities must make a determination of subsidization in respect of a product and cannot simply assume subsidization where subsidies were bestowed on a product other than the one subject to a countervailing duty investigation, and where the input producers were unrelated to the producers of the subject merchandise. However, the European Communities disagrees with the Panel's application of this general principle to the specific case of an aggregate investigation. According to the European Communities, the Panel's reasoning fails to preserve fully the right of WTO Members to conduct aggregate investigations. The European Communities agrees with the United States that the *SCM Agreement* does not oblige investigating authorities to make a company-specific assessment by investigating and determining, in each case, what portion of the subsidies to the production of softwood lumber in Canada was received by specific producers of those products, before imposing the countervailing duty. The European Communities contrasts the first sentence of Article 6.10 of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "Anti-Dumping Agreement"), which explicitly requires a determination of an individual margin for exporters of the dumped goods unless special situations occur which render individual examination impractical, with the *SCM Agreement*, which does not require WTO Members to determine an

individual margin of subsidization for exporters of the subsidized goods. The European Communities finds further support for the ability of Members to conduct aggregate investigations in Article 19.3 of the *SCM Agreement*.

41. For the European Communities, investigating authorities have a broad margin of discretion in establishing the existence of subsidization, including the ability to select the appropriate methodology for each case. Investigating authorities must be able to make a determination that is not based on a company-specific investigation and determination. The European Communities notes, however, that where the available facts reveal the existence of different categories of producers who have received different amounts of subsidization, such categories should be taken into account in any methodology chosen.

2. India

42. Pursuant to Rule 24 of the *Working Procedures*, India chose not to submit a third participant's submission. In its statement at the oral hearing, India addressed the issue of calculation of benefit and contested the admissibility of unsolicited *amicus curiae* briefs in WTO dispute settlement proceedings.

3. Japan

(a) Financial Contribution

43. Japan submits that the Panel's finding that "goods" in Article 1.1(a)(1)(iii) encompasses "tangible or movable personal property other than money" provides useful guidance on the interpretation of the meaning of "subsidy" in the *SCM Agreement*. For Japan, the concepts of "goods" and "services" in Article 1.1(a)(1)(iii) have broad meanings paralleling monetary transfers. In the light of the fact that, in the context of providing the financial contribution described in Article 1.1(a)(1)(iii), "goods" are provided by governments to domestic producers, Japan disagrees with Canada that "goods" should be limited to tradable items with an actual or potential tariff classification.

(b) Calculation of Benefit

44. Japan submits that the Panel correctly relied on a textual interpretation of Article 14(d) of the *SCM Agreement* in finding that the prevailing market conditions to be used as a benchmark are those in the country of the provision of goods. Thus, according to Japan, the United States has the burden of proving that, despite this explicit requirement of an in-country analysis, a cross-border analysis is also permissible. Japan asserts that, even if a cross-border analysis were deemed permissible in certain exceptional situations, the United States has not demonstrated that a cross-border analysis is appropriate in this case. In particular, the United States failed to show that no market prices existed for stumpage in Canada, or that it was not possible to construct a proxy for, or estimate of, the market price in Canada. Therefore, Japan asserts that it is not clear why a comparison with the United States domestic market was the only option available for the United States to conduct a benefit analysis under Article 14(d) of the *SCM Agreement*.

**III. Issues Raised in This Appeal**

45. This appeal raises the following issues:

- (a) whether the Panel erred, in paragraph 7.30 of the Panel Report, in finding that Canadian provincial stumpage programs "provide goods", in the sense of Article 1.1(a)(1)(iii) of the *SCM Agreement*, thereby making a financial contribution in accordance with that provision;
- (b) whether the Panel erred, in paragraphs 7.64 and 7.65 of the Panel Report, in finding that USDOC failed to determine benefit in a manner consistent with Articles 14 and 14(d) of the *SCM Agreement* by not using as a benchmark prices of private stumpage in Canada, and that, therefore, USDOC's imposition of countervailing measures was inconsistent with the United States' obligations under Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement*; and
- (c) whether the Panel erred, in paragraph 7.99 of the Panel Report, in finding that USDOC's failure to conduct a "pass-through" analysis in respect of arm's length sales of *logs* and *lumber* by tenure-holding timber harvesters owning sawmills and producing lumber, to unrelated sawmills or lumber remanufacturers, is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.

#### IV. Financial Contribution

##### A. Introduction

46. We first consider Canada's appeal regarding the existence of a financial contribution within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*. In its final determination, USDOC found that Canadian provincial governments made a financial contribution because, through stumpage arrangements, those governments *provide goods* to timber harvesters.

47. The Panel found that:

... the USDOC Determination that the Canadian provinces are providing a financial contribution in the form of the provision of a good by providing standing timber to the timber harvesters through the stumpage programmes is not inconsistent with Article 1.1 (a) (1) (iii) [of the] *SCM Agreement*.<sup>32</sup>

On this basis, the Panel rejected all of the claims of violation raised by Canada in respect of the *SCM Agreement* and the GATT 1994 that flowed from Canada's allegation that stumpage programs do not constitute financial contributions.<sup>33</sup>

48. Canada requests us to *reverse* this finding on the ground that the Panel erred in its interpretation of Article 1.1(a)(1)(iii) of the *SCM Agreement* or, alternatively, that it erred in the legal characterization of the facts before it. Canada argues that standing timber, that is, trees attached to the land and therefore incapable of being traded as such, are not "goods" in the sense of Article 1.1(a)(1)(iii). It further contends that the Panel erred in finding that the provincial governments "provide" standing timber through stumpage arrangements.

49. The United States requests us to *uphold* the Panel's finding. The United States contends that the meaning of the term "goods" in Article 1.1(a)(1)(iii) encompasses things severable from land, such as standing timber. It also argues that the Panel was right in finding that standing timber is "provided" to harvesters through the conferral of a right to harvest it.

##### B. General Interpretation of the Requirements of Article 1.1(a)(1)(iii) of the *SCM Agreement*

50. We begin our analysis of this issue with the text of the relevant provision. Article 1 sets out a definition of "subsidy" for the purposes of the *SCM Agreement*. It reads as follows:

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<sup>32</sup>Panel Report, para. 7.30.

<sup>33</sup>*Ibid.*

*Definition of a Subsidy*

1.1 *For the purpose of this Agreement, a subsidy shall be deemed to exist if:*

(a)(1) *there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:*

- (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);
- (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);
- (iii) a government provides goods or services other than general infrastructure, or purchases goods;
- (iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments;

or

(a)(2) there is any form of income or price support in the sense of Article XVI of GATT 1994;

and

(b) a benefit is thereby conferred. (emphasis added, footnote omitted)

51. The concept of subsidy defined in Article 1 of the *SCM Agreement* captures situations in which something of economic value is transferred by a government to the advantage of a recipient. A subsidy is deemed to exist where two distinct elements are present.<sup>34</sup> First, there must be a financial contribution by a government, or income or price support. Secondly, any financial contribution, or income or price support, must confer a benefit. Canada's appeal focuses on the Panel's finding with respect to the first element, namely the existence of a financial contribution.

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<sup>34</sup>Appellate Body Report, *Brazil – Aircraft*, para. 157.



52. An evaluation of the existence of a financial contribution involves consideration of the nature of the transaction through which something of economic value is transferred by a government. A wide range of transactions falls within the meaning of "financial contribution" in Article 1.1(a)(1). According to paragraphs (i) and (ii) of Article 1.1(a)(1), a financial contribution may be made through a direct transfer of funds by a government, or the foregoing of government revenue that is otherwise due. Paragraph (iii) of Article 1.1(a)(1) recognizes that, in addition to such monetary contributions, a contribution having financial value can also be made *in kind* through governments providing goods or services, or through government purchases. Paragraph (iv) of Article 1.1(a)(1) recognizes that paragraphs (i) – (iii) could be circumvented by a government making payments to a funding mechanism or through entrusting or directing a private body to make a financial contribution. It accordingly specifies that these kinds of actions are financial contributions as well. This range of government measures capable of providing subsidies is broadened still further by the concept of "income or price support" in paragraph (2) of Article 1.1(a).<sup>35</sup>

53. Article 1.1(a)(1)(iii) of the *SCM Agreement*, the specific provision at issue in Canada's appeal, sets forth that a financial contribution exists where a government "provides goods or services other than general infrastructure, or purchases goods". As such, the Article contemplates two distinct types of transaction. The first is where a government provides goods or services other than general infrastructure. Such transactions have the potential to lower artificially the cost of producing a product by providing, to an enterprise, inputs having a financial value. The second type of transaction falling within Article 1.1(a)(1)(iii) is where a government purchases goods from an enterprise. This type of transaction has the potential to increase artificially the revenues gained from selling the product.

54. Canada's appeal requires us to focus upon one element of the first type of transaction contemplated by Article 1.1(a)(1)(iii), namely, whether, through stumpage programs, provincial governments *provide goods*. Canada takes issue with the Panel's interpretation of each of the two words in this expression. With respect to the meaning of the term "goods" in Article 1.1(a)(1)(iii) of

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<sup>35</sup>We note, however, that not all government measures capable of conferring benefits would necessarily fall within Article 1.1(a). If that were the case, there would be no need for Article 1.1(a), because all government measures conferring benefits, *per se*, would be subsidies. In this regard, we find informative the discussion of the negotiating history of the *SCM Agreement* contained in the panel report in *US – Export Restraints*, which was not appealed. That panel, at paragraph 8.65 of the panel report, said that the:

... negotiating history demonstrates ... that the requirement of a financial contribution from the outset was intended by its proponents precisely to ensure that not all government measures that conferred benefits could be deemed to be subsidies. This point was extensively discussed during the negotiations, with many participants consistently maintaining that only government actions constituting financial contributions should be subject to the multilateral rules on subsidies and countervailing measures. (footnote omitted)

the *SCM Agreement*, Canada submits that the Panel erred in finding that "standing timber" falls within the meaning of that term. Canada advances two arguments in support of this aspect of its appeal. First, it argues that, in the context of Article 1.1(a)(1)(iii) of the *SCM Agreement*, the term "goods" is limited to "tradable items with an actual or potential tariff classification."<sup>36</sup> Secondly, even if we were to find that the Panel's interpretation of the term "goods" is correct, Canada argues that the Panel erred in its legal characterization of the facts before it, because standing timber does not fall within the definition proposed by the Panel, which defines goods, *inter alia*, by reference to the concept of "personal property".<sup>37</sup>

55. Canada further argues that the Panel erred in its interpretation of the term "provides".<sup>38</sup> In particular, Canada submits that the Panel incorrectly found that standing timber was "provided" to harvesters merely by virtue of the conferral, through stumpage arrangements, of an intangible right to harvest.<sup>39</sup>

56. Before we consider each of the separate elements of Canada's appeal, we observe that the arguments put forward by Canada relating to the nature of "personal property", raise issues concerning the relevance, for WTO dispute settlement, of the way in which the municipal law of a WTO Member classifies or regulates things or transactions. Previous Appellate Body Reports confirm that an examination of municipal law or particular transactions governed by it might be relevant, as evidence, in ascertaining whether a financial contribution exists.<sup>40</sup> However, municipal laws—in particular those relating to property—vary amongst WTO Members. Clearly, it would be inappropriate to characterize, for purposes of applying any provisions of the WTO covered agreements, the same thing or transaction differently, depending on its legal categorization within the jurisdictions of different Members. Accordingly, we emphasize that municipal law classifications are not determinative of the issues raised in this appeal.

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<sup>36</sup>Canada's other appellant's submission, para. 25.

<sup>37</sup>*Ibid.*, para. 43 *ff.*, referring to para. 7.24 of the Panel Report.

<sup>38</sup>*Ibid.*, para. 52 *ff.*

<sup>39</sup>*Ibid.*, para. 56.

<sup>40</sup>In *US – FSC*, for example, a consideration of the meaning of United States tax law was required to determine whether the taxation measure at issue in those proceedings represented the foregoing of "revenue that is otherwise due", as contemplated by Article 1.1(a)(1)(ii) of the *SCM Agreement*. (Appellate Body Report, *US – FSC*, para. 90) We recall as well that, in *India – Patents (US)*, the Appellate Body observed that panels must often complete a detailed examination of the relevant aspects of a Member's domestic law to determine whether a situation regulated by the covered agreements exists. (Appellate Body Report, *India – Patents (US)*, paras. 65–71) See also Appellate Body Report, *US – Section 211 Appropriations Act*, paras. 103–106.

C. *Do Provincial Stumpage Programs "Provide Goods" in the Sense of Article 1.1(a)(1)(iii) of the SCM Agreement?*

57. With this in mind, we turn to Canada's argument that standing timber does not fall within the meaning of the term "goods" in the phrase "provides goods or services other than general infrastructure". At the outset, we note that there is no dispute that trees are goods once they are harvested.<sup>41</sup> The question raised by Canada's appeal is, rather, whether the term "goods" in Article 1.1(a)(1)(iii) captures trees *before they are harvested*, that is, standing timber attached to the land (but severable from it) and incapable of being traded across borders as such.

58. The meaning of a treaty provision, properly construed, is rooted in the ordinary meaning of the terms used.<sup>42</sup> The Panel adopted a definition of the term "goods", drawn from *Black's Law Dictionary*, put forward in the submissions of both Canada and the United States, that the term "goods" includes "tangible or movable personal property other than money".<sup>43</sup> In particular, the Panel noted that this definition set out in *Black's Law Dictionary* contemplates that the term "goods" could include "growing crops, and other identified things to be severed from real property".<sup>44</sup> We observe that the *Shorter Oxford English Dictionary* offers a more general definition of the term "goods" as including "property or possessions" especially—but not exclusively—"movable property".<sup>45</sup>

59. These definitions offer a useful starting point for discerning the ordinary meaning of the word "goods". In particular, we agree with the Panel that the ordinary meaning of the term "goods", as used in Article 1.1(a)(1)(iii), includes items that are tangible and capable of being possessed. We note, however, as we have done on previous occasions, that dictionary definitions have their limitations in revealing the ordinary meaning of a term.<sup>46</sup> This is especially true where the meanings of terms used

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<sup>41</sup>See, for example, Canada's other appellant's submission, paras. 46 and 58.

<sup>42</sup>Article 31(1) of the *Vienna Convention on the Law of Treaties* (the "Vienna Convention") provides: "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose". (Done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679)

<sup>43</sup>Panel Report, paras. 7.23–7.24, citing *Black's Law Dictionary*, 7th ed., B.A. Garner (ed.) (West Group, 1999), pp. 701–702. The Panel also noted that *The New Shorter Oxford Dictionary* defines "goods" as "saleable commodities, merchandise, wares". (*The New Shorter Oxford Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. I, p. 1116)

<sup>44</sup>Panel Report, para. 7.23.

<sup>45</sup>*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. I, p. 1125.

<sup>46</sup>Appellate Body Report, *Canada – Aircraft*, para. 153. See also, Appellate Body Report, *EC – Asbestos*, para. 92.

in the different authentic texts of the *WTO Agreement* are susceptible to differences in scope. We note that the European Communities, in its third participant's submission, observed that in the French version of the *SCM Agreement*, Article 1.1(a)(1)(iii) addresses, *inter alia*, the provision of "*biens*".<sup>47</sup> In the Spanish version, the term used is "*bienes*".<sup>48</sup> The ordinary meanings of these terms include a wide range of property, including immovable property. As such, they correspond more closely to a broad definition of "goods" that includes "property or possessions" generally, than with the more limited definition adopted by the Panel. As we have observed previously, in accordance with the customary rule of treaty interpretation reflected in Article 33(3) of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*"), the terms of a treaty authenticated in more than one language—like the *WTO Agreement*—are presumed to have the same meaning in each authentic text.<sup>49</sup> It follows that the treaty interpreter should seek the meaning that gives effect, simultaneously, to all the terms of the treaty, as they are used in each authentic language.<sup>50</sup> With this in mind, we find that the ordinary meaning of the term "goods" in the English version of Article 1.1(a)(1)(iii) of the *SCM Agreement* should not be read so as to exclude tangible items of property, like trees, that are severable from land.

60. We find that terms that accompany the word "goods" in Article 1.1(a)(1)(iii) support this interpretation. In Article 1.1(a)(1)(iii), the only explicit exception to the general principle that the provision of "goods" by a government will result in a financial contribution is when those goods are provided in the form of "general infrastructure". In the context of Article 1.1(a)(1)(iii), all goods that might be used by an enterprise to its benefit—including even goods that might be considered

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<sup>47</sup>European Communities' third participant's submission, para. 7. The term "*biens*" includes "*chose matérielle susceptible d'appropriation, et tout droit faisant partie du patrimoine*" and can mean "*acquêt, ... capital, cheptel, domaine, fortune, ... fruit, héritage, patrimoine, possession, produit, propriété, récolte, richesse*". (*Le Nouveau Petit Robert*, P. Robert (ed.) (Dictionnaires le Robert, 2003), p. 252)

<sup>48</sup>According to the *Diccionario de la Lengua Española*, the term "*bienes*" encompasses both "*bienes muebles*" and "*bienes inmuebles*". (*Diccionario de la Lengua Española*, (22nd ed.) (Real Academia Española, 2001), p. 213)

<sup>49</sup>Article 33(3) of the *Vienna Convention*, *supra*, footnote 42, provides: "[t]he terms of the treaty are presumed to have the same meaning in each authentic text."

<sup>50</sup>See Appellate Body Report, *EC – Bed Linen (Article 2.15 – India)*, footnote 153 to para. 123. We also note that, in discussing the draft article that was later adopted as Article 33(3) of the *Vienna Convention*, the International Law Commission observed that the "presumption [that the terms of a treaty are intended to have the same meaning in each authentic text] requires that every effort should be made to find a common meaning for the texts before preferring one to another". (*Yearbook of the International Law Commission* (1966), Vol. II, p. 225) With regard to the application of customary rules of interpretation in respect of treaties authenticated in more than one language, see also International Court of Justice, Merits, *Case Concerning Elettronica Sicula S.p.A. (ELSI) (United States v. Italy)* 1989, ICJ Reports, para. 132, where, in interpreting a provision of the Treaty of Friendship, Commerce and Navigation between the United States of America and the Italian Republic of 1948, the International Court of Justice noted that it was possible to interpret the English and Italian versions "as meaning much the same thing", despite a potential divergence in scope.

*infrastructure*—are to be considered "goods" within the meaning of the provision, unless they are infrastructure of a *general* nature.

61. Canada puts two arguments in support of its contention that the context of Article 1.1(a)(1)(iii) requires that—notwithstanding its ordinary meaning—the term "goods" must be read as limited to "tradable items with an actual or potential tariff classification". First, Canada observes that Article 3.1(b) of the *SCM Agreement* deals with "subsidies contingent ... upon the use of domestic over imported goods". Because the reference to "imported goods" necessarily refers to tradable (and indeed traded) goods, Canada reasons that all goods must be tradable and capable of bearing a tariff classification.<sup>51</sup> Secondly, in a similar vein, Canada submits that "goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement* has the same meaning as the term "products" in Part V of the *SCM Agreement* and elsewhere in the covered agreements. Canada observes that Part V of the *SCM Agreement* represents an elaboration of Article VI of the GATT 1994, which itself is an exception to Article II of the GATT 1994. For Canada, this means that the scope of Part V of the *SCM Agreement* and Article II of the GATT must be the same.<sup>52</sup> Canada seems to imply that, because Article II of the GATT deals with the binding of tariffs in respect of particular "products", such "products"—and therefore "goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement*—must inherently be susceptible to tariff classification. Canada raises a similar argument with respect to other rules that either regulate "trade in goods" generally<sup>53</sup>; that address "imported or exported goods"<sup>54</sup>; or, that simply deal with "goods" in the context of trade.<sup>55</sup> Canada claims that these provisions also imply that all goods must be tradable.<sup>56</sup>

62. Canada's arguments in this regard are not convincing. Article 3.1(b) of the *SCM Agreement* addresses a certain situation in which subsidies favour domestic goods over "imported goods". In that provision, the word "goods" is qualified by the word "imported". In Article 1.1(a)(1)(iii), the word "goods" is not so qualified. The use of the word "goods" in Article 3.1(b), therefore, gives little contextual guidance to the meaning of the term "goods" in Article 1.1(a)(1)(iii). Contrary to Canada's argument, it does not preclude that there may be "goods" in the sense of Article 1.1(a)(1)(iii) that are not actually "imported" or traded.

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<sup>51</sup>Canada's other appellant's submission, paras. 30–32.

<sup>52</sup>*Ibid.*, paras. 33–34.

<sup>53</sup>Canada points to the rule of conflict set out in the *General Interpretative Note to Annex 1A* and to Articles 1 and 2 of the *Agreement on Trade-Related Investment Measures*. (*Ibid.*, paras. 35–36)

<sup>54</sup>Canada cites generally the *Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994*. (Canada's other appellant's submission, para. 37)

<sup>55</sup>Canada observes that the *Agreement on Rules of Origin* refers to goods in the context of Articles I, II, III, XI and XIII of the GATT 1994. (Canada's other appellant's submission, para. 38)

<sup>56</sup>Canada's other appellant's submission, para. 39.

63. For the same reason, we are of the view that the fact that certain agreements falling within the Multilateral Agreements on Trade in Goods (Annex 1A of the *WTO Agreement*) regulate "trade in goods" and deal with "imported" or "exported" goods, does not control the meaning of the term "goods" as used in Article 1.1(a)(1)(iii) of the *SCM Agreement*. Similarly, we disagree with Canada's argument relating to the term "products" in Article II of the GATT 1994. We do not see why a provision that governs an aspect of commerce between WTO Members and contemplates the binding of tariffs in respect of certain "products", requires that the "goods" referred to in Article 1.1(a)(1)(iii) must also be capable of having tariff classifications. "Goods" in Article 1.1(a)(1)(iii) of the *SCM Agreement* and "products" in Article II of the GATT 1994 are different words that need not necessarily bear the same meanings in the different contexts in which they are used.

64. Moreover, to accept Canada's interpretation of the term "goods" would, in our view, undermine the object and purpose of the *SCM Agreement*, which is to strengthen and improve GATT disciplines relating to the use of both subsidies and countervailing measures, while, recognizing at the same time, the right of Members to impose such measures under certain conditions.<sup>57</sup> It is in furtherance of this object and purpose that Article 1.1(a)(1)(iii) recognizes that subsidies may be conferred, not only through monetary transfers, but also by the provision of non-monetary inputs. Thus, to interpret the term "goods" in Article 1.1(a)(1)(iii) narrowly, as Canada would have us do, would permit the circumvention of subsidy disciplines in cases of financial contributions granted in a form other than money, such as through the provision of standing timber for the sole purpose of severing it from land and processing it.

65. In seeking to exclude "standing timber" from the definition of "goods" in Article 1.1(a)(1)(iii), Canada contends in the alternative that, even if we find that the term is not limited to "tradable items with an actual or potential tariff classification", standing timber is still not "goods" as the Panel has defined them, because it is neither "personal property" nor an "identified thing to be severed from real property". The concepts of "personal" and "real" property are, in the context Canada raises them, creatures of municipal law that are not reflected in Article 1.1(a)(1)(iii) itself. As we have said above, the manner in which the municipal law of a WTO Member classifies an item cannot, in itself, be determinative of the interpretation of provisions of the WTO covered agreements.<sup>58</sup> As such, we do not believe that the distinction drawn by Canada is dispositive of the issues raised in this appeal.

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<sup>57</sup>Appellate Body Report, *US – Carbon Steel*, paras. 73–74.

<sup>58</sup>See *supra*, para. 56. See also Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, footnote 87 to para. 87.

66. Similarly, we reject Canada's argument that specific trees are not "identified" in stumpage contracts and therefore cannot fall within the scope of "goods" within the meaning of the dictionary definition relied upon by the Panel. We disagree that trees must be specifically and individually "identified" in order to constitute "goods" for purposes of Article 1.1(a)(1)(iii) of the *SCM Agreement*. As the Panel found, stumpage contracts concern a specified area of land containing a predictable quantity of timber that may be harvested under certain conditions.<sup>59</sup> Harvesters pay a volumetric "stumpage fee" only for that volume of timber actually harvested.<sup>60</sup> In these circumstances, we do not see the relevance, for an assessment of whether trees are goods, of the fact that each individual tree within the specified area of land covered by a stumpage contract may not be identified at the time the contract is made. Indeed, the identification of trees by reference to a general area of forest renders the situation of the timber growing in that area similar to that of *fungible goods*. Fungible goods are goods even though they are identifiable only by number, volume, value or weight. We see no reason why disciplines on subsidies that regulate the provision of non-monetary resources should focus on identifiable physical objects and not on tangible, but fungible, input material. We note that, in *Canada – Dairy*, the Appellate Body reasoned that "the provision of *milk* at discounted prices to processors for export ... constitutes 'payments', in a form other than money, within the meaning of Article 9.1(c) [of the *Agreement on Agriculture*]" .<sup>61</sup> We see no reason to treat differently the *standing timber* subject to stumpage arrangements, for purposes of determining what constitutes a financial contribution through the provision of goods within the definition of subsidy in Article 1 of the *SCM Agreement*.

67. In sum, nothing in the text of Article 1.1(a)(1)(iii), its context, or the object and purpose of the *SCM Agreement*, leads us to the view that tangible items—such as standing, unfelled trees—that are not both tradable as such and subject to tariff classification, should be excluded, as Canada suggests, from the coverage of the term "goods" as it appears in that Article. It follows that we agree with the Panel that standing timber—trees—are "goods" within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*.

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<sup>59</sup>Panel Report, para. 7.18. The Panel said that it did:

... not consider relevant the distinction that Canada makes between a contract which identifies individual trees to be cut, and an agreement concerning harvesting rights over a certain area of forest land. In our view, in both cases, trees are provided. In any case, it appears to us that, although a tenure agreement may not provide for a precise number of identified trees to be cut, the tenure holder knows all too well how many trees and which species of trees can be found on the area of land covered by his tenure. (footnote omitted)

<sup>60</sup>*Ibid.*, para. 7.16.

<sup>61</sup>Appellate Body Report, *Canada – Dairy*, para. 113. (emphasis added)

68. Having considered the meaning of the term "goods", we now turn to consider what it means to "provide" goods, for purposes of Article 1.1(a)(1)(iii) of the *SCM Agreement*. Canada argues that stumpage arrangements do not "provide" standing timber. According to Canada, all that is provided by these arrangements is an intangible right to harvest. At best, this intangible right "makes available" standing timber. But, in Canada's submission, the connotation "makes available" is not an appropriate reading of the term "provides" in Article 1.1(a)(1)(iii). In contrast, the United States argues that the Panel's interpretation that stumpage arrangements "provide" standing timber is correct. The United States contends that, where a government transfers ownership in goods by giving enterprises a right to take them, the government "provides" those goods, within the meaning of Article 1.1(a)(1)(iii).

69. Again, we begin with the ordinary meaning of the term. Before the Panel, the United States pointed to a definition of the term "provides", which suggested that the term means, *inter alia*, to "supply or furnish for use; make available".<sup>62</sup> This definition is the same as that relied upon by USDOC in making its determination that "regardless of whether the Provinces are supplying timber or making it available through a right of access, they are providing timber" within the meaning of the provision of United States countervailing duty law that corresponds to Article 1.1(a)(1)(iii) of the *SCM Agreement*.<sup>63</sup> We note that another definition of "provides" is "to put at the disposal of".<sup>64</sup>

70. Notwithstanding these definitions, Canada submits that the meaning of the term "provides" in Article 1.1(a)(1)(iii) of the *SCM Agreement* should be limited to the supplying or giving of goods or services. Canada raises two arguments to support this view. First, Canada suggests that the terms "provides goods" and "provides services" cannot be read to include the mere "making available" of goods or services, because "[t]o 'make available' services' ... would include any circumstance in which a government action makes possible a later receipt of services and to 'make available' goods' would capture every property law in a jurisdiction".<sup>65</sup> Secondly, Canada points to the use of the term

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<sup>62</sup>United States' first written submission to the Panel, para. 29, referring to *The New Shorter Oxford English Dictionary*, *supra*, footnote 43, Vol. II, p. 2393. We observe that this definition is unchanged in the recently published fifth edition of the *Shorter Oxford English Dictionary*, *supra*, footnote 45, Vol. II, p. 2382.

<sup>63</sup>*Decision Memorandum*, *supra*, footnote 3, pp. 29–30.

<sup>64</sup>*Collins Dictionary of the English Language*, G.A. Wilkes (ed.) (Wm. Collins Publishing, 1979), p. 1176.

<sup>65</sup>Canada's other appellant's submission, para. 54. (original emphasis)



"provide" in Articles 3.2 and 8 of the *Agreement on Agriculture*<sup>66</sup> and in Article XV:1 of the *General Agreement on Trade in Services* (the "GATS")<sup>67</sup> to suggest that "provides", when used in the context of the granting of subsidies, requires the actual *giving* of a subsidy.<sup>68</sup>

71. With respect to Canada's first argument, we do not see how the general governmental acts referred to by Canada would necessarily fall within the concept of a government "making available" services or goods. In our view, such actions would be too remote from the concept of "making available" or "putting at the disposal of", which requires there to be a reasonably proximate relationship between the action of the government providing the good or service on the one hand, and the use or enjoyment of the good or service by the recipient on the other. Indeed, a government must have some control over the *availability* of a specific thing being "made available".

72. Moreover, Canada's argument in this respect seems to disregard the fact that, in order to be subject to the disciplines of the *SCM Agreement*, or countervailing measures under Part V of that Agreement, a government action would also need to meet all other elements of the subsidy definition. Under Article 1.1(a)(1)(iii) of the *SCM Agreement*, not all government actions providing goods and services are necessarily financial contributions. If a government provides goods and services that are "general infrastructure", no financial contribution will exist. Furthermore, not all financial contributions are subsidies. The definition of subsidy includes further elements, in particular, that a financial contribution by a government must confer a "benefit". Finally, in accordance with

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<sup>66</sup>Article 3.2 of the *Agreement on Agriculture* reads:

Subject to the provisions of Article 6, a Member shall not *provide* support in favour of domestic producers in excess of the commitment levels specified in Section I of Part IV of its Schedule. (emphasis added)

Article 8 of the *Agreement on Agriculture* reads:

*Export Competition Commitments*

Each Member undertakes not to *provide* export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member's Schedule. (emphasis added)

<sup>67</sup>Article XV:1 of the GATS reads:

Members recognize that, in certain circumstances, subsidies may have distortive effects on trade in services. Members shall enter into negotiations with a view to developing the necessary multilateral disciplines to avoid such trade-distortive effects. The negotiations shall also address the appropriateness of countervailing procedures. Such negotiations shall recognize the role of subsidies in relation to the development programmes of developing countries and take into account the needs of Members, particularly developing country Members, for flexibility in this area. For the purpose of such negotiations, Members shall exchange information concerning all subsidies related to trade in services that they *provide* to their domestic service suppliers. (emphasis added; footnote omitted)

<sup>68</sup>Canada's other appellant's submission, para. 55.

Articles 1.2 and 2 of the *SCM Agreement*, a subsidy must be "specific" in order to be subject to the disciplines of the Agreement.

73. In any event, in our view, it does not make a difference, for purposes of applying the requirements of Article 1.1(a)(1)(iii) of the *SCM Agreement* to the facts of this case, if "provides" is interpreted as "supplies", "makes available" or "puts at the disposal of". What matters for determining the existence of a subsidy is whether all elements of the subsidy definition are fulfilled as a result of the transaction, irrespective of whether all elements are fulfilled *simultaneously*.

74. With respect to Canada's second argument regarding the *Agreement on Agriculture* and the GATS<sup>69</sup>, the articles cited by Canada involve the provision of "subsidies" or "support". We note that in Article 1.1(a)(1)(iii) of the *SCM Agreement*, the term "provides" relates to the provision of "goods" and "services" in the context of describing a certain type of financial contribution. The different context of these provisions means that it is not necessarily appropriate to equate, precisely, the scope of the term "provide" or "provides" as they are used in these different agreements. Accordingly, even if we were to accept Canada's contention that the context of Articles 3.2 and 8 of the *Agreement on Agriculture* and Article XV:1 of the GATS limits the meaning of the term "provide" in those provisions, this would not necessarily imply that the meaning of the term "provides" should be similarly limited in the context of Article 1.1(a)(1)(iii) of the *SCM Agreement*.

75. Turning to the Panel's finding regarding what is provided by provincial stumpage programs, we note that the Panel found that stumpage arrangements give tenure holders a right to enter onto government lands, cut standing timber, and enjoy exclusive rights over the timber that is harvested.<sup>70</sup> Like the Panel, we conclude that such arrangements represent a situation in which provincial governments provide standing timber. Thus, we disagree with Canada's submission that the granting of an intangible right to harvest standing timber cannot be equated with the act of providing that standing timber. By granting a right to harvest, the provincial governments put particular stands of timber at the disposal of timber harvesters and allow those enterprises, exclusively, to make use of those resources. Canada asserts that governments do not supply felled trees, logs, or lumber through stumpage transactions.<sup>71</sup> In our view, this assertion misses the point, because felled trees, logs and lumber are all distinct from the "standing timber" on which the Panel based its conclusions. Moreover, what matters, for purposes of determining whether a government "provides goods" in the sense of Article 1.1(a)(1)(iii), is the consequence of the transaction. Rights over felled trees or logs crystallize as a natural and inevitable consequence of the harvesters' exercise of their harvesting

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<sup>69</sup>See *supra*, para. 70.

<sup>70</sup>Panel Report, paras. 7.14–7.15.

<sup>71</sup>Canada's other appellant's submission, para. 56.

rights.<sup>72</sup> Indeed, as the Panel indicated, the evidence suggests that making available timber is the *raison d'être* of the stumpage arrangements.<sup>73</sup> Accordingly, like the Panel, we believe that, by granting a right to harvest standing timber, governments provide that standing timber to timber harvesters. We therefore agree with the Panel that, through stumpage arrangements, the provincial governments "provide" such goods, within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*.

76. For these reasons, we *uphold* the Panel's finding, in paragraph 7.30 of the Panel Report, that USDOC's "[d]etermination that the Canadian provinces are providing a financial contribution in the form of the provision of a good by providing standing timber to timber harvesters through the stumpage programmes" is not inconsistent with Article 1.1(a)(1)(iii) of the *SCM Agreement*.

## V. Calculation of Benefit

### A. Introduction

77. We turn next to the issue whether the Panel erred in its interpretation of Article 14(d) of the *SCM Agreement*, which relates, *inter alia*, to the calculation of benefit when goods are provided by a government. In the countervailing duty investigation underlying this dispute, USDOC determined that there were "no useable market-determined prices between Canadian buyers and sellers" that could be used to determine whether provincial stumpage programmes provide goods for less than adequate remuneration.<sup>74</sup> Therefore, USDOC used as a benchmark prices of stumpage in certain bordering

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<sup>72</sup>The Panel found, at paragraph 7.14 of the Panel Report, that:

In light of Canada's answers, it appears that the United States is correct when it argues that "there is no record evidence of stumpage contracts under which the contracting party (tenure holder or licensee) does not have ownership rights to the harvested timber". (footnote omitted)

<sup>73</sup>In this regard, we note that the Panel cited with approval a finding by the panel in *US – Softwood Lumber III* that "from the perspective of the tenure holder, the *only reason* to enter into tenure agreements with the provincial governments is to obtain the timber." (Panel Report, para. 7.16 (emphasis added)) In footnote 97 to that paragraph, the Panel continued, noting "that Canada acknowledged before that Panel that the main interest of tenure holders is the *end-product* of the harvest." (emphasis added) Indeed, the panel record in these proceedings shows that timber harvesters pay a "stumpage fee" only on the basis of the volume of timber that is *actually harvested*. (See, for example, Canada's response to Question 2 posed by the Panel at the First Panel Meeting; Panel Report, p. A-2) Moreover, the record shows that, at least in Quebec, Ontario and Alberta, the provincial governments retain a residual interest in the timber harvested until such time as the harvester has paid this volumetric fee. (See Canada's response to Question 3 posed by the Panel at the First Panel Meeting; Panel Report, pp. A-3–A-4). These considerations indicate that it is *standing timber*, as opposed to a mere right to harvest trees, that is the thing of value contracted for in a stumpage contract.

<sup>74</sup>*Decision Memorandum, supra*, footnote 3, pp. 36 ff. USDOC also refused to use as a benchmark the prices of stumpage from Canadian provinces not subject to the countervailing duty investigation, namely, the "Maritime Provinces" as defined by USDOC as New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland. (Final Determination, *supra*, footnote 3, pp. 15547) Those stumpage prices were rejected by USDOC for lack of sufficient pricing data. (*Decision Memorandum, supra*, footnote 3, p. 39)

states in the northern United States<sup>75</sup>, making adjustments purportedly to account for differences in conditions between those states and Canadian provinces.<sup>76</sup>

78. Before the Panel, Canada claimed that, by rejecting private prices in Canada, and using instead adjusted cross-border prices, USDOC acted inconsistently with Articles 10, 14, 14(d), 19.1, 19.4, and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.<sup>77</sup> The United States responded that the "appropriate benchmark for measuring benefit in this case would normally have been the fair market value of timber in Canada", but that private timber sales in Canada did not represent a "commercial" market because they were distorted by government intervention.<sup>78</sup> Therefore, according to the United States, USDOC was entitled to use prices for comparable stumpage from alternative sources, in this case from the bordering states in the northern United States, which were then adjusted to reflect market conditions in Canada, in accordance with Articles 1 and 14(d) of the *SCM Agreement*.<sup>79</sup>

79. The Panel agreed with Canada and found that:

In light of the fact that the USDOC acknowledged the existence of a private stumpage market in Canada, we find that the resort to US prices as the benchmark for the determination of benefit on grounds that private prices in Canada were distorted is inconsistent with Article 14 (d) [of the] *SCM Agreement*.<sup>80</sup>

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<sup>75</sup>Prices of stumpage in the bordering states of the northern United States were used by USDOC as representing world market prices available in Canada. (See *Decision Memorandum, supra*, footnote 3, p. 40) The specific states of the United States used as a benchmark for each Canadian province were: Maine for Quebec; Washington, Idaho and Montana for British Columbia; Michigan and Minnesota for Ontario; and Minnesota for Alberta, Manitoba and Saskatchewan. (See *ibid.*, pp. 54 ff) We use the term "cross-border prices" to refer to prices from those bordering states in the northern United States.

<sup>76</sup>With respect to the prices in the states of the northern United States chosen as benchmarks for specific Canadian provinces, USDOC assessed the need for adjustments to account for differences in market conditions, including factors such as road construction and maintenance requirements, fire extinction and protection costs, insect and disease protection and prevention costs, silviculture requirements, silviculture credits for non-mandatory activities, sustainable forest management and planning, reforestation and forest care costs, seedling transport expenses, environmental costs, forest inventory costs, geographic information system (GIS) costs, costs of developing annual reports, land use administration costs, other administration costs, transportation distances, harvesting costs, procurement costs, logging camp costs, helicopter logging costs, harvesting costs, rot and quality differences, differences in timber size, timber sale costs, old growth timber and quality characteristics, scaling costs, time value of money, time of payment, taxes and fees on United States harvesters, obligations to the First Nations, overlapping tenure costs, and bid preparation costs. *Decision Memorandum, supra*, footnote 3, pp. 54 ff)

<sup>77</sup>Request for the Establishment of a Panel by Canada, WT/DS257/3, 19 August 2002, p. 2.

<sup>78</sup>Panel Report, para. 7.38.

<sup>79</sup>*Ibid.*

<sup>80</sup>*Ibid.*, para. 7.64.

In addition, the Panel found consequential violations of Articles 10 and 32.1 of the *SCM Agreement* because the "countervailing measures were imposed on the basis of an inconsistent determination of the existence and amount of a subsidy".<sup>81</sup>

80. On appeal, the United States claims that the Panel erred in interpreting Article 14(d) as requiring that the determination of the adequacy of remuneration be based on *any* observed non-government prices, even when those prices are "substantially influenced" or "effectively determined" by the government's financial contribution.<sup>82</sup> The United States argues that the Panel's interpretation of Article 14(d) is "completely at odds" with the concept of "benefit", as used in Article 1.1 of the *SCM Agreement* and as interpreted by the Appellate Body.<sup>83</sup> The United States refers to the Appellate Body's interpretation of the term "benefit" in Article 1.1(b) in *Canada – Aircraft*, where it said that a government financial contribution confers a benefit if the "'financial contribution' makes the recipient 'better off' than it would otherwise have been, absent that contribution", and that the marketplace provides the appropriate basis for comparison.<sup>84</sup> According to the United States, the Panel's interpretation would not permit an investigating authority to determine whether the recipient is better off than it would have been absent the financial contribution.<sup>85</sup> In addition, the United States contends that the term "market conditions" in Article 14(d) "can only mean a market undistorted by the government's financial contribution."<sup>86</sup> Therefore, the United States submits that USDOC could rightfully reject the prices of private transactions in Canada as a benchmark and, consequently, requests that we *reverse* the Panel's finding that the United States acted inconsistently with Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement*.<sup>87</sup>

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<sup>81</sup>Panel Report, para. 7.65. (footnote omitted) The Panel declined to rule on Canada's claims relating to the calculation of benefit under Articles 19.1 and 19.4 of the *SCM Agreement* and Article VI:3 of the GATT 1994.

<sup>82</sup>United States' appellant's submission, para. 8.

<sup>83</sup>*Ibid.*, para. 17.

<sup>84</sup>Appellate Body Report, *Canada – Aircraft*, para. 157.

<sup>85</sup>United States' appellant's submission, paras. 16–17.

<sup>86</sup>*Ibid.*, para. 30.

<sup>87</sup>*Ibid.*

81. Canada submits that the Panel correctly interpreted Article 14(d) of the *SCM Agreement*. According to Canada, the ordinary meaning of Article 14(d) requires a comparison with "prevailing"—in the sense of existing—market conditions in the country of provision.<sup>88</sup> Canada asserts, furthermore, that the Panel's analysis is consistent with the Appellate Body's interpretation of the term "benefit" under Article 1.1(b) of the *SCM Agreement* in *Canada – Aircraft*.<sup>89</sup> In addition, Canada argues that the Panel's interpretation has contextual support in the chapeau of Article 14, which uses the term "shall", thus negating the United States' contention that the use of the term "guidelines" in the chapeau suggests that paragraph (d) does not set out mandatory rules.<sup>90</sup> Moreover, the absence of a reference to the country of provision in paragraphs (b) and (c) demonstrates, according to Canada, that when the drafters intended to permit consideration of conditions in another country, they did so explicitly.<sup>91</sup> Finally, Canada contends that the "inherent economic problems with cross-border comparisons", coupled with the broad range of other considerations that affect the comparison of forestry resources, demonstrate the correctness of the Panel's interpretation of Article 14(d) as applied in this case.<sup>92</sup> Consequently, Canada requests that we *uphold* the Panel's finding that the United States acted inconsistently with Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement*.

B. *Whether Article 14(d) of the SCM Agreement Permits Investigating Authorities to Use a Benchmark Other Than Private Prices in the Country of Provision*

82. The initial issue before us is whether an investigating authority may use a benchmark, under Article 14(d) of the *SCM Agreement*, other than private prices in the country of provision for determining if goods have been provided by a government for less than adequate remuneration.<sup>93</sup> If our answer were to be in the affirmative, two additional questions would arise: (i) what are the specific circumstances under Article 14(d) in which an investigating authority may use a benchmark other than private prices in the country of provision; and (ii) assuming such circumstances exist, what alternative benchmarks may an investigating authority use to determine whether goods were provided by a government for less than adequate remuneration.

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<sup>88</sup>Canada's appellee's submission, para. 32.

<sup>89</sup>*Ibid.*, paras. 33 and 38, referring to Appellate Body Report, *Canada – Aircraft*, paras. 157–158.

<sup>90</sup>Canada's appellee's submission, paras. 45–48.

<sup>91</sup>*Ibid.*, para. 49.

<sup>92</sup>*Ibid.*, paras. 51–52.

<sup>93</sup>As we have discussed in Section IV, the underlying countervailing duty investigation involved a financial contribution in the form of the provision of goods. Therefore, we limit our examination of this issue to instances involving the provision of goods and do not address situations where the financial contribution takes the form of the provision of services or the purchase of goods.

83. Article 14 of the *SCM Agreement* provides:

*Calculation of the Amount of a Subsidy in Terms  
of the Benefit to the Recipient*

For the purpose of Part V, any method used by the investigating authority to calculate the benefit to the recipient conferred pursuant to paragraph 1 of Article 1 shall be provided for in the national legislation or implementing regulations of the Member concerned and its application to each particular case shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines:

- (a) government provision of equity capital shall not be considered as conferring a benefit, unless the investment decision can be regarded as inconsistent with the usual investment practice (including for the provision of risk capital) of private investors in the territory of that Member;
- (b) a loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts;
- (c) a loan guarantee by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees;
- (d) the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. *The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).* (emphasis added)

84. As we observed earlier in this Report, not every financial contribution by a government in the form of provision of goods constitutes a subsidy, because a "benefit" must be conferred by virtue of that provision of goods.<sup>94</sup> Article 14(d) establishes that the provision of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration. As the Panel observed, the term "adequate" in this context means "sufficient, satisfactory".<sup>95</sup> "Remuneration" is defined as "reward, recompense; payment, pay".<sup>96</sup> Thus, a benefit is conferred when a government provides goods to a recipient and, in return, receives insufficient payment or compensation for those goods.

85. The question then becomes how to determine whether adequate remuneration was paid for the goods provided by the government. This is dealt with in the second sentence of Article 14(d), which provides that "[t]he adequacy of remuneration shall be determined *in relation to prevailing market conditions* for the good or service in question *in the country of provision* or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale)". (emphasis added)

86. In interpreting the second sentence of Article 14(d), the Panel noted first that, in this context, the term "in relation to" means "in comparison with".<sup>97</sup> The Panel next observed that "prevailing" market conditions refers to "the market conditions 'as they exist' or 'which are predominant' in the country of provision".<sup>98</sup> From this, the Panel reasoned that:

Therefore, according to Article 14 (d), the price of the good provided, its quality, availability, marketability, transportation and other conditions of purchase or sale which are used as the benchmark for determining the adequacy of the remuneration have to be such as are prevailing in the country of provision. In sum, a plain reading of the text of Article 14 (d) leads us to the initial conclusion that the market which is to be used as the benchmark for determining benefit to the recipient is the market of the country of provision, in this case Canada.<sup>99</sup>

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<sup>94</sup>See *supra*, para. 51.

<sup>95</sup>Panel Report, para. 7.48, quoting from *The New Shorter Oxford English Dictionary*, *supra*, footnote 43, Vol. I, p. 26. The *Shorter Oxford English Dictionary* includes the following definitions for "adequate" when used as an adjective: "Equal in magnitude or extent; ... Commensurate in fitness; sufficient, satisfactory; ... Of an idea or concept; fully and clearly representing its object". *Shorter Oxford English Dictionary*, *supra*, footnote 45, Vol. I, p. 26)

<sup>96</sup>*Shorter Oxford English Dictionary*, *supra*, footnote 45, Vol. II, p. 2529.

<sup>97</sup>Panel Report, para. 7.48.

<sup>98</sup>*Ibid.*, para. 7.50, quoting from *The New Shorter Oxford English Dictionary*, *supra*, footnote 43, Vol. II, p. 2347. (footnote omitted)

<sup>99</sup>Panel Report, para. 7.50. (footnote omitted)



The Panel then went on to reject the United States' contention that the term "market" means "fair market value" or a market "undistorted by government intervention"<sup>100</sup>, stating that:

... Article 14 (d) [of the] SCM Agreement identifies the market conditions which shall be used to determine adequacy of remuneration as those which are "prevailing" in respect of the price of the good, its quality, availability, marketability, transportation, and other conditions of purchase or sale, in other words, the market conditions "as can be found".<sup>101</sup>

The Panel reasoned that, "as long as there are prices determined by independent operators following the principle of supply and demand, even if supply or demand are affected by the government's presence in the market, there is a 'market' in the sense of Article 14(d) [of the] SCM Agreement."<sup>102</sup> Therefore, the Panel concluded that "[i]n light of the fact that the USDOC acknowledged the existence of a private stumpage market in Canada ... resort to US prices as the benchmark for the determination of benefit on grounds that private prices in Canada were distorted is inconsistent with Article 14(d) [of the] SCM Agreement."<sup>103</sup>

87. Turning first to the text of Article 14(d), we consider the submission of the United States that the term "market conditions" necessarily implies a market undistorted by the government's financial contribution. In our view, the United States' approach goes too far. We agree with the Panel that "[t]he text of Article 14 (d) [of the] SCM Agreement does not qualify in any way the 'market' conditions which are to be used as the benchmark ... [a]s such, the text does not explicitly refer to a 'pure' market, to a market 'undistorted by government intervention', or to a 'fair market value'."<sup>104</sup>

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<sup>100</sup>Panel Report, paras. 7.50–7.51.

<sup>101</sup>*Ibid.*, para. 7.51.

<sup>102</sup>*Ibid.*, para. 7.60. (footnote omitted)

<sup>103</sup>*Ibid.*, para. 7.64. The Panel noted the following summary by USDOC of the market situation in various Canadian provinces:

During the POI, total softwood harvested from Crown lands accounted for between approximately 83 and 99 per cent of all softwood timber harvested in each of the Provinces. Specifically, the Provincial, federal and private share of softwood timber harvests, by Province are:

British Columbia – 90 per cent Provincial, less than 1 per cent federal, and almost 10 per cent private;

Quebec – 83 per cent Provincial, and 17 per cent private;

Ontario – 92 per cent Provincial and 7 per cent private;

Alberta – 98 per cent Provincial, 1 per cent federal, and 1 per cent private;

Manitoba – 94 per cent Provincial, 1 per cent federal and 5 per cent private;

Saskatchewan – 90 per cent Provincial, 1 per cent federal and 9 per cent private.

(*Ibid.*, para. 7.61, quoting from the *Decision Memorandum, supra*, footnote 3, pp. 37-38)

<sup>104</sup>Panel Report, paras. 7.50–7.51.

This is confirmed by the Spanish and French versions of Article 14(d), neither of which supports the contention that the term "market" qualifies the term "conditions" so as to exclude situations in which there is government involvement.<sup>105</sup>

88. We now examine the meaning of the phrase "in relation to" in Article 14(d). We are of the view that the Panel failed to give proper meaning and effect to the phrase "in relation to" as it is used in Article 14(d). The Panel reasoned that the phrase "in relation to" in the context of Article 14(d) means "in comparison with".<sup>106</sup> Hence, the Panel concluded that the determination of the adequacy of remuneration has to be made "in comparison with" prevailing market conditions for the goods in the country of provision, and thus no other comparison will do when private market prices exist. We do not agree.

89. As we see it, the phrase "in relation to" implies a comparative exercise, but its meaning is not limited to "in comparison with".<sup>107</sup> The phrase "in relation to" has a meaning similar to the phrases "as regards" and "with respect to".<sup>108</sup> These phrases do not denote the rigid comparison suggested by the Panel, but may imply a broader sense of "relation, connection, reference".<sup>109</sup> Thus, the use of the phrase "in relation to" in Article 14(d) suggests that, contrary to the Panel's understanding, the drafters did not intend to exclude any possibility of using as a benchmark something other than private prices in the market of the country of provision. This is not to say, however, that private prices in the market of provision may be disregarded. Rather, it must be demonstrated that, based on the facts of the case, the benchmark chosen relates or refers to, or is connected with, the conditions prevailing in the market of the country of provision.

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<sup>105</sup>The phrase used in the French version is "*aux conditions du marché existantes*" and the Spanish version is "*condiciones reinantes en el mercado*".

<sup>106</sup>Panel Report, para. 7.48.

<sup>107</sup>We observe that the phrase "in relation to" is used in other provisions of the *SCM Agreement* in a manner that does not connote "in comparison with". For instance, Article 15.6 of the *SCM Agreement* states that "[t]he effect of the subsidized imports shall be assessed in relation to the domestic production of the like product". Article 15.6 cannot properly be read as requiring a comparison between "[t]he effect of the subsidized imports" and "the domestic production of the like product". Similarly, Article 15.3 of that Agreement provides that, in order to assess cumulatively the effects of imports of a product from more than one country that are simultaneously subject to countervailing duty investigations, investigating authorities must determine that, *inter alia*, "the amount of subsidization established in relation to the imports from each country is more than *de minimis*". In this provision, the phrase "in relation to" is not used in the sense of "in comparison with" but rather in the sense of "in proportion to". Therefore, the precise meaning of the phrase "in relation to" will vary depending on the specific context in which it is used.

<sup>108</sup>*Shorter Oxford English Dictionary*, *supra*, footnote 45, Vol. II, p. 2520, defines "in relation to" as "as regards". In turn, "as regards" is defined as "concerning, with respect to". (*Ibid*, Vol. II, p. 2512) The French version of Article 14(d) of the *SCM Agreement* supports our view. It uses the term "*par rapport aux*". *Le Nouveau Petit Robert* includes the following definition for "*rapport*": "*Lien, relation qui existe entre plusieurs objets distincts et que l'esprit constate.*" (*Le Nouveau Petit Robert*, *supra*, footnote 47, p. 2170)

<sup>109</sup>The definition of "respect" includes "Relation, connection, reference, regard" as well as "Comparison". (*Shorter Oxford English Dictionary*, *supra*, footnote 45, Vol. II, p. 2550)

90. Although Article 14(d) does not dictate that private prices are to be used as the *exclusive* benchmark in all situations, it does emphasize by its terms that prices of similar goods sold by private suppliers in the country of provision are the primary benchmark that investigating authorities must use when determining whether goods have been provided by a government for less than adequate remuneration.<sup>110</sup> In this case, both participants and the third participants agree that the starting-point, when determining adequacy of remuneration, is the prices at which the same or similar goods are sold by private suppliers in arm's length transactions in the country of provision. This approach reflects the fact that private prices in the market of provision will generally represent an appropriate measure of the "adequacy of remuneration" for the provision of goods. However, this may not always be the case. As will be explained below, investigating authorities may use a benchmark other than private prices in the country of provision under Article 14(d), if it is first established that private prices in that country are distorted because of the government's predominant role in providing those goods.<sup>111</sup>

91. In addition to confining, in our view incorrectly, the meaning of the phrase "in relation to" in Article 14(d) to "in comparison with", the Panel's interpretation does not give due consideration to the provision's immediate context, particularly the chapeau of Article 14. The chapeau of Article 14 requires that "*any*" method used by investigating authorities to calculate the benefit to the recipient shall be provided for in a WTO Member's legislation or regulations, and it requires that its application be transparent and adequately explained. The reference to "*any*" method in the chapeau clearly implies that more than one method consistent with Article 14 is available to investigating authorities for purposes of calculating the benefit to the recipient. The Panel's interpretation of paragraph (d) that, whenever available, private prices have to be used *exclusively* as the benchmark, is not supported by the text of the chapeau, which gives WTO Members the possibility to select *any* method that is in conformity with the "guidelines" set out in Article 14.

92. The chapeau of Article 14 also provides that any method used by an investigating authority in calculating benefit "*shall* be consistent with the ... *guidelines*" set out in paragraphs (a) through (d). (emphasis added) The Panel observed that:

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<sup>110</sup>As Canada noted, paragraph (d) of Article 14 refers expressly to "in the country of provision". Paragraph (a) of Article 14 similarly refers to "in the territory of that Member". By contrast, paragraphs (b) and (c) do not refer either to the country of provision or the territory of the Member.

<sup>111</sup>See *infra*, para. 103.

... Article 14 (d) [of the] SCM Agreement uses the term "shall" to indicate that adequacy of remuneration must be determined in relation to, i.e. compared with, the prevailing market conditions in the country of provision, and the data to be used are those which reflect the prevailing market conditions in the country of provision. The precise detailed method of calculation is not determined, in that sense Article 14 (a) – (d) [of the] SCM Agreement are guidelines, but the framework within which this calculation is to be performed is clearly determined and limited in a mandatory manner by the prevailing market conditions in the country of provision.<sup>112</sup>

We agree with the Panel that the term "shall" in the last sentence of the chapeau of Article 14 suggests that calculating benefit consistently with the guidelines is mandatory. We also agree that the term "guidelines" suggests that Article 14 provides the "framework within which this calculation is to be performed", although the "precise detailed method of calculation is not determined".<sup>113</sup> Taken together, these terms establish mandatory parameters within which the benefit must be calculated, but they do not require using only one methodology for determining the adequacy of remuneration for the provision of goods by a government. Thus, we find merit in the United States' submission that the use of the term "guidelines" in Article 14 suggests that paragraphs (a) through (d) should not be interpreted as "rigid rules that purport to contemplate every conceivable factual circumstance".<sup>114</sup>

93. Furthermore, the Panel's interpretation is not supported by the objective of Article 14. As the title indicates, Article 14 deals with the "Calculation of the Amount of a Subsidy in Terms of the Benefit to the Recipient". As noted above, in *Canada – Aircraft*, the Appellate Body stated that the "there can be no 'benefit' to the recipient unless the 'financial contribution' makes the recipient 'better off' than it would otherwise have been, absent that contribution".<sup>115</sup> According to Article 14(d), this benefit is to be found when a recipient obtains goods from the government for "less than adequate remuneration", and such adequacy is to be evaluated in relation to prevailing market conditions in the country of provision. Under the approach advocated by the Panel (that is, private prices in the country of provision must be used whenever they exist), however, there may be situations in which there is no way of telling whether the recipient is "better off" *absent the financial contribution*. This is because the government's role in providing the financial contribution is so predominant that it effectively determines the price at which private suppliers sell the same or similar goods, so that the comparison contemplated by Article 14 would become circular.<sup>116</sup>

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<sup>112</sup>Panel Report, para. 7.49.

<sup>113</sup>*Ibid.*

<sup>114</sup>United States' appellant's submission, para. 25.

<sup>115</sup>Appellate Body Report, *Canada – Aircraft*, para. 157.

<sup>116</sup>United States' appellant's submission, para. 16.

94. The Panel itself acknowledged that there were problems of "economic logic" inherent in its interpretation of Article 14(d).<sup>117</sup> As the Panel explained, in certain situations where government involvement in the market is substantial, the prices of private suppliers may be artificially suppressed because of the prices charged for the same goods by the government.<sup>118</sup> "In such cases", the Panel said:

... a comparison of the conditions of the government financial contribution with the conditions prevailing in the private market would not fully capture the extent of the distortion arising from the government financial contribution, a result that in our view would not necessarily be the most sensible one from the perspective of economic logic.<sup>119</sup>

Notwithstanding this, the Panel concluded that it would not be appropriate "to substitute its economic judgement for that of the drafters".<sup>120</sup>

95. We have said that the Panel's restrictive interpretation of paragraph (d) frustrates the purpose of Article 14. More generally, it also frustrates the object and purpose of the *SCM Agreement*, which includes disciplining the use of subsidies and countervailing measures while, at the same time, enabling WTO Members whose domestic industries are harmed by subsidized imports to use such remedies.<sup>121</sup> This is because the determination of the existence of a benefit is a necessary condition for the application of countervailing measures under the *SCM Agreement*. If the calculation of the benefit yields a result that is artificially low, or even zero, as could be the case under the Panel's approach, then a WTO Member could not fully offset, by applying countervailing duties, the effect of the subsidy as permitted by the Agreement.

96. In sum, the Panel's interpretation of Article 14(d) appears, in our view, to be overly restrictive and based on an isolated reading of the text. To us, such a restrictive reading of Article 14(d) is not supported by the text of the provision, when read in the light of its context and the object and purpose of the *SCM Agreement*, as required by Article 31 of the *Vienna Convention*. Thus, in our view, Members are obliged, under Article 14(d), to abide by the guideline for determining whether a government has provided goods for less than adequate remuneration. However, contrary to the views of the Panel, that guideline does not require the use of private prices in the market of the country of

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<sup>117</sup>Panel Report, para. 7.58.

<sup>118</sup>USDOC found that there were no "usable" market-determined prices from transactions involving Canadian buyers and sellers that could be used to measure whether the provincial stumpage programs provide goods for less than adequate remuneration. (*Decision Memorandum, supra*, footnote 3, pp. 36 ff.)

<sup>119</sup>Panel Report, para. 7.58.

<sup>120</sup>*Ibid.*, para. 7.59.

<sup>121</sup>Appellate Body Report, *US – Carbon Steel*, paras. 73–74.

provision in every situation. Rather, that guideline requires that the method selected for calculating the benefit must relate or refer to, or be connected with, the prevailing market conditions in the country of provision, and must reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale, as required by Article 14(d).

C. *When May Investigating Authorities Use a Benchmark Other Than Private Prices in the Country of Provision?*

97. Having established that prices in the market of the country of provision are the primary, but not the exclusive, benchmark for calculating benefit, we come to the next question that arises in our analysis, namely, when an investigating authority may use a benchmark other than private prices in the country of provision for purposes of calculating the benefit under Article 14(d).

98. Despite the Panel's finding that Article 14(d) requires the use of private prices in the country of provision as the benchmark whenever they exist, the Panel nevertheless acknowledged that "it will in certain situations not be possible to use in-country prices" as a benchmark, and gave two examples of such situations, neither of which it found to be present in the underlying countervailing duty investigation: (i) where the government is the only supplier of the particular goods in the country; and, (ii) where the government administratively controls all of the prices for those goods in the country.<sup>122</sup> In these situations, the Panel reasoned that the "only remaining possibility would appear to be the construction of some sort of a proxy for, or estimate of, the market price for the good in that country".<sup>123</sup>

99. The United States claims, on appeal, that the Panel erred in not recognizing that Article 14(d) also allows investigating authorities to use a benchmark other than private prices in a third situation: where private prices are "substantially influenced" or "effectively determined" by the government's financial contribution.<sup>124</sup> We understand that by "substantially influenced" or "effectively determined", the United States refers to a situation where the government has such a predominant role in the market, as a provider of certain goods, that private suppliers will align their prices with those of the government-provided goods; in other words, a situation where the government effectively acts as a "price-setter" and private suppliers are "price-takers". Considering that the situation of government predominance in the market, as a provider of certain goods, is the only one raised on appeal by the

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<sup>122</sup>In both situations, the Panel assumed an absence of imports. (Panel Report, para. 7.57)

<sup>123</sup>*Ibid.*, para. 7.57. In footnote 136 to that paragraph, the Panel noted, moreover, that Canada itself agreed that, where a government is the sole supplier, "import prices for the same good, which may or may not be 'world market prices', if available to purchasers in the country of provision, could be used as a benchmark".

<sup>124</sup>United States' appellant's submission, para. 8.

United States, we will limit our examination to whether an investigating authority may use a benchmark other than private prices in the country of provision in that particular situation.

100. In analyzing this question, we have some difficulty with the Panel's approach of treating a situation in which the government is the sole supplier of certain goods differently from a situation in which the government is the predominant supplier of those goods. In terms of market distortion and effect on prices, there may be little difference between situations where the government is the sole provider of certain goods and situations where the government has a predominant role in the market as a provider of those goods. Whenever the government is the predominant provider of certain goods, even if not the sole provider, it is likely that it can affect through its own pricing strategy the prices of private providers for those goods, inducing the latter to align their prices to the point where there may be little difference, if any, between the government price and the private prices. This would be so even if the government price does not represent adequate remuneration. The resulting comparison of prices carried out under the Panel's approach to interpreting Article 14(d) would indicate a "benefit" that is artificially low, or even zero, such that the full extent of the subsidy would not be captured, as the Panel itself acknowledged.<sup>125</sup> As a result, the subsidy disciplines in the *SCM Agreement* and the right of Members to countervail subsidies could be undermined or circumvented when the government is a predominant provider of certain goods.

101. It appears to us that the language found in Article 14(d) ensures that the provision's purposes are not frustrated in such situations. Thus, while requiring investigating authorities to calculate benefit "in relation to" prevailing conditions in the market of the country of provision, Article 14(d) permits investigating authorities to use a benchmark other than private prices in that market. When private prices are distorted because the government's participation in the market as a provider of the same or similar goods is so predominant that private suppliers will align their prices with those of the government-provided goods, it will not be possible to calculate benefit having regard exclusively to such prices.

102. We emphasize once again that the possibility under Article 14(d) for investigating authorities to consider a benchmark other than private prices in the country of provision is very limited. We agree with the United States that "[t]he fact that the government is a significant supplier of goods does not, in itself, establish that all prices for the goods are distorted".<sup>126</sup> Thus, an allegation that a government is a significant supplier would not, on its own, prove distortion and allow an investigating authority to choose a benchmark other than private prices in the country of provision. The determination of whether private prices are distorted because of the government's predominant role in

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<sup>125</sup>Panel Report, para. 7.58.

<sup>126</sup>United States' appellant's submission, para. 28.

the market, as a provider of certain goods, must be made on a case-by-case basis, according to the particular facts underlying each countervailing duty investigation.

103. For these reasons, we *reverse* the Panel's finding, in paragraph 7.64 of the Panel Report, with respect to the interpretation of Article 14(d) of the *SCM Agreement*. We find, instead, that an investigating authority may use a benchmark other than private prices of the goods in question in the country of provision, when it has been established that those private prices are distorted, because of the predominant role of the government in the market as a provider of the same or similar goods. When an investigating authority resorts, in such a situation, to a benchmark other than private prices in the country of provision, the benchmark chosen must, nevertheless, relate or refer to, or be connected with, the prevailing market conditions in that country, and must reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale, as required by Article 14(d).

#### D. *Alternative Benchmarks*

104. Having reached this conclusion, the question thus arises what alternative benchmark, consistent with Article 14(d), could be available in such situations, for purposes of determining whether the goods have been provided by the government for less than adequate remuneration.

105. During the Panel proceedings, Canada suggested that an alternative benchmark that investigating authorities could possibly use for these purposes was "import prices for the same good, which may or may not be 'world market prices', if available to purchasers in the country of provision".<sup>127</sup> At the oral hearing, Canada referred to three possible alternative benchmarks: (i) a benchmark constructed using a methodology similar to that provided in Article 2.2 of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "*Anti-Dumping Agreement*"); (ii) a proxy estimated on the basis of costs of production<sup>128</sup>; and (iii) a methodology that examines whether government prices are consistent with market principles. The United States submitted that, in certain situations, world market prices available in the country of

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<sup>127</sup>Canada suggested this alternative benchmark in the context of a situation where the government is the sole supplier of certain goods or services. The European Communities suggested that world market prices could be used in a similar context. (See Panel Report, footnote 136 to para. 7.57) As noted earlier, the Panel stated that, where the government is the sole supplier or administratively controls all of the prices, "[t]he only remaining possibility would appear to be the construction of some sort of a proxy for, or estimate of, the market price for the good in that country". (*ibid.*, para. 7.57) During the countervailing duty investigation, the respondents contended that USDOC should use prices in the Canadian provinces not subject to the investigation, namely the Maritime Provinces, as a benchmark. USDOC rejected the use of prices in other Canadian provinces, namely the Maritime Provinces, as a benchmark, due to lack of information in the record about prices in those provinces. (*Decision Memorandum, supra*, footnote 3, p. 39)

<sup>128</sup>Canada, in this regard, referred to the Appellate Body Report, in *Canada – Dairy (Article 21.5 – New Zealand and US)*.



provision, on the one hand, and an examination of the consistency with market principles, on the other, may be alternative benchmarks that could be used to determine the adequacy of remuneration.<sup>129</sup>

106. We agree with the submissions of the participants and third participants that alternative methods for determining the adequacy of remuneration could include proxies that take into account prices for similar goods quoted on world markets, or proxies constructed on the basis of production costs. We emphasize, however, that where an investigating authority proceeds in this manner, it is under an obligation to ensure that the resulting benchmark relates or refers to, or is connected with, prevailing market conditions in the country of provision, and must reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale, as required by Article 14(d). At any rate, we are not called upon, in this appeal, to suggest alternative methods that would be available to investigating authorities upon a determination that private prices in the country of provision are distorted due to the government's predominant role in the market as provider of the same or similar goods. Nor are we required to determine the consistency with Article 14(d) of all the alternative methods mentioned by the participants and third participants; such assessment will depend on how any such method is applied in a particular case. We, therefore, make no findings on the WTO-consistency of any of these methods in the abstract.

107. Rather, it is only the specific alternative method used by USDOC in the underlying countervailing duty investigation for determining the adequacy of remuneration that is at issue in this appeal. The benchmark used by USDOC consisted of prices of stumpage in bordering states of the northern United States.<sup>130</sup> The United States explained before the Panel that cross-border stumpage prices were duly adjusted to take into account market conditions prevailing in Canada.<sup>131</sup> We turn to this method used by USDOC next.

E. *The Consistency of the Alternative Benchmark Used by USDOC with Article 14(d)*

108. Before reviewing the Panel's finding with respect to the particular benchmark used by USDOC, we observe that, when choosing an alternative method for determining the adequacy of

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<sup>129</sup>United States' responses to questioning at oral hearing.

<sup>130</sup>We note that, in the underlying countervailing duty investigation, USDOC considered that adjusted prices of stumpage in the bordering states of the northern United States represented world market prices available in Canada. (See *supra*, footnote 75 to para. 77)

<sup>131</sup>During the oral hearing, the United States explained that, generally speaking, the adjustments made related to three areas: silviculture, roads construction and maintenance, and fire protection. Before the Panel, the United States also mentioned adjustments related to species mix. (United States' response to Question 8 posed by the Panel at the First Panel Meeting; Panel Report, pp. A-38–A-39) As noted previously, the *Decision Memorandum* discusses other adjustments considered specifically by province. (*Decision Memorandum, supra*, footnote 3, pp. 54 *ff*; see *supra*, footnote 76)

remuneration, it has to be kept in mind that prices in the market of a WTO Member would be expected to reflect prevailing market conditions in that Member; they are unlikely to reflect conditions prevailing in another Member. Therefore, it cannot be presumed that market conditions prevailing in one Member, for instance the United States, relate or refer to, or are connected with, market conditions prevailing in another Member, such as Canada for example. Indeed, it seems to us that it would be difficult, from a practical point of view, for investigating authorities to replicate reliably market conditions prevailing in one country on the basis of market conditions prevailing in another country. First, there are numerous factors to be taken into account in making adjustments to market conditions prevailing in one country so as to replicate those prevailing in another country; secondly, it would be difficult to ensure that all necessary adjustments are made to prices in one country in order to develop a benchmark that relates or refers to, or is connected with, prevailing market conditions in another country, so as to reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale in that other country.<sup>132</sup>

109. It is clear, in the abstract, that different factors can result in one country having a comparative advantage over another with respect to the production of certain goods. In any event, any comparative advantage would be reflected in the market conditions prevailing in the country of provision and, therefore, would have to be taken into account and reflected in the adjustments made to any method used for the determination of adequacy of remuneration, if it is to relate or refer to, or be connected with, prevailing market conditions in the market of provision. This is because countervailing measures may be used only for the purpose of offsetting a subsidy bestowed upon a product, provided that it causes injury to the domestic industry producing the like product. They must not be used to offset differences in comparative advantages between countries.

110. Turning to the examination of the specific alternative method used by USDOC in the underlying countervailing duty investigation, we note that the Panel examined Canada's claims against USDOC's benefit determination in the light of the Panel's interpretation of Article 14(d) of the *SCM Agreement*. According to that interpretation, "as long as there are prices determined by independent operators following the principle of supply and demand, even if supply or demand are affected by the government's presence in the market, there is a 'market' in the sense of Article 14(d)

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<sup>132</sup>USDOC acknowledged that "it may be difficult to achieve perfect comparability", but rejected the contention that "the size and scope of the adjustments make comparability impossible". According to USDOC, prices of stumpage in the United States were not, in this case, "outside the spectrum of commercial reality and availability". (*Decision Memorandum, supra*, footnote 3, p. 41)

[of the] SCM Agreement."<sup>133</sup> The Panel found further "that the USDOC acknowledged the existence of a private market for stumpage in Canada"<sup>134</sup> and concluded that:

In light of the fact that the USDOC acknowledged the existence of a private stumpage market in Canada, we find that the resort to US prices as the benchmark for the determination of benefit on grounds that private prices in Canada were distorted is inconsistent with Article 14 (d) [of the] SCM Agreement.<sup>135</sup>

111. The Panel further stated that it did not need to "address the issue whether the USDOC had sufficient evidence of price suppression or conducted a proper analysis of the alleged distortive effect of the dominant government presence in the market."<sup>136</sup> Thus, the Panel did not establish whether private prices of the goods in question in the country of provision were distorted because of the predominant role of the government in that market as a provider of the same or similar goods.

112. Therefore, the Panel's ultimate finding that USDOC failed to determine benefit consistently with Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement* is predicated exclusively on its interpretation of Article 14(d), which we have already reversed above. Thus, we must also *reverse* the Panel's consequential finding, in paragraph 7.65 of the Panel Report, that USDOC failed to determine benefit consistently with Articles 14 and 14(d) of the *SCM Agreement* and that the imposition of countervailing duties based on that determination was inconsistent with Articles 10 and 32.1 of that Agreement.<sup>137</sup> It does not necessarily follow, however, that we find that USDOC's determination of benefit in the underlying countervailing duty investigation is consistent with Article 14(d), as we have interpreted this provision in the preceding paragraphs.

113. In order to determine the WTO-consistency of USDOC's benefit determination, we would have to complete the legal analysis. Thus, as a preliminary step, we must consider whether it is possible for us to do so in order to facilitate the prompt settlement of the dispute, in accordance with Article 3.3 of the DSU, by examining Canada's claim ourselves. The Appellate Body has stated in

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<sup>133</sup>Panel Report, para. 7.60.

<sup>134</sup>*Ibid.*, para. 7.63.

<sup>135</sup>*Ibid.*, para. 7.64.

<sup>136</sup>*Ibid.*

<sup>137</sup>The Panel found in paragraph 7.65 of the Panel Report that:

... USDOC failed to determine benefit in a manner consistent with Articles 14 and 14(d) [of the] SCM Agreement and we therefore find that the USDOC's imposition of countervailing measures was inconsistent with the United States' obligations under Articles 14 and 14(d) [of the] SCM Agreement as well as Articles 10 and 32.1 of the SCM Agreement as these countervailing measures were imposed on the basis of an inconsistent determination of the existence and amount of a subsidy. (footnote omitted)

previous cases that it is possible and appropriate to complete the legal analysis provided there are sufficient findings of fact by the Panel or undisputed facts in the Panel record to enable it to do so.<sup>138</sup>

114. Both participants acknowledged during the oral hearing that, if we were to modify or reverse the Panel's interpretation of Article 14(d), there would be insufficient findings of fact by the Panel or undisputed facts in the Panel record to enable us to complete the legal analysis of this issue. We agree. In concluding that the United States acted inconsistently with Article 14(d), the Panel made only the following two findings of fact: (i) that "the USDOC acknowledged the existence of a private market for stumpage in Canada"; and (ii) that "the USDOC had before it private stumpage prices for four of the most important [Canadian] provinces".<sup>139</sup> The Panel abstained from making additional findings and said:

... we need not address the issue whether the USDOC had sufficient evidence of price suppression or conducted a proper analysis of the alleged distortive effect of the dominant government presence in the market. Nor need we address whether the proxy used by the United States for the prevailing market conditions in Canada was appropriate, i.e. whether the USDOC made proper adjustments to the US stumpage prices to reflect market conditions in Canada. Neither do we consider it relevant to rule on the argument made by Canada that any benefit analysis should include a determination of the potential trade advantage for the recipient of the subsidy.<sup>140</sup>

115. We have already found that Article 14(d) permits investigating authorities to use a benchmark other than private prices in the country of provision, if it is established that those private prices are distorted because the government's participation in the market, as a provider of the same or similar goods, is so predominant that private suppliers will align their prices with those of the government-provided goods. As stated above, the Panel, however, made no findings of fact relating to the alleged distortive effect on prices of the provincial governments' participation in the market for standing timber.<sup>141</sup> The Panel record indicates that the facts surrounding this question are not undisputed, and that Canada challenged the evidence relied on by USDOC to conclude that private prices for stumpage in Canada were distorted.<sup>142</sup> Therefore, there are insufficient Panel findings or undisputed facts in the record to enable us to determine whether USDOC was justified, under Article 14(d), in

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<sup>138</sup>Appellate Body Report, *US – Section 211 Appropriations Act*, para. 343.

<sup>139</sup>Panel Report, para. 7.63.

<sup>140</sup>*Ibid.*, para. 7.64.

<sup>141</sup>For instance, the Panel made no findings regarding the level of market distortion in each Canadian province given the differences in government market share, which ranged from 83 to 99 percent. (See *supra*, footnote 103)

<sup>142</sup>Canada's response to questions posed by the Panel at the First Panel Meeting, paras. 90–103; Panel Report, pp. A-19–A-21.

using a benchmark other than private prices in Canada, on the basis that prices of private stumpage in Canada were distorted by the Canadian provinces' predominant participation in the market as providers of standing timber.

116. Even if we were to assume that USDOC was justified in rejecting private prices in Canada, we would then have to determine whether the particular benchmark used by USDOC in the underlying countervailing duty investigation complies with the requirements of Article 14(d). This would require an examination of whether the prices of private stumpage in the bordering states in the northern United States that USDOC selected as a benchmark, following the adjustments performed by USDOC, related or referred to, or were connected with, prevailing market conditions in Canada, (including price, quality, availability, marketability, transportation and other conditions of purchase or sale). In other words, an examination would be required whether USDOC correctly determined that standing timber was provided by the provincial governments for less than adequate remuneration and whether the benefit received by the recipients was correctly calculated. The Panel, however, made no findings of fact relating to whether prices of private stumpage in the bordering states of the northern United States used by USDOC as a benchmark were adequately adjusted so as to be consistent with Article 14(d).

117. Moreover, the Panel record indicates that Canada disputed most aspects of the USDOC's decision to use cross-border prices, including the adjustment factors. For instance, Canada questioned USDOC's assertion that United States standing timber is "available" in Canada so as to reflect world market prices available in Canada.<sup>143</sup> Canada also alleged that "[United States] state agencies recognize that a range of differences affect stumpage values even within a single state".<sup>144</sup> Canada, moreover, disputed the United States' contention that USDOC "made adjustments that took into account the prevailing market conditions 'to ensure a proper comparison between the government price and the market benchmark price'".<sup>145</sup> It also pointed out before the Panel and reiterated on appeal a number of factors that undermine the cross-border comparability of forestry resources.<sup>146</sup> Canada emphasized that cross-border comparisons do not account for comparative advantages arising

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<sup>143</sup>Canada argued before the Panel that "... even if in certain areas of the United States Canadian producers can legally bid on certain cutting rights in the United States, harvest US timber and import US logs for milling, US standing timber – the alleged good provided, not logs produced from the standing timber - is still not available 'in' Canada". (Panel Report, para. 7.35)

<sup>144</sup>Canada's appellee's submission, footnote 52 to para. 52.

<sup>145</sup>Canada's second written submission to the Panel, para. 29, referring to the United States' response to Question 8 posed by the Panel at the First Panel Meeting, para. 11; Panel Report, p. A-39.

<sup>146</sup>These include: differences in timber characteristics and operating conditions such as the type, mix, quality and location of forest resources, as well as costs of harvesting and transporting timber; measurement systems; and the rights and obligations related to tenures, including the duration of harvesting rights and responsibilities including silviculture, road-building and forest management. (Canada's appellee's submission, para. 52) See also Panel Report, footnote 109 to para. 7.35.

from differences in natural resource endowments between countries. It is also clear from the participants' submissions during the oral hearing that the factual information is not undisputed.

118. Accordingly, there are insufficient factual findings by the Panel and undisputed facts in the Panel record to enable us to examine whether the benchmark used by USDOC in the underlying investigation related or referred to, or was connected with, prevailing market conditions in Canada, as required by Article 14(d), so as to adequately reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale. Consequently, we are unable to complete the legal analysis of Canada's claim that the United States acted inconsistently with Article 14(d) of the *SCM Agreement*. We observe, in this regard, that panels sometimes make alternative factual findings that serve to assist the Appellate Body in completing the legal analysis should it disagree with legal interpretations developed by the panel, but this is not the case in the Panel Report before us.

119. In conclusion, for the reasons stated above, we *reverse* the Panel's finding, in paragraph 7.64 of the Panel Report, with respect to the interpretation of Article 14(d) of the *SCM Agreement* and find, instead, that an investigating authority may use a benchmark other than private prices in the country of provision, when it has been established that private prices of the goods in question in that country are distorted, because of the predominant role of the government in the market as a provider of the same or similar goods.

120. We emphasize, however, that when an investigating authority proceeds in this manner, it is obliged, pursuant to Article 14(d), to ensure that the alternative benchmark it uses relates or refers to, or is connected with, prevailing market conditions in the country of provision, (including price, quality, availability, marketability, transportation and other conditions of purchase or sale), with a view to determining, ultimately, whether the goods at issue were provided by the government for less than adequate remuneration.

121. We also *reverse* the Panel's consequential finding, in paragraph 7.65 of the Panel Report, that the United States acted inconsistently with Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement*, because it is predicated exclusively on the Panel's finding, which we reversed, with respect to the interpretation of Article 14(d) of the *SCM Agreement*.

122. We also find that we are unable to complete the legal analysis of whether USDOC's determination of benefit is consistent with Article 14(d) of the *SCM Agreement*. Having found that there is an insufficient factual basis to complete the legal analysis, we do not make findings on whether USDOC's determination of the existence and amount of benefit in the underlying countervailing duty investigation is consistent or inconsistent with Articles 14 and 14(d) of the

*SCM Agreement* and whether the imposition of countervailing duties based on that determination is consistent or inconsistent with Articles 10 and 32.1 of that Agreement.

## VI. Pass-Through

### A. Introduction

123. The third issue raised in this appeal is whether the Panel erred in finding that USDOC's failure to conduct a "pass-through" analysis, in respect of arm's length sales of *logs* and *lumber* by tenure-holding timber harvesters owning sawmills and producing lumber, to unrelated sawmills or lumber remanufacturers, is inconsistent with Article 10 and thus Article 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.<sup>147</sup>

124. We found above that the stumpage programs of Canadian provinces at the heart of this case provide standing timber to timber harvesters, allegedly conferring a benefit.<sup>148</sup> The standing timber eventually becomes felled trees or logs, which are processed into softwood lumber as well as remanufactured lumber products. USDOC defined the product subject to the investigation at issue as "certain softwood lumber", which includes "primary" lumber and "remanufactured" lumber.<sup>149</sup> The United States imposed countervailing duties on imports of these softwood lumber products from Canada. The pass-through issues in this appeal concern situations where the activities of harvesting standing timber, processing logs into softwood lumber, and further processing lumber into remanufactured lumber products, are *not* carried out by vertically integrated enterprises. This appeal, therefore, concerns only arm's length sales of logs and lumber by tenured timber harvesters/sawmills<sup>150</sup> to sawmills<sup>151</sup> and lumber remanufacturers<sup>152</sup>, none of which is related through common ownership or in any other way. Thus, we must examine whether a Member is required to analyze whether the subsidy conferred on products of certain enterprises in the production chain was "passed through", in arm's length transactions, to other enterprises producing the countervailed product.

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<sup>147</sup>Panel Report, para. 7.99.

<sup>148</sup>See *supra*, para. 76 of this Report.

<sup>149</sup>"Primary" lumber is lumber that is produced when a log is processed for the first time. "Remanufactured" lumber is primary lumber that undergoes some additional processing, such as cutting to odd lengths and planing.

<sup>150</sup>We use the term "tenured timber harvester/sawmill" to refer to an enterprise holding a stumpage contract that fells trees and produces logs, and also processes logs into softwood lumber.

<sup>151</sup>We use the term "sawmill" to refer to an enterprise that processes logs into softwood lumber and does not hold a stumpage contract.

<sup>152</sup>We use the term "remanufacturer" to refer to an enterprise that further processes softwood lumber into remanufactured lumber products.

125. The Panel found that:

... USDOC's failure to conduct a pass-through analysis in respect of logs sold by tenure-holding timber harvesters (whether or not also lumber producers) to unrelated sawmills producing subject softwood lumber; and in respect of lumber sold by tenure-holding harvester/sawmills to unrelated lumber re-manufacturers was inconsistent with Article 10 and thus Article 32.1 [of the] SCM Agreement, and with Article VI:3 of GATT 1994.<sup>153</sup>

126. The United States appeals this finding in part, as we explain in the next section.

B. *Scope of the Issue Appealed*

127. The United States notes that it "does *not appeal* the Panel's finding that, where the subsidy is received by independent harvesters, *i.e.*, entities that do *not* produce [softwood lumber] product[s] under investigation and operate at arm's length, a pass through analysis would be required to determine if the subsidy received by the independent harvesters was indirectly bestowed on production of softwood lumber".<sup>154</sup> Thus, the situation where tenured timber harvesters do not process logs into softwood lumber and sell at arm's length all the logs they harvest to unrelated sawmills is not before us in this appeal. We also note that Canada does not argue that a pass-through analysis is required in the absence of arm's length transactions between tenured timber harvesters, sawmills and remanufacturers.<sup>155</sup> Hence, the situation where vertically integrated enterprises, *not* operating at arm's length, harvest timber under stumpage contracts, produce softwood lumber and remanufacture lumber, is also not before us.

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<sup>153</sup>Panel Report, para. 7.99. The Panel continued, stating that, in the light of its finding, it did "not find it necessary to address Canada's pass-through claims pursuant to Articles 19.1 and 19.4 [of the] SCM Agreement". (*Ibid.*)

<sup>154</sup>United States' appellant's submission, footnote 7 to para. 5 (emphasis added), referring to Panel Report, paras. 7.94–7.95. Before the Panel, the United States had acknowledged that log sales at arm's length to sawmills by tenured timber harvesters not owning sawmills, could overstate the aggregate amount of subsidization of softwood lumber, but argued that the "vast majority of Crown timber enters harvesters' own sawmills". (Panel Report, para. 7.94) In the Panel's view, it was for the United States to submit information establishing the insignificance of arm's length transactions between tenured timber harvesters not processing logs into lumber, and unrelated sawmills. The Panel found that the United States "did not do so, and point[ed] to no factual basis in the record for its conclusion that such [pass-through] analysis was not necessary" and concluded that "in respect of the upstream log sales at issue, the US acted inconsistently with Article 10 [of the] SCM [Agreement] and Article VI:3 of GATT 1994". (*Ibid.*, para. 7.95)

<sup>155</sup>Canada's appellee's submission, paras. 8–12. Canada's responses to questioning at the oral hearing. See also, paras. 110–112 of Canada's response to Question 11 posed by the Panel at the First Panel Meeting; Panel Report, pp. A-22–A-23.



128. The United States requests us to *reverse* the Panel's finding, in paragraph 7.99 of the Panel Report, that a pass-through analysis is required with respect to sales of logs or lumber by tenured harvester/sawmills to sawmills or re-manufacturers.<sup>156</sup> This appeal thus concerns the situations where: (i) a tenured timber harvester owns a sawmill and processes some of the logs it harvests into softwood lumber, but at the same time sells at arm's length some of the logs it harvests to unrelated sawmills for processing into lumber; and (ii) a tenured timber harvester processes logs it harvests into lumber, and sells at arm's length some, or all, of the lumber it produces to lumber remanufacturers for further processing.<sup>157</sup> Having defined the scope of the pass-through issues raised in this appeal, we start our analysis with a brief account of the arguments submitted by the participants.

C. *General Interpretative Analysis of the Pass-Through Issue*

129. On appeal, the United States accepts that a pass-through analysis is required where a subsidy is bestowed *indirectly* on producers of products subject to the investigation ("subject products"). Thus, if a subsidy is received directly by an entity *other* than a producer of subject products, and that entity subsequently sells inputs to producers of subject products, the investigating authority is required to determine whether at least some of that subsidy is passed through in the sale to the producers of such products.<sup>158</sup> In other words, in such a situation, it cannot be assumed that some or all of the indirect subsidy has passed through. This situation is contrasted with that of stumpage subsidies received directly by a tenured timber harvester that owns a sawmill, and thus is also a producer of softwood lumber. According to the United States, a pass-through analysis is not required in respect of arm's length sales of *logs*, by such tenured timber harvesters who own sawmills, to unrelated sawmills.<sup>159</sup> For the United States, in such a situation, where both entities involved in the transaction produce products subject to the investigation, pass-through of the subsidy can be presumed.

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<sup>156</sup>United States' appellant's submission, para. 31.

<sup>157</sup>The United States' appeal does not include the situation where a tenured timber harvester not owning a sawmill sells logs at arm's length to sawmills producing softwood lumber. The Panel made findings on this situation in paragraph 7.99 of the Panel Report, together with findings on the situations that *are* at issue in this appeal.

<sup>158</sup>United States' response to questioning at the oral hearing.

<sup>159</sup>United States' appellant's submission, para. 39.

130. The United States further argues that both primary lumber and remanufactured lumber are products subject to the investigation, and, therefore, primary lumber is not upstream to subject products; accordingly, a pass-through analysis is not required in respect of arm's length sales of *lumber* by tenured timber harvesters who own sawmills, to unrelated remanufacturers, because both produce products subject to the investigation. According to the United States, in this situation, pass-through can also be presumed.

131. The United States finds support in Article 19.3 of the *SCM Agreement*, which permits conducting investigations on an aggregate, as opposed to company-specific, basis. According to the United States, investigations could not be conducted on an aggregate basis if pass-through analyses were required for every arm's length transaction between different producers of products subject to the investigation.<sup>160</sup> The United States submits further that Article VI:3 of the GATT 1994, and footnote 36 to Article 10 of the *SCM Agreement*, contain no obligation regarding the methodology that a Member is to use in calculating the country-wide countervailing duty rate in an *aggregate* investigation.<sup>161</sup> Indeed, the United States submits that no obligation can be found anywhere in the *SCM Agreement* requiring adjustment of a subsidy found to exist to account for the fact that certain producers of softwood lumber may not have received the subsidy, because they purchased logs and lumber inputs at arm's length from other lumber producers.<sup>162</sup>

132. Canada submits that, by not appealing the Panel's finding that a pass-through analysis is required where stumpage subsidies are received by "independent harvesters" of logs who do not own a sawmill and thus do not produce softwood lumber, the United States has accepted that a pass-through analysis is required in instances of *indirect* subsidization. Canada contends that the requirement for a pass-through analysis applies equally for arm's length sales of both *log* inputs and *lumber* inputs by tenured timber harvesters owning sawmills, to unrelated sawmills or lumber remanufacturers. In Canada's view, by failing to conduct a pass-through analysis with respect to these categories of transactions, the United States countervailed subsidies, the existence and amount of which it presumed, instead of determined.<sup>163</sup>

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<sup>160</sup>United States' response to questioning at the oral hearing.

<sup>161</sup>United States' appellant's submission, para. 43.

<sup>162</sup>*Ibid.*, paras. 31 and 46–47.

<sup>163</sup>Canada's appellee's submission, para. 65.

133. Canada argues that Article 1.1 of the *SCM Agreement* requires, also in the case of indirect subsidization, that investigating authorities establish the existence of both a financial contribution by a government (albeit indirect), and the conferral of a benefit, in relation to the product on which countervailing duties are imposed.<sup>164</sup> Canada notes that Article VI:3 of the GATT 1994, and Articles 10 and 32.1 of the *SCM Agreement*, do not permit subsidization to be presumed in respect of products. Nor do they permit imposing countervailing duties in excess of the subsidy found to exist for a particular product, even if an investigation is conducted on an aggregate (country-wide) basis, as contemplated by Article 19.3 of the *SCM Agreement*.<sup>165</sup> Thus the requirement to conduct a pass-through analysis is not avoided simply because there is a right to conduct an investigation on an aggregate basis. For these reasons, Canada requests us to *uphold* the Panel's finding that, by failing to establish that the benefit of the financial contribution was passed through, at least in part, from the upstream producers of log and lumber inputs, to the downstream producers of the lumber products subject to the investigation, the United States imposed countervailing duties contravening Articles 10 and 32.1 of the *SCM Agreement*, and Article VI:3 of the GATT 1994.<sup>166</sup>

134. We now examine the pass-through issue before us. At the outset, we observe that provisions in both the GATT 1994 and the *SCM Agreement* are relevant to this dispute. We note the Appellate Body's earlier ruling that a provision of an agreement included in Annex 1A of the *WTO Agreement* (including the *SCM Agreement*), and a provision of the GATT 1994, that have identical coverage, both apply, but that the provision of the agreement that "deals specifically, and in detail" with a question should be examined first.<sup>167</sup> The Appellate Body has also ruled that "countervailing duties may only be imposed in accordance with the provisions of Part V of the *SCM Agreement* and Article VI of the GATT 1994, taken together"<sup>168</sup>, and that "[i]f there is a conflict between the provisions of the *SCM Agreement* and Article VI of the GATT 1994 ... the provisions of the *SCM Agreement* would prevail as a result of the general interpretative note to Annex 1A."<sup>169</sup> No conflict between Articles 10 and 32.1 of the *SCM Agreement* on the one hand, and Article VI:3 of the GATT 1994 on the other hand, is alleged in this appeal, nor do we see any such conflict. Therefore, the requirements of these provisions of the *SCM Agreement* and the GATT 1994 apply on a cumulative basis.

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<sup>164</sup>Canada's appellee's submission, para. 68, referring to Article 1.1 of the *SCM Agreement*.

<sup>165</sup>*Ibid.*, paras. 9–10 and 77–78.

<sup>166</sup>*Ibid.*, paras. 55 ff and 80.

<sup>167</sup>Appellate Body Report, *EC – Bananas III*, para. 204.

<sup>168</sup>Appellate Body Report, *Brazil – Desiccated Coconut*, DSR 1997:I, 167, at 181. (original italics; underling added)

<sup>169</sup>*Ibid.*

135. Article 10 of the *SCM Agreement* provides that:

Members shall take all necessary steps to ensure that the imposition of a countervailing duty<sup>36</sup> on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement. Countervailing duties may only be imposed pursuant to investigations initiated and conducted in accordance with the provisions of this Agreement and the Agreement on Agriculture. (footnotes omitted in part)

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<sup>36</sup> The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise, as provided for in paragraph 3 of Article VI of GATT 1994.<sup>170</sup>

According to Article 32.1 of the *SCM Agreement*:

[n]o specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement. (footnote omitted)

Article VI:3 of the GATT 1994 reads:

[n]o countervailing duty shall be levied on any product of the territory of a Member imported into the territory of another Member in excess of an amount equal to the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product in the country of origin or exportation... The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export or any merchandise.

136. According to Canada, the United States acted inconsistently with: (i) Article 10 of the *SCM Agreement*, by failing to "take all necessary steps" to determine subsidization in accordance with the provisions of the *SCM Agreement* and Article VI:3 of the GATT 1994; (ii) Article 32.1 of that Agreement, by taking action against a subsidy not in accordance with the provisions of the GATT 1994, as interpreted by the *SCM Agreement*; and (iii) Article VI:3 of the GATT 1994, by imposing duties without establishing the existence of indirect subsidization and failing to ensure that countervailing measures are not in excess of the subsidy found to exist.

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<sup>170</sup> We also take note of Article 19.4 of the *SCM Agreement*, which provides:

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. (footnote omitted)

137. We observe that, in this case, Canada's claims under Article 10 and footnote 36 thereto<sup>171</sup>, and Article 32.1 of the *SCM Agreement*, are largely derivative of its claim under Article VI:3 of the GATT 1994; Canada alleges that a violation by the United States of the requirements in Article VI:3 of the GATT 1994 would necessarily result also in violations of its obligations under Article 10 and footnote 36 thereto, and Article 32.1 of the *SCM Agreement*. Therefore, our discussion focuses first on whether Article VI:3 of the GATT 1994 requires a pass-through analysis, and if so, under what circumstances.

138. We note that, if we were to find that USDOC's final determination and the imposition of countervailing duties on Canadian imports of softwood lumber products contravene the requirements of Article VI:3 of the GATT 1994, the United States necessarily would *not* have "take[n] all necessary steps to ensure that the imposition of a countervailing duty ... is in accordance with the provisions of Article VI of GATT 1994", as required by Article 10 of the *SCM Agreement*. The "specific action against a subsidy" taken by the United States would also *not*, as required by Article 32.1 of the *SCM Agreement*, be "in accordance with the provisions of GATT 1994, as interpreted by the [SCM] Agreement". Consequently, any inconsistency of the United States' imposition of countervailing duties on Canadian imports of softwood lumber products with Article VI:3 of the GATT 1994, would necessarily render this measure inconsistent *also* with Articles 10 and 32.1 of the *SCM Agreement*.

139. The Panel described the pass-through problem as follows: "[w]here the subsidies at issue are received by someone other than the producer of the investigated product, the question arises whether there is subsidization in respect of that product."<sup>172</sup> In addressing this question, we note that Article VI:3 prohibits levying countervailing duties on an imported product "*in excess* of an amount equal to the estimated ... subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product". (emphasis added) According to Article VI:3, countervailing duties are "levied for the purpose of offsetting ... subsid[ies] bestowed, *directly or indirectly*, upon the *manufacture, production or export* of any *merchandise*". (emphasis added) The definition of the term "countervailing duties" in footnote 36 to Article 10 of the *SCM Agreement* is along the same lines.

140. The phrase "subsid[ies] bestowed ... *indirectly*", as used in Article VI:3, implies that financial contributions by the government to the production of *inputs* used in manufacturing products subject to an investigation are not, in principle, excluded from the amount of subsidies that may be offset

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<sup>171</sup>The definition of "countervailing duties" in footnote 36 to Article 10 of the *SCM Agreement* echoes the definition of that term in Article VI:3 of the GATT 1994.

<sup>172</sup>Panel Report, para. 7.85.

through the imposition of countervailing duties on the *processed product*. Where the producer of the input is not the same entity as the producer of the processed product, it cannot be presumed, however, that the subsidy bestowed on the input passes through to the processed product. In such case, it is necessary to analyze to what extent subsidies on inputs may be included in the determination of the total amount of subsidies bestowed upon processed products. For it is only the subsidies determined to have been granted upon the *processed products* that may be offset by levying countervailing duties on those products.

141. In our view, it would not be possible to determine whether countervailing duties levied on the processed product are *in excess* of the amount of the total subsidy accruing to that product, without establishing whether, and in what amount, subsidies bestowed on the producer of the input flowed through, downstream, to the producer of the product processed from that input. Because Article VI:3 permits *offsetting*, through countervailing duties, no more than the "subsidy determined to have been granted ... directly or indirectly, on the manufacture [or] production ... of such *product*", it follows that Members must not impose duties to offset an amount of the input subsidy that has *not* passed through to the countervailed processed products. It is only the amount by which an indirect subsidy granted to producers of inputs flows through to the processed product, together with the amount of subsidy bestowed directly on producers of the processed product, that may be offset through the imposition of countervailing duties. The definition of "countervailing duties" in footnote 36 to Article 10 of the *SCM Agreement* supports this interpretation of the requirements of Article VI:3 of the GATT 1994.

142. This interpretation is also borne out by the general definition of a "subsidy" in Article 1 of the *SCM Agreement*. According to that definition, a subsidy shall be deemed to exist only if there is both a *financial contribution* by a government within the meaning of Article 1.1(a)(1)<sup>173</sup>, and a *benefit* is thereby conferred within the meaning of Article 1.1(b).<sup>174</sup> If countervailing duties are intended to offset a subsidy granted to the producer of an input product, but the duties are to be imposed on the *processed product* (and not the input product), it is *not* sufficient for an investigating authority to establish only for the *input* product the existence of a financial contribution and the conferral of a benefit to the input producer. In such a case, the cumulative conditions set out in Article 1 must be established with respect to the processed product, especially when the producers of the input and the processed product are not the same entity. The investigating authority must establish that a *financial contribution* exists; and it must also establish that the benefit resulting from the subsidy has passed

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<sup>173</sup>Or income or price support within the meaning of Article 1.1(a)(2).

<sup>174</sup>Appellate Body Report, *Brazil – Aircraft*, para. 157.

through, at least in part, from the input downstream, so as to *benefit* indirectly the processed product to be countervailed.

143. In this respect, the Appellate Body's interpretation of the term "benefit" in *Canada – Aircraft* is useful:

A "benefit" does not exist in the abstract, but must be received and enjoyed by a beneficiary or a recipient. Logically, a "benefit" can be said to arise only if a person, natural or legal, or a group of persons, has in fact received something. The term "benefit", therefore, implies that there must be a recipient.<sup>175</sup>

Thus, for a potentially countervailable subsidy to exist, there must be a financial contribution by the government that confers a benefit to a *recipient*. Where a subsidy is conferred on input products, and the countervailing duty is imposed on processed products, the initial recipient of the subsidy and the producer of the eventually countervailed product, may not be the same. In such a case, there is a *direct recipient* of the benefit—the producer of the *input* product. When the input is subsequently processed, the producer of the *processed product* is an *indirect recipient* of the benefit—provided it can be established that the benefit flowing from the input subsidy is passed through, at least in part, to the processed product. Where the input producers and producers of the processed products operate at *arm's length*, the pass-through of input subsidy benefits from the direct recipients to the indirect recipients downstream cannot simply be presumed; it must be established by the investigating authority. In the absence of such analysis, it cannot be shown that the essential elements of the subsidy definition in Article 1 are present in respect of the *processed product*. In turn, the right to impose a countervailing duty on the processed product for the purpose of offsetting an input subsidy, would not have been established in accordance with Article VI:3 of the GATT 1994, and, consequently, would also not have been in accordance with Articles 10 and 32.1 of the *SCM Agreement*.

144. The panel report, adopted under GATT 1947, in *US – Canadian Pork* reasoned along the same lines under Article VI:3. That panel dealt with a situation where Canada had granted subsidies to swine producers, while the United States imposed countervailing duties on imports of pork products.<sup>176</sup> The panel noted that:

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<sup>175</sup>Appellate Body Report, *Canada – Aircraft*, para. 154.

<sup>176</sup>GATT Panel Report, *US – Canadian Pork*, para. 4.3. The panel noted that swine producers and pork producers were separate industries operating at arm's length and that the subsidies granted to swine producers could have only indirectly bestowed a subsidy on the production of pork.

Article VI:3 stipulates that a countervailing duty levied on any product shall not exceed an amount equal to the subsidy granted directly or indirectly on the production of "such product". *According to this clear wording, the United States may impose a countervailing duty on pork only if a subsidy has been determined to have been bestowed on the production of pork;* the mere fact that trade in pork is affected by the subsidies granted to producers of swine is not sufficient.<sup>177</sup> (emphasis added)

145. It is also useful to refer to *US – Countervailing Measures on Certain EC Products*, where the Appellate Body stated that:

... under Article VI:3 of the GATT 1994, investigating authorities, before imposing countervailing duties, must ascertain the precise amount of a subsidy attributed to the imported products under investigation. In furtherance of this obligation, Article 10 of the *SCM Agreement* provides that Members must "ensure" that duties levied for the purpose of offsetting a subsidy are imposed only "in accordance with" the provisions of Article VI:3 of the GATT 1994 and the *SCM Agreement*. Moreover, Article 19.4 of the *SCM Agreement*, consistent with the language of Article VI:3 of the GATT 1994, requires that "[n]o countervailing duty shall be levied on any imported product in excess of the amount of the *subsidy found to exist*". ... In sum, these provisions set out the obligation of Members to limit countervailing duties to the amount and duration of the subsidy found to exist by the investigating authority.<sup>178</sup> (original italics; underlining added; footnotes omitted)

146. In the light of the above, GATT/WTO dispute settlement practice is consistent with and confirms our interpretation that, where countervailing duties are used to offset subsidies granted to producers of input products, while the duties are to be imposed on *processed* products, and where input producers and downstream processors operate at *arm's length*, the investigating authority must establish that the benefit conferred by a financial contribution directly on input producers is passed through, at least in part, to producers of the processed product subject to the investigation. Therefore, we agree with the Panel that:

If it is not demonstrated that there has been such a pass-through of subsidies from the subsidy recipient to the producer or exporter of the product, then it cannot be said that subsidization in respect of that product, in the sense of Article 10, footnote 36, and Article VI:3 of GATT 1994, has been found.<sup>179</sup>

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<sup>177</sup>GATT Panel Report, *US – Canadian Pork*, para. 4.6.

<sup>178</sup>Appellate Body Report, *US – Countervailing Measures on Certain EC Products*, para. 139.

<sup>179</sup>Panel Report, para. 7.91.



147. This would mean that a financial contribution conferring a benefit on tenure-holding harvesters of *timber* could be offset by imposing countervailing duties on exports of *timber*—or, in other words, *logs*—without carrying out a pass-through analysis.<sup>180</sup> However, if countervailing duties on *softwood lumber products* are meant to offset a financial contribution received by and conferring a benefit directly on producers of *timber/logs*, the investigating authority must establish that those benefits have been passed through, at least in part, from producers of logs to producers of softwood lumber (and remanufactured lumber), which are the products subject to the investigation.

D. *Conduct of the Investigation on an Aggregate Basis*

148. Before proceeding further, we address the argument of the United States that Article 19.3 of the *SCM Agreement* contemplates the conduct of an investigation on an *aggregate* basis and that, therefore, the approach it took in this investigation in calculating the total subsidy and the country-wide countervailing duty rate is consistent with the *SCM Agreement* and the GATT 1994. The United States argues that no pass-through analysis was required with respect to arm's length sales of logs and lumber by tenured timber harvesters owning sawmills, to unrelated sawmills and remanufacturers, because Article 19.3 recognizes that exporters who are not investigated individually may nevertheless be subject to countervailing duties; accordingly, it is not necessary, in an aggregate investigation, to determine whether individual producers or exporters actually received subsidies.<sup>181</sup>

149. The United States submits that no pass-through analysis was required in this aggregate investigation because the total subsidy from the sawmills' stumpage inputs (that is, the total subsidy bestowed on logs entering sawmills) is known, and can be used in its entirety as the appropriate *numerator* in the calculation of a country-wide *ad valorem* countervailing duty rate. This numerator is then spread equally over a *denominator*, consisting of the total amount of sales of the softwood lumber products subject to this investigation, produced by both "first" sawmills and remanufacturers. According to the United States, therefore, Canada's pass-through claims relate, in fact, to the calculation of the countervailing duty rate on an aggregate basis, rather than to the existence of the subsidy.<sup>182</sup> For the United States, an expedited review under Article 19.3 is the appropriate avenue for exporters that have not been investigated individually to establish that they did not receive countervailable benefits and thus that the country-wide countervailing duty rate is not appropriate for that exporter.<sup>183</sup>

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<sup>180</sup> Provided that all the other conditions for using countervailing measures as set forth in Part V of the *SCM Agreement* are met.

<sup>181</sup> United States' appellant's submission, paras. 31 and 45–47.

<sup>182</sup> United States' response to questioning at the oral hearing.

<sup>183</sup> United States' appellant's submission, footnote 60 to para. 46.

150. Canada contends that the fact that the investigation at issue was conducted on an aggregate basis does not excuse USDOC from establishing the existence and amount of the alleged subsidy to producers of the investigated products, consistently with Article VI:3 of the GATT 1994 and Articles 10 and 32.1 of the *SCM Agreement*.<sup>184</sup> Canada acknowledges that Article 19.3 permits aggregate investigations, but, in Canada's view, the fact that the investigation at issue was conducted on an aggregate basis cannot absolve the United States of the requirement to establish the existence of a subsidy in respect of the products of sawmills and lumber remanufacturers that purchased log and lumber inputs at arm's length. Finally, Canada points to substantial record evidence demonstrating the existence of arm's length sales of logs and lumber by tenured timber harvesters/sawmills to unrelated sawmills not holding stumpage rights and to remanufacturers.<sup>185</sup>

151. In discussing these arguments, we note, at the outset, that information about how USDOC calculated the total amount of subsidy and the country-wide countervailing duty rate on an aggregate basis in the investigation at issue may be relevant in deciding the pass-through issues before us. However, we are mindful that the Panel declined to rule on Canada's claims against certain aspects of the method applied by USDOC in these calculations, and that these claims are not before us in this appeal.<sup>186</sup>

152. We agree with the United States that Article 19 of the *SCM Agreement* authorizes Members to perform an investigation on an *aggregate* basis.<sup>187</sup> Article 19.3 requires that countervailing duties "shall be levied, in the appropriate amounts in each case, on a *non-discriminatory basis* on imports of such product from *all sources* found to be subsidized and causing injury".<sup>188</sup> (emphasis added) Article 19.3 further provides that "[a]ny exporter whose exports are subject to a definitive

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<sup>184</sup>Canada's appellee's submission, paras. 11 and 78 *ff*.

<sup>185</sup>*Ibid.*, para. 61.

<sup>186</sup>Canada's other appellant's submission, para. 7; United States' appellant's submission, paras. 1–6.

<sup>187</sup>In response to questioning at the oral hearing, Canada did not contest that Article 19 contemplates conducting countervailing duty investigations on an aggregate basis. However, Canada maintained that the aggregate investigation leading to the final determination and imposition of countervailing duties in this case is inconsistent with the *SCM Agreement*.

<sup>188</sup>Article 19.3 of the *SCM Agreement* reads:

When a countervailing duty is imposed in respect of any product, such countervailing duty shall be levied, in the appropriate amounts in each case, on a non-discriminatory basis on imports of such product from all sources found to be subsidized and causing injury, except as to imports from those sources which have renounced any subsidies in question or from which undertakings under the terms of this Agreement have been accepted. Any exporter whose exports are subject to a definitive countervailing duty but who was not actually investigated for reasons other than a refusal to cooperate, shall be entitled to an expedited review in order that the investigating authorities promptly establish an individual countervailing duty rate for that exporter.

countervailing duty *but who was not actually investigated* ... shall be entitled to an expedited review in order that the investigating authorities promptly establish an *individual* countervailing duty rate for that exporter." (emphasis added) Accordingly, countervailing duties shall be imposed, on a non-discriminatory basis, on *all sources* found to be subsidized, although *no prior* investigation of all *individual* exporters or producers is required by Article 19. This implies that countervailing duties may be imposed on imports of products subject to the investigation, even though specific shipments from exporters or producers that were not investigated individually might not at all be subsidized, or not subsidized to an extent equal to a countervailing duty rate calculated on an aggregate (country-wide) basis.<sup>189</sup>

153. We also observe that Article 19.4 requires the calculation of countervailing duties in terms of "subsidization *per unit* of the subsidized and exported product".<sup>190</sup> (emphasis added) In our view, the reference to calculation of countervailing duty rates on a per unit basis under Article 19.4 supports the interpretation that an investigating authority is permitted to calculate the total amount and the rate of subsidization on an aggregate basis.

154. We note, however, that country-wide or company-specific countervailing duty rates may be imposed under Part V of the *SCM Agreement* only *after* the investigating authority has determined the existence of subsidization, injury to the domestic industry, and a causal link between them. In other words, the fact that Article 19 permits the imposition of countervailing duties on imports from producers or exporters not investigated individually, does not exonerate a Member from the obligation to determine the total amount of subsidy and the countervailing duty rate consistently with the provisions of the *SCM Agreement* and Article VI of the GATT 1994. In this respect, as the panel in *US – Countervailing Measures on Certain EC Products* correctly stated, the "determination of a benefit (as a component of subsidization) must be made *before* countervailing duties can be

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<sup>189</sup>We note, in this respect, as pointed out by the European Communities, that the first sentence of Article 6.10 of the *Anti-Dumping Agreement* requires, as a rule, a determination of an individual margin of dumping for each known producer or exporter of the product under investigation, unless this is rendered impracticable due to the high number of producers and exporters or of the types of products involved. If that is the case, the second sentence of Article 6.10 permits investigating authorities to limit the investigation to a statistically valid sample, or the largest percentage of the volume of exports that can reasonably be investigated. By contrast, the *SCM Agreement* does not contain a similar rule requiring Members, in principle, to determine an individual margin of subsidization for each known producer or exporter of the subsidized good. (European Communities' third participant's submission, paras. 45–47)

<sup>190</sup>Article 19.4 of the *SCM Agreement* provides:

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. (footnote omitted)

imposed."<sup>191</sup> Therefore, turning to the issue in this case, before being entitled to impose countervailing duties on a processed product, for the purpose of offsetting an input subsidy, a Member must first determine, in accordance with Article 1.1, that a financial contribution exists, and that the benefit conferred directly on the input producer has been passed through, at least in part, to the producer of the processed product. We reject, therefore, the argument of the United States that the pass-through issues arising in this appeal relate merely to the method used by USDOC, in this aggregate investigation, in calculating the total amount of subsidy and the countervailing duty rate.

E. *Sales of Logs at Arm's Length by Tenured Timber Harvesters/Sawmills to Unrelated Lumber Producers*

155. Having thus dealt with the participants' arguments relating to Article 19 of the *SCM Agreement*, we turn to the question whether a pass-through analysis was required, in the light of our general interpretation above, with respect to the categories of arm's length transactions at issue in this appeal. As noted above, this appeal concerns, *first*, the situation where a tenured timber harvester owns a sawmill and processes some of the logs it harvests into softwood lumber, but, at the same time, sells at arm's length some of the logs it harvests to other, unrelated sawmills for processing into lumber; and, *secondly*, the situation where a tenured timber harvester owns a sawmill and processes some of the logs it harvests into softwood lumber, but, at the same time, sells at arm's length some or all of the lumber it produces to lumber remanufacturers for further processing. We also note that it is undisputed between the participants that the United States did not carry out any pass-through analyses in the investigation at issue.<sup>192</sup>

156. In the first situation, the question is whether a pass-through analysis is required with respect to arm's length sales of *logs* by harvesters who own sawmills to unrelated sawmills for further processing. For this category of arm's length transactions, the United States argues that no pass-through analysis is required, because the tenured harvester/sawmill processes *some* logs into softwood *lumber* in its own sawmill, and is thus a producer of the product subject to the

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<sup>191</sup>Panel Report, *US – Countervailing Measures on Certain EC Products*, para. 7.44. (emphasis added) In the same vein, the Appellate Body held in *EC – Bed Linen (Article 21.5 – India)* that, under the *Anti-Dumping Agreement*:

Members have the right to impose and collect anti-dumping duties only *after* the completion of an investigation in which it *has been established* that the requirements of dumping, injury, and causation "*have been fulfilled*". In other words, the right to impose anti-dumping duties under Article 9 is a *consequence* of the prior determination of the existence of dumping margins, injury, and a causal link. (original italics)

(Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, para. 123)

<sup>192</sup>United States' and Canada's responses to questioning at the oral hearing; Panel Report, para. 7.93.

investigation.<sup>193</sup> We are not persuaded that the fact that the harvester/sawmill processes in-house *some* of the logs it harvests into softwood lumber is relevant in determining whether a pass-through analysis is necessary.

157. As we mentioned above, the United States acknowledges that a pass-through analysis is required where a tenured "independent" harvester, which does not own a sawmill and thus does not produce softwood lumber, sells *logs* at arm's length to unrelated sawmills. We do not see why the mere fact that a tenured harvester owns—or does not own—a sawmill, should affect whether a pass-through analysis is necessary with respect to logs sold at arm's length. We understand the United States to argue that benefits, initially attached to logs, but retained by a harvester/sawmill when the logs are sold in arm's length transactions to unrelated buyers, may be used by such a vendor to "cross-subsidize" its own production of softwood lumber processed in-house from other logs. We agree, in the abstract, that a transfer of benefits from logs sold in arm's length transactions to lumber produced in-house from different logs *is possible* for a harvester that owns a sawmill. But whether, *in fact*, this occurs depends on the particular case under examination. In any event, these arm's length sales at issue concern logs, which are *not* products subject to the investigation. Accordingly, in cases where logs are sold by a harvester/sawmill in arm's length transactions to unrelated sawmills, it may not be assumed that benefits attaching to the *logs* (non-subject products) automatically pass through to the *lumber* (the subject product) produced by the harvester/sawmill. A pass-through analysis is thus required in such situations.

158. Indeed, we disagree with the proposition that, as long as an enterprise produces products subject to an investigation, *any* benefits accruing to the same enterprise from subsidies conferred on any different products it produces (which are *not* subject to that investigation), could be included, without need of a pass-through analysis, in the total amount of subsidization found to exist for the investigated product, and that may be offset by levying countervailing duties on that product.<sup>194</sup> We conclude that the pass-through of the benefit cannot be presumed with respect to arm's length sales of logs by harvesters, who own sawmills, to unrelated sawmills, for further processing.

159. For these reasons, we *uphold* the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *logs* by tenured harvesters/sawmills to unrelated sawmills is inconsistent with Articles 10 and 32.1 of the *SCM Agreement*, and Article VI:3 of the GATT 1994.

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<sup>193</sup>Canada does not argue that a pass-through analysis is required in respect of logs harvested by a tenured harvester/sawmill and subsequently processed *in-house* into softwood lumber.

<sup>194</sup>United States' responses to questioning at the oral hearing.

F. *Sales of Lumber at Arm's Length by Tenured Timber Harvesters/Sawmills to Unrelated Lumber Remanufacturers*

160. We turn now to the second pass-through situation at issue, which concerns tenured timber harvesters that own or are related to sawmills, process the logs they harvest into softwood lumber, and sell lumber to unrelated remanufacturers for further processing. The question here is whether a pass-through analysis is required in respect of these arm's length sales of softwood lumber.

161. In this situation, the products of *both* the harvesters/sawmills and the remanufacturers are subject to the investigation. It is uncontested that "certain softwood lumber" includes "primary" lumber produced by sawmills and "remanufactured" lumber produced by remanufacturers. We also note that USDOC chose to conduct this investigation on an *aggregate* basis. Canada accepts that aggregate investigations are contemplated by Article 19 of the *SCM Agreement*, but takes issue with how USDOC calculated the total amount of the subsidy and the countervailing duty rate in the investigation at issue. We have confirmed above that performing investigations on an aggregate basis is permitted under the *SCM Agreement* and the GATT 1994, and we have observed that calculation issues are beyond the scope of this appeal.

162. The Panel reasoned in this respect:

... some portion of any subsidy from stumpage is attributable to the harvester/sawmill's production of the lumber for re-manufacturing and some is attributable to the other products (including lumber) that the harvester/sawmill produces. Here, if the subsidies attributable to the lumber for re-manufacturing are not passed through to the re-manufacturer that purchases it, then those subsidies should not be included in the numerator of the subsidization equation, as in this situation it is the re-manufactured product, not the upstream lumber product, that is the subject merchandise under investigation.<sup>195</sup>

163. In our view, the Panel's reasoning confuses pass-through questions that may arise when individual enterprises are investigated, with questions arising in the calculation of the total amount and the rate of subsidization on an aggregate basis. The question before us is whether it is necessary to analyze whether benefits have been passed through from one product subject to the investigation (primary softwood lumber) to another product subject to that investigation (remanufactured softwood lumber). Once it has been established that benefits from subsidies received by producers of *non-subject* products (that is, inputs) have passed through to producers of *subject* products (primary and remanufactured softwood lumber), we do not see why a further pass-through analysis *between* producers of subject products should be required in an investigation conducted on an aggregate basis.

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<sup>195</sup>Panel Report, para. 7.97.

In this situation, it is not necessary to calculate precisely how subsidy benefits are divided up between the producers of subject products in order to calculate, on an aggregate basis, the total amount of subsidy and the country-wide countervailing duty rate for those subject products.

164. It is true, as pointed out by the Panel, that a particular shipment of remanufactured softwood lumber entering the United States might not be subsidized at all, especially if the remanufacturer purchased the primary lumber it processed at arm's length. It is also far from certain that every single shipment of primary lumber will, in fact, be subsidized, or, even if it is, that it is subsidized at the average *ad valorem* country-wide rate determined in an aggregate investigation. Nevertheless, as we indicated above, Article 19 of the *SCM Agreement* contemplates the imposition of a country-wide countervailing duty rate, even when a specific exporter is not subsidized, or when that country-wide rate does not match the precise amount of subsidization benefiting a specific shipment. And as mentioned above, the possibility for an exporter not investigated individually to request, pursuant to Article 19.3, an expedited review to establish an individual countervailing duty rate for that exporter, also confirms that a country-wide duty rate may, in principle, be imposed. However, the pass-through question would not be the same when determining, through the review procedure provided for in Article 19.3, an individual countervailing duty rate for the exporter that requested the review. In such a review, it is likely that a pass-through analysis would be required to determine whether input subsidies on logs, having passed through to the production of softwood lumber inputs, have passed through *also* to remanufactured lumber produced from those inputs by the *particular exporter*.<sup>196</sup>

165. For these reasons, we *reverse* the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *lumber* by tenured harvesters/sawmills to unrelated remanufacturers is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.

166. Finally, we note that the Panel's findings, in paragraph 7.99 of the Panel Report, are *not appealed* to the extent that they refer to the Panel's reasoning in paragraphs 7.94–7.95.<sup>197</sup> Accordingly, we do not address the Panel's finding that USDOC's failure to conduct a pass-through

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<sup>196</sup>In an aggregate investigation, by contrast, the correct calculation of the countervailing duty rate would depend on *matching* the elements taken into account in the numerator with the elements taken into account in the denominator. For example, assuming that the numerator would represent the total amount of subsidy determined on the basis of logs entering sawmills, this numerator would have to be spread over a denominator consisting of the total amount of products processed from those logs in order to accurately calculate a country-wide *ad valorem* countervailing duty rate to be imposed on lumber imports.

We note, however, that the Panel declined to rule on Canada's claims regarding USDOC's subsidy calculation in the investigation underlying this dispute and that these findings are not before us on appeal. (See *supra*, para. 151)

<sup>197</sup>See *supra*, para. 127.

analysis in respect of sales of logs to unrelated lumber producers by tenured timber harvesters not owning sawmills, and thus not producing softwood lumber products subject to the investigation, is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.

## VII. Findings and Conclusions

167. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the Panel's finding, in paragraph 7.30 of the Panel Report, that USDOC's "[d]etermination that the Canadian provinces are providing a financial contribution in the form of the provision of a good by providing standing timber to the timber harvesters through the stumpage programmes" is not inconsistent with Article 1.1(a)(1)(iii) of the *SCM Agreement*;
- (b) reverses the Panel's finding, in paragraph 7.64 of the Panel Report, with respect to the interpretation of Article 14(d) of the *SCM Agreement*, and finds, instead, that an investigating authority may use a benchmark other than private prices in the country of provision, provided that:
  - (i) the investigating authority has established that private prices of the goods in question in the country of provision are distorted, because of the predominant role of the government in the market as a provider of the same or similar goods; and
  - (ii) when the investigating authority proceeds in this manner, it ensures that the alternative benchmark relates or refers to, or is connected with, prevailing market conditions in the country of provision (including price, quality, availability, marketability, transportation and other conditions of purchase or sale);
- (c) reverses the Panel's consequential finding, in paragraph 7.65 of the Panel Report, that the United States acted inconsistently with Articles 10, 14, 14(d) and 32.1 of the *SCM Agreement* with respect to USDOC's determination of the existence and amount of benefit in the underlying countervailing duty investigation;



- (d) finds, however, that there is not a sufficient factual basis to complete the analysis as to whether, under Article 14(d) of the *SCM Agreement*, USDOC was justified in using a benchmark other than private prices in Canada, and as to whether such benchmark relates or refers to, or is connected with, prevailing market conditions in Canada, (including price, quality, availability, marketability, transportation and other conditions of purchase or sale), and, therefore, does not make findings on whether USDOC's determination of the existence and amount of benefit in the underlying countervailing duty investigation is consistent or inconsistent with Articles 14 and 14(d) of the *SCM Agreement*, or on whether the imposition of countervailing duties based on that determination is consistent or inconsistent with Articles 10 and 32. 1 of the *SCM Agreement*;
- (e) upholds the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *logs* by tenured harvesters/sawmills to unrelated sawmills is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994;
- (f) reverses the Panel's finding, in paragraph 7.99 of the Panel Report, that USDOC's failure to conduct a pass-through analysis in respect of arm's length sales of *lumber* by tenured harvesters/sawmills to unrelated remanufacturers is inconsistent with Articles 10 and 32.1 of the *SCM Agreement* and Article VI:3 of the GATT 1994.

168. The Appellate Body *recommends* that the DSB request the United States to bring its measure, which has been found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with the *SCM Agreement* and the GATT 1994, into conformity with its obligations under those Agreements.

Signed in the original at Geneva this 18th day of December 2003 by:

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Luiz Olavo Baptista  
Presiding Member

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John Lockhart  
Member

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Giorgio Sacerdoti  
Member

ANNEX 1

**WORLD TRADE  
ORGANIZATION**

**WT/DS257/8**  
24 October 2003

(03-5606)

Original: English

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

Notification of an Appeal by the United States  
under paragraph 4 of Article 16 of the Understanding on Rules  
and Procedures Governing the Settlement of Disputes (DSU)

The following notification, dated 21 October 2003, sent by the United States to the Dispute Settlement Body (DSB), is circulated to Members. This notification also constitutes the Notice of Appeal, filed on the same day with the Appellate Body, pursuant to the *Working Procedures for Appellate Review*.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review*, the United States hereby notifies its decision to re-file its appeal to the Appellate Body of certain issues of law covered in the Report of the Panel on *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* (WT/DS257/R) and certain legal interpretations developed by the Panel.

1. The United States seeks review by the Appellate Body of the Panel's legal conclusion that the determination of the U.S. Department of Commerce ("USDOC") of the existence and amount of benefit to the producers of the subject merchandise was inconsistent with Articles 14 and 14(d) of the *WTO Agreement on Subsidies and Countervailing Measures* ("SCM Agreement"), and that therefore the imposition of countervailing duties on the basis of that determination was inconsistent with Articles 14, 14(d), 10, and 32.1 of the SCM Agreement. (Panel Report, paras. 7.65 and 8.1(b).) These findings are in error, and are based on erroneous findings on issues of law and related legal interpretations, including, for example,

- (a) that "market" conditions in the country of provision within the meaning of Article 14(d) are simply "prevailing" conditions or conditions "as can be found"; therefore, nothing in the text of Article 14(d) justifies disregarding prices in the country of provision on the grounds that they were distorted or did not reflect the fair market value of the goods provided;<sup>198</sup>

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<sup>198</sup> See e.g., para. 7.51.

- (b) that even in cases where the impact of the government's influence due to its provision of goods is "substantial or determinative of conditions in the private market," there is nevertheless a "market" in the sense of Article 14(d) of the SCM Agreement;<sup>199</sup>
- (c) that the use of U.S. prices as the basis for establishing the benchmark for the determination of benefit on the grounds that private prices in Canada were distorted by the provincial governments' financial contributions is inconsistent with Article 14(d) of the SCM Agreement.<sup>200</sup>

2. The United States seeks review by the Appellate Body of the Panel's legal conclusion that the lack of a "pass-through" analysis with respect to transactions for log and lumber inputs between producers of the subject merchandise was inconsistent with Article 10 of the SCM Agreement and Article VI:3 of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994"), and that therefore the U.S. imposition of countervailing duties was inconsistent with Articles 10 and 32.1 of the SCM Agreement and Article VI:3 of the GATT 1994 (paras. 7.99 and 8.1(c)). These findings are in error, and are based on erroneous findings on issues of law and related legal interpretations, including, for example,

- (a) that where the lumber producer who receives the subsidy sells logs or lumber to other lumber producers, a pass-through analysis is required to determine the total subsidy to production of the subject merchandise;<sup>201</sup>
- (b) that the USDOC's failure to conduct a pass-through analysis with respect to transactions between producers of the subject merchandise was itself inconsistent with Article 10 and thus Article 32.1 of the SCM Agreement, and with Article VI:3 of the GATT 1994.<sup>202</sup>

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<sup>199</sup> See e.g., paras. 7.58 and 7.60.

<sup>200</sup> See e.g., para. 7.64.

<sup>201</sup> See e.g., paras. 7.97 and 7.98.

<sup>202</sup> See e.g., para. 7.99.