

ANNEX B

PARTIES' RESPONSES TO QUESTIONS FROM THE SECOND MEETING

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ANNEX B-1

RESPONSES OF CANADA TO QUESTIONS POSED IN THE CONTEXT OF THE SECOND SUBSTANTIVE MEETING OF THE PANEL

(26 August 2003)

A. GENERAL QUESTIONS

To Canada:

85. In response to Question 1 of the Panel, Canada restated its claims. The Panel's understanding is that the claims contained in this restatement are the only claims that are before the Panel (Articles 5.2, 5.3, 5.8, 2.6, 2.4, 2.4.2, 2.2.1.1, 2.2.2, 2.2, 1, 9.3, and 18.1 of the *AD Agreement* as well as GATT 1994 Articles VI:1 and VI:2 – sequencing as per Canada's response to Question 1 of the Panel). Could Canada please confirm that the Panel's understanding is correct?

1. In addition to the provisions of the *Anti-Dumping Agreement* and GATT 1994 cited by the Panel in Question 85, Canada retains its claims based on Article 5.1, Article 5.4 and Article 2.2.1, which were referred to in Canada's written answer to Question 1 from the Panel

B. ARTICLE 5.2

To Canada:

87. The Panel notes that Canada has made a number of allegations on shortcomings of the data in the application in Section II of its Second Oral Statement. In Canada's view, does the examination it claims should have been done by the DOC, require a pre-initiation investigation?

2. Canada's claims, as detailed in Section II of Canada's Second Oral Statement and Canada's previous submissions, do not require that an investigating authority conduct a pre-initiation investigation.

3. Article 5.3 obligates an investigating authority to examine the accuracy and adequacy of the evidence provided in an application and to determine whether there is sufficient evidence to justify initiating an investigation.

4. Commerce did not properly examine the accuracy and adequacy of the information provided in the Application and did not properly determine, based on the facts before it, that there was sufficient evidence to justify initiating this investigation. The *Anti-Dumping Agreement* requires an objective and unbiased examination and determination in accordance with Article 5.3 prior to initiation.

5. There is an additional obligation that arises prior to initiation in the circumstances of this investigation. Article 5.2 instructs that the "application shall contain such information as is

reasonably available to the applicant” on a number of subjects. The Application in this investigation was both insufficient to justify initiation and did not contain the minimum information that was reasonably available to the Applicant, on prices and the constructed value, including costs of production, of the softwood lumber products at issue.¹

6. There has been a dispute in this proceeding over whether the investigating authority must ensure that the application contains some, any, or all reasonably available information. This issue is hypothetical. In this case, there was material information readily available that the Applicant withheld and that Commerce, based on information in the Application, knew it withheld.

7. The United States has admitted that the Application contained information indicating that the Applicant International Paper owned Weldwood, a major Canadian producer and exporter of softwood lumber.² Therefore, there was information in the Application establishing that actual cost and price information from a major Canadian producer was available.³ Such cost and price information was not provided in the Application.

8. An objective and unbiased investigating authority, as a part of its examination and determination of the sufficiency of the evidence in the Application in this investigation, would have determined that the Applicant had not provided reasonably available information on prices and costs. As part of its examination prior to initiation of the facts before it, Commerce was aware that the Application did not, in spite of the Applicant’s repeated statements to the contrary,⁴ contain such information as was reasonably available to the Applicant on prices and costs. The United States has admitted that Commerce did not discuss the “Weldwood-IP relationship, because it was not relevant to either the industry support question or the sufficiency of the evidence presented in the application as to prices and costs.”⁵ Therefore, any suggestion by the United States that some sort of elaborate pre-initiation investigation was required to satisfy Canada’s claim under Article 5.2⁶ is not credible and is an attempt to distract from the facts before the Panel in this proceeding. Based on the Application, Commerce knew that reasonably available information had not been provided; it chose simply to ignore that fact.

¹ See Article 5.2(iii) of the *Anti-Dumping Agreement*.

² US First Answers to Questions, at paras. 12-13; Petition, Exhibit I.B-7, Article from The Vancouver Sun, 23 March 2001 (Exhibit US-62). See also Petition, Vol. 1B, Exhibit 1B-9, Top Canadian Exporters of Softwood Lumber to the United States 2000 (Exhibit CDA-39).

³ Further, the availability of Weldwood as a source of data was made clear to Commerce five days before publication of the Notice of Initiation in this investigation. See Quebec Lumber Manufacturers Association Letter to DOC (25 April 2001) (Exhibit CDA-50). The Notice of Initiation was published in the Federal Register on 30 April 2001 (*Certain Softwood Lumber Products from Canada*, 66 Fed. Reg. 21,328 (Dep’t Commerce 30 April 2001) (initiation) [hereinafter “Initiation Notice”] (Exhibit CDA-9)). Canada also notes that Weldwood provided data and information to Commerce in connection with this investigation on at least two occasions and asked to be a voluntary respondent in this investigation. See Letter from Hunton & Williams re Softwood Lumber from Canada with attached Questionnaire Response of Weldwood of Canada Limited, 3 May 2001 (Exhibit CDA-138) and Cover Letter for Weldwood Sections B, C and D Questionnaire Response from Hunton & Williams to DOC, 16 July 2001 (public version) (Exhibit CDA-49). Commerce never considered the data or information. See *Certain Softwood Lumber Products from Canada*, 66 Fed. Reg. 56,062 (Dep’t Commerce 6 November 2001) (prelim. anti-dumping determination) at 56,064 (Exhibit CDA-11).

⁴ See, e.g., *Certain Softwood Lumber Products from Canada*, Petition for the Imposition of Antidumping Duties Pursuant to Section 731 of the Tariff Act of 1930, As Amended, Vol. I (2 April 2001) at 1 [hereinafter the volumes of the Petition are referred to as “Petition”] (Exhibit CDA-36); Petition, Vol. III (2 April 2001) at p. III-1, III-13 to III-16 (Exhibit CDA-37); and Petitioners’ Amendment to Petitions for Imposition of Antidumping and Countervailing Duties on Certain Softwood Lumber Products from Canada (10 April 2001) at 2 (Exhibit CDA-40).

⁵ US First Answers to Questions, at para. 12.

⁶ Opening Statement of the United States at the Second Meeting of the Panel, 11 August 2003, at para. 17 [hereinafter “US Second Oral Statement”].

9. In any event, Canada's claims under Articles 5.2 and 5.3 are separate. Leaving aside Canada's claim under Article 5.2, the same question before the panel in *Argentina – Poultry* is before this Panel: could an objective and unbiased investigating authority, looking at the facts before it, properly have determined that there was sufficient evidence of dumping to justify initiating an anti-dumping investigation?⁷ Based on Canada's submissions and the information before this Panel indicating, *inter alia*, that the Application did not allege dumping by any particular Canadian producer, the answer is no.

C. ARTICLE 5.3

To Canada:

88. In paras. 34 to 43 of Canada's reply to Question 8, Canada has made certain allegations regarding the information contained in the application as submitted by the US domestic industry, and which formed the basis for the initiation of the investigation. In its Second Oral Statement, Canada has also alluded to some of these issues. Could the US please comment in detail on these allegations?

10. Based on Canada's submissions and the information before this Panel, the Panel must conclude that an objective and unbiased investigating authority, looking at the facts before it, could not have properly determined that there was sufficient evidence of dumping to initiate this investigation. Therefore, the United States violated Article 5.3.

11. Canada reserves the right to respond to any new evidence or information, should such evidence or information exist, that the United States may proffer in support of its assertion that Commerce had sufficient evidence before it to justify initiating this investigation.

89. In its reply to Question 8, Canada submits that using the Applicants *Random Lengths* price data for Quebec, a comparison of all of the Quebec ex-factory price data for ESPF (2x4, Studs&Btr, KD, RL and 2x4-8', PET, KD) products sold in Quebec and in the US, shows that the US price was consistently higher during the period and that there was therefore no price-to-price dumping demonstrated by the evidence in the Application. It further provides a calculation in footnote 32 to substantiate the allegation. Could the US please comment on this allegation and on the calculations?

12. Commerce properly rejected the home market price data as supplied in the Application for British Columbia.⁸ The Quebec pricing data, as demonstrated in the footnote referenced in the Panel's question, showed no dumping.⁹ Therefore, the Application contained no evidence of dumping on a price-to-price basis with respect to any company or even any region of Canada.

13. Canada reserves the right to respond to any new evidence or information, should such evidence or information exist, that the United States may proffer in support of its assertion that Commerce had sufficient evidence before it to justify initiating this investigation.

⁷ *Argentina – Definitive Anti-Dumping Duties on Poultry from Brazil*, Report of the Panel, WT/DS241/R, adopted 19 May 2003, at para. 7.60.

⁸ Initiation Notice, 66 Fed. Reg. at 21,330 (Exhibit CDA-9). See also Canada's Second Oral Statement, at para. 13; Canada's Responses to Questions to the Parties from the Panel in Connection with the First Substantive Meeting, 30 June 2003, at para. 33 [hereinafter "Canada's First Responses to Questions"]; and Canada's Second Written Submission, at para. 49.

⁹ Canada's First Responses to Questions, at para. 33 and footnote 32.

90. Please comment on Canada's Second Oral Statement, para. 20 which states that:

"[t]he United States, hiding behind the pretence of confidentiality, has not provided this Panel with any information that was before Commerce about the two US surrogate mills. These US mills were at the heart of Commerce's decision to initiate. Canada has not seen, and the Panel still does not have before it, basic information in the hands of the United States, such as the names of the US mills and what Commerce knew about those mills. The United States has responded to Canada's claims with nothing but assertions."

14. Canada emphasizes four points regarding the issues raised by this question.

15. First, the United States has no reasonable basis for refusing to provide whatever information it has as to the identity of the two US surrogate mills used to model the costs of Quebec producers and any information concerning what Commerce knew, if anything, about the mills prior to initiation. There are mechanisms in this proceeding for keeping information confidential. Trusting in those mechanisms, Canada has provided highly confidential information to the Panel and the United States. There is no basis for the United States to claim that any information about these mills is so sensitive that it cannot be shared with the Panel.

16. Second, the two US surrogate mills used to model the costs of Quebec producers were critical to the decision to initiate. All of the price comparisons indicated that there was no dumping; the initiation was based solely on costs.¹⁰ There were no usable home market prices, nor surrogate prices, from British Columbia, and therefore Commerce could not legally initiate the investigation on the basis of any information in the Application pertaining to British Columbia.¹¹ With respect to Quebec, there was no cost evidence from any Quebec producer.¹² Instead, the Applicant constructed a surrogate cost for Quebec mills using information from US mills regarding overhead, and labour, electricity and fuel usage factors.¹³ Therefore, the validity of the decision to initiate turns largely on whether an objective investigating authority, looking at the facts before it, could properly have determined that the US surrogate mills were representative of Canadian mills, and that the costs of the US surrogate mills were reasonably allocated to the products at issue.

17. Third, it is more than a theoretical possibility that the US surrogate mills are not representative and that using their overhead and "usage factors" skewed the costs alleged in the Application. There is a wide range in performance of US mills in areas of the United States that

¹⁰ *Ibid.*

¹¹ Initiation Notice, 66 Fed. Reg. at 21,330 (Exhibit CDA-9). See also Canada's Second Oral Statement, at para. 13; Canada's First Responses to Questions, at para. 33; and Canada's Second Written Submission, at para. 49.

¹² Petition, Exhibit VI.A, Petitioners' Cost Methodology (public version), at 1-2 (Exhibit CDA-134).

¹³ See DOC AD Investigation Initiation Checklist: Certain Softwood Lumber Products from Canada, Inv. No. A-122-838, at 8 (Exhibit CDA-10); and Petition, Exhibit VI.A, Petitioners' Cost Methodology (public version), at 1-4 (Exhibit CDA-134). See also Petition, Exhibit VI.C-1 (public version), (Exhibit CDA-135). Column "C" of each of the "Costs of Manufacturing" calculations charts in Exhibit CDA-135 indicates that the "input units required per MBF of lumber" are taken from the two redacted "Certifications" from employees of two US mills that follow the calculations charts. Therefore, the "input units" or usage factors for the components of the cost model, including the "processing costs" component of the model, are derived from some undisclosed combination of the experience of the two US mills. Neither of the "Certifications" provides cost information for the US mills for a full calendar year. Canada also notes that the United States has admitted that data from US mills were used to provide "production" or usage factors for the Applicant's cost model. See US Second Written Submission, at paras. 24-25.

border Quebec. Some of those mills might be representative of mills in Quebec, but many others were inefficient mills with outdated equipment and substantial operational problems that would have driven up their cost of producing a thousand board feet of lumber.¹⁴ Any constructed normal value based on such mills would be unduly high and would tend to show dumping where there was, in fact, no dumping. Further, the use of such mills to model costs makes it more likely that legitimate home market sales would be improperly rejected as below cost (*i.e.*, not in the ordinary course of trade).

18. The Application itself lists several US mills in Maine that curtailed operations or had layoffs during the relevant time period. For example, Pleasant River Lumber Co. in Dover-Foxcroft, Maine; Moose River Lumber Co. in Jackman, Maine; Georgia Pacific in Woodland, Maine; and J.D. Irving in Ashland, Maine, all experienced curtailments and layoffs.¹⁵ Because of the wide range in the performance of the US mills, it is important to know the identity of the US surrogate mills and additionally, to know what Commerce knew, did not know and failed to ask about the US surrogate mills that formed the basis of its decision to initiate.

19. Finally, there is no evidence on the record that Commerce knew much about the US surrogate mills. For example, there are no annual reports or product lists in the public version of the Application. Nor are there significant areas redacted in the public version of the Application that might discuss the representative nature or the cost allocations of these mills. It appears that Commerce based its initiation on unsubstantiated assertion by the Applicant. The Application was deficient, and the investigating authority has tried from the beginning to avoid the consequences of the deficiency.

20. Canada reserves the right to respond to any new evidence or information, should such evidence or information exist, that the United States may proffer in support of its assertion that Commerce had sufficient evidence before it to justify initiating this investigation.

D. ARTICLE 2.6

To the US:

91. The Panel notes in para. 36 of the US Second Oral Statement that “Canada misunderstands the analysis that was actually applied”. Could the US expand on what it perceives the misunderstanding of Canada is?

21. As there is some discrepancy between what the United States actually did, and what it now tells the Panel, Canada would like to summarize its understanding of “the analysis that was actually applied”.

22. The United States told the Panel in its first written submission that it reviewed five factors, from *Diversified Products*, “[a]s **part of** its analysis in determining whether ‘clear dividing lines’ exist within the product under consideration identified within the petition.”¹⁶ In paragraph 36 of its opening statement in the Second Panel Meeting, however, the United States told the Panel, “Commerce’s assessment of whether there are ‘clear dividing lines’ between products is **part of** the

¹⁴ As Canada has stated in previous submissions, including Canada’s Second Oral Statement at paragraph 17, the Applicant noted that costs vary significantly among producers based on a number of factors including level of efficiency, type of equipment, physical location and wood fibre source material. See Petition, Exhibit VI.A, Petitioners’ Cost Methodology (public version), at 4-5 (Exhibit CDA-134).

¹⁵ Petition, Vol. I (2 April 2001) at I-34 (Exhibit CDA-36); and Petition, Vol. IB, Exhibit 1B-33, Mill Closures – August 2000-March 2001 (Exhibit CDA-177).

¹⁶ US First Written Submission, at para. 103 (emphasis added).

Diversified Products analysis, not subordinate to this analysis.”¹⁷ Canada submits that the United States has offered a distinction with a material difference.

23. The central question is whether the *Diversified Products* criteria as applied by the United States satisfy the requirements of Article 2.6. In the first formulation, *Diversified Products* is stated to be part of a “clear dividing lines” test. In the second formulation, the relationship is reversed, and the examination of whether there are clear dividing lines is part of the *Diversified Products* analysis.

24. Although the United States most recently has told the Panel that the “clear dividing lines” test was treated as part of *Diversified Products*, the test actually applied in the investigation was consistent with the first formulation: the United States subordinated the *Diversified Products* criteria to a new and different test for “clear dividing lines”, which does not exist in *Diversified Products*.

25. The United States reported to the Panel that its assessment referred to “whether ‘clear dividing lines’ exist within the product under consideration”, but the obligation in Article 2.6 is to determine the like product. The United States thus admits that, in looking for “clear dividing lines”, it was not determining whether like products were “identical” to the product under consideration or, in the absence of identical, bearing “characteristics closely resembling” the characteristics of the product under consideration.

26. When the Department of Commerce enumerated the *Diversified Products* criteria for bed frame components and finger-jointed flangestock, it admitted that it did not complete the test. In each instance where the Department of Commerce found bed frame components or finger-jointed flangestock to be unique, entirely unlike the product under consideration, it discarded the criterion from the analysis, preferring to conclude that there was no “clear dividing line” between the disputed product and the product under consideration because of some undefined category of “specialty lumber” that, without explanation, supposedly subsumed both bed frame components and finger-jointed flangestock.¹⁸ Thus, *Diversified Products* was subsumed by a test for “clear dividing lines”.

27. The comparisons of Western Red Cedar and Eastern White Pine to the product under consideration suffered a similar fate. Unique characteristics were discarded, as with bed frame components and finger-jointed flangestock, but characteristics that were different were judged not to be “so different” as to warrant the finding of a “clear dividing line”. An isolated physical characteristic of an appearance grade species, such as Eastern White Cedar, was found to be similar to a physical characteristic of Western Red Cedar, for example, thus placing the two species on a “continuum” not separated by a clear dividing line.¹⁹

28. The allegedly similar species did not have to be adjacent to one another on Commerce’s continuum. They merely had to have a characteristic that could “link” them. The greater the scope of the investigation, the more characteristics were available to select, creating greater assurance that any distinct like product would have some characteristics also found on the so-called continuum. In such a case, there could never be a “clear dividing line”.

29. At no point in its analysis did Commerce attempt to determine whether a product at issue actually possessed characteristics closely resembling those of the product under consideration, as required by Article 2.6. Hence, Canada understands that the US statement offered to the Panel in the

¹⁷ US Second Oral Statement, at para. 36 (emphasis in original).

¹⁸ DOC Issues and Decision Memorandum for the Antidumping Duty Investigation of *Certain Softwood Lumber Products from Canada* (21 March 2002), Comment 52, at 163-164 (bed frame stock/square-end bed frame components); and at 165-166 (flangestock) [hereinafter “IDM”] (Exhibit CDA-2).

¹⁹ *Ibid.*, at 152-153 (Western Red Cedar) and at 159-160 (Eastern White Pine).

first written submission is an accurate description of the methodology applied, and that the most recent description is not.

E. PHYSICAL CHARACTERISTICS

To Canada:

92. Could Canada explain why in the case of softwood lumber products cost accounting records of companies do not show differences in variable costs according to different dimensions?

30. Softwood lumber producers, whether in Canada or the United States, do not measure cost differences among the various lumber grades and dimensions that are produced in the sawmill, per common unit of measure. The US implication that producers' books and records identified variable costs for every attribute except dimension is factually incorrect and misleading. In the normal course of business, softwood lumber producers calculate an average cost of production, per thousand board feet of lumber, by process for all production from harvest through planing. They do not attempt to assign different costs to different grades of lumber, or to different dimensions of lumber, but instead track a single, average cost for all joint products jointly produced.

31. Canadian and US producers record an average cost per thousand board feet because of the nature of lumber production, which accountants refer to as a joint production process. In a joint process, products with different characteristics are not produced sequentially, as is typical for most products from steel pipe to semiconductors, but simultaneously. In the case of lumber, logs are processed simultaneously into green lumber of different sizes and grades. While the producers can influence the characteristics of the lumber produced, the principal determinates are the characteristics of the log processed, which, among others, include the quality of the fibre, the length and the diameter. Other examples of joint products include all beef products and all pork products. Producers can track the costs of raising a group of hogs or cattle, as well as the costs of processing the animals into different cuts of beef or pork, but one cannot track the unit cost of an individual cut of meat from an individual animal, just as one cannot track the costs of an individual "cut" of lumber from an individual log.

32. In a joint production process, because it is not possible to measure the unit cost of production using typical cost accounting techniques developed for sequential production, producers have two alternatives. The producers can measure the cost on the basis of a simple physical measure such as average cost by weight or volume (in this case, unit cost per thousand board feet); or the producers can assign cost on the basis of the relative value of the goods produced. The latter, value-allocated cost, has the advantage of assigning costs based on the revenue generating potential of the various products produced, thereby assuring that aberrantly large losses or gains are not recorded at the time of sale. On the other hand, value-allocated cost is more burdensome and costly to administer. Since in the lumber industry value-allocated costs are impossible to measure on an ongoing basis (in terms of measuring the operating results of the company), producers have adopted the first alternative, an average cost per thousand board feet. Rather, they assess profitability based on the portfolio of lumber products they produce; that is, lumber producers look to whether the revenue from all the different sizes and grades of products they produce jointly is sufficient to cover the costs of producing those products.

33. In its Final Determination, Commerce recognized that the use of a single average cost in a dumping analysis for a range of joint products with a range of values would distort the margin calculation. Thus, Commerce adopted a hybrid method that allocated fibre costs (that is, the costs of obtaining timber, harvesting and transporting logs) and sawmill costs by value by grade, but used

average costs for thickness, width, and length.²⁰ That is, while different grades of lumber were allocated different joint costs, based on the relative values of the grades, different dimensions of lumber within a particular grade were allocated the same “average” joint cost. It was only for this reason that Commerce *created* variable cost differences by allocation among products by grade, but not dimension.

34. In any event, whether or not a difference in the variable costs of production for lumber products of different dimensions can be directly ascertained, the obligation pursuant to Article 2.4 remains the same. Nothing in Article 2.4 relieves an investigating authority from its “due allowance” obligation in cases in which it decides not to calculate a variable cost difference between products with differences in physical characteristics that affect price comparability.

35. It is important to note that, in raising the question of variable costs, the United States has attempted to confuse this issue. The issue before the Panel is simple: whether Article 2.4, which requires an allowance for physical characteristics which affect price comparability, obligates the United States to make an adjustment for dimension in the face of un rebutted evidence before Commerce that dimension affects price. As Canada has noted, the Applicant and the respondent companies agreed that dimension affects price comparability. Commerce itself concluded in the Preliminary Determination²¹ that dimension had an effect on price comparability. Commerce also concluded that dimension affects price by using thickness, width and length as product characteristics critical to establish when an identical product was matched. The United States is trying to change the focus to convince the Panel to address the question of *how* the allocation would be calculated, rather than whether an allocation is required.

93. Please show whether and where on the record the respondents demonstrated that dimension had an effect on price comparability. Please also explain at what stage of the investigation these were demonstrated.

36. There are two distinct factual issues regarding the impact of dimension on price that the United States is seeking to confound. The first is the general issue of whether dimension has an effect on price comparability. The second issue is the more specific: what differences were shown to exist by the pricing data collected for the actual pairs of non-identical products compared by Commerce?

37. The first issue is the one most relevant to the Panel’s question, and, as explained below, the only one Canadian respondents had an opportunity to address. Evidence relevant to this issue includes (1) statements by US and Canadian producers that they differentiate and price their products based on differences in dimension; (2) industry pricing publications, such as Random Lengths, that report product pricing data differentiated by dimension; (3) findings by other US government agencies knowledgeable about the industry that dimension affects product pricing, and (4) examples from the pricing data collected by Commerce that different dimension products sell for different prices. Such evidence was presented by Canadian respondents throughout the proceeding before Commerce, as Canada has detailed in response to Questions 22 and 25. All of the citations to the record before Commerce were provided in Canada’s response to Question 22.

38. In addition, a 11 May 2001 letter from counsel for Tembec, consistent with the citations provided in response to Question 22, is attached as an exhibit.²² As Canada noted, there was agreement among all interested parties that dimension affected price comparability. The evidence that

²⁰ *Ibid.*, Comment 4, at 19-25 (Exhibit CDA-2).

²¹ *Certain Softwood Lumber Products from Canada*, 66 Fed. Reg. 56,062 (Dep’t Commerce 6 November 2001) (prelim. antidumping determination) (Exhibit CDA-11).

²² Tembec Response to the 3 May 2001 Submission of the Coalition for Fair Lumber Imports Executive Committee concerning Respondent Selection, Product Matching Criteria, and Simplification Issues (11 May 2001) (Contains Business Confidential Information) (Exhibit CDA -178).

dimension affected price comparability was the same as the evidence that grade affected price comparability. Canada also noted that there is *no* evidence in the record to the effect that dimension does *not* affect price comparability. No party, including the Applicant, argued, much less provided evidence, that producers and buyers do not consider dimension in setting prices, or that dimension did not have to be considered in deciding what prices to compare. Nor does the record contain any other alternative explanation or evidence of why price differences exist among products of different dimensions (all other characteristics being equal).

39. Second, Canadian respondents never had the opportunity to provide the product-specific pricing analyses the United States contends is missing. Where normal value and export price of products of identical dimension were compared, there was of course no dimensional “difmer” requirement. This fact had the effect of greatly reducing the number of “difmers” that Commerce had to calculate. Only non-identical comparisons required a “difmer”. And only Commerce could know, prior to the Final Determination, which non-identical comparisons would be made and thus, which products would require a “difmer” calculation. That is, respondents had no opportunity to provide analyses to Commerce with respect to the non-identical comparisons used or any allowances that were required to account for physical differences in the products actually compared that affected price comparability, since Commerce never disclosed to the respondents the non-identical product comparisons it would use or the methodology it would use to select those comparisons. As Canada has noted, Commerce, in its Preliminary Determination, did not make any non-identical comparisons, and thus did not develop any model matching methodology that respondents could analyze. Rather, Commerce developed a model matching methodology and utilized non-identical comparisons only in its Final Determination. This methodology, and the resulting non-identical product comparisons, were disclosed to respondents only after the conclusion of the proceeding. Thus, respondents could never have provided the product-specific pricing analysis the United States contends is missing. Only Commerce could have performed such an analysis, because only Commerce knew the identical (no “difmer” required) and non-identical (dimension “difmer” required) product comparisons to be used in the Final Determination. This analysis, if one ever was performed, is also missing from the record.

To the US:

95. Could the United States explain in detail how the issue of dimension was addressed in the lead-up to the Preliminary Determination and from the Preliminary Determination to the Final Determination, including after the DOC found that there were no differences in variable costs? Was DOC’s statement in the Preliminary Determination that dimension has an effect on price comparability made before DOC knew that there was no difference in variable costs? Indicate what made DOC change its position with respect to the effect of dimension on price comparability between the Preliminary Determination and the Final Determination.

40. The United States has focussed its response to Canada’s Article 2.4 claim on the fact that Commerce did not have information on variable cost differences among different sizes of lumber products. In so doing, the United States attempted to distract the Panel from two critical facts.

41. First, as discussed above, the fact that there were no variable cost differences among different sizes of lumber was simply a necessary consequence of Commerce’s decision not to take dimension into account in allocating costs based on value.

42. Second, and more fundamentally, as noted above, the Article 2.4 obligation to give due allowance is not contingent on the existence of differences in variable cost of production. As long as dimension affects price comparability – an issue that was not in dispute until this proceeding – due allowance must be made for dimensional differences when prices of different dimension products are compared. The obligation to make such an adjustment is separate from the issue of *how* the allowance is calculated. Variable cost differences are one way of calculating the allowance, but there

are other ways to do so. For example, when differences in variable costs are not available, US law provides for calculating the required due allowance by using differences in market value.²³ None of the US arguments on the lack of variable cost differences is relevant to the issue before the Panel concerning the obligations imposed by Article 2.4, and none of the arguments contradicts Commerce's earlier finding that dimension affects price.

96. At what stage were the respondents informed of DOC's finding that differences in dimension do not affect price comparability? What opportunities were provided to respondents to comment on that finding?

43. The Canadian respondents were not informed of Commerce's decision not to make allowance for differences in dimension until Commerce's Final Determination, after which comments cannot be filed. Moreover, as the Panel has noted in the preceding question, Commerce found in its Preliminary Determination that dimension affected price comparability and reiterated that finding in its Final Determination.²⁴ Thus, there was no need for respondents to provide pricing or other analyses on this issue following the Preliminary Determination, during the normal briefing period, since Commerce and the Applicant had agreed with respondents' position on this issue.

99. With respect to the consistency in price patterns, the Panel has the following questions:

- (a) Could DOC explain in detail the methodology it used to carry out its consistency test? Illustrate your explanation with an example from the test that was carried out in this case, including any sampling, selection of dates, etc. Did the US consider using other methodologies?**
- (b) Could the US explain in detail how the results of its test were evaluated? Please explain the evaluation leading up to that conclusion.**

44. Canada notes that Commerce performed no "consistency" test on the record, and there is no information on the record concerning what methodology would have been used for such a test. To the extent that the United States provides such an analysis now, after the fact, Canada requests that it be provided with a copy of the computer programme used to generate that analysis and an opportunity to comment. Canada also suggests that the Panel evaluate whether the analysis the United States offers is comprehensive or selective (the Panel has information on the number of non-identical comparisons used for each respondent) and when the analysis was prepared.

45. Canada further notes that a "consistency" of the relationship among prices for products of particular dimensions is not relevant to the question of whether dimension affects price comparability. Even assuming that, for selective product pairs, the difference in price fluctuates, the very fact that the prices are different to begin with, establishes that dimension affects price comparability. Fluctuations in relative prices are no different than fluctuations in absolute prices – neither precludes price-to-price comparisons or adjustments.

46. The United States makes much of the fact that for some undisclosed, selected product pairs, for undisclosed respondents, it observed that sometimes one product price was higher and sometimes the other product price was higher. If it were established, for a specific non-identical product comparison used for a specific respondent, that the relative price difference fluctuated above and below zero such that on average it was zero, then the appropriate adjustment for that specific comparison would be zero, as the average difference in value of the products compared was zero. But this result would be by far the exception rather than the rule, and could not relieve Commerce from its

²³ See 19 C.F.R. 351.411(b) (Exhibit CDA-179).

²⁴ See IDM, Comment 7, at 42-46 (Exhibit CDA-2).

obligation to make an adjustment for non-identical product comparisons where differences in the home market prices of those products were not on average zero.

To both parties:

103. Could the parties confirm whether the percentages mentioned in para. 40 and footnote 33 of the US reply to Question 25 of the Panel relate to differences in dimension only?

47. Canada confirms its understanding that the US analysis relates to differences in dimension only.

F. ZEROING

To Canada:

104. According to Canada, would zeroing be permissible if the transaction-to-transaction methodology of Article 2.4.2 is used to calculate the margin of dumping? If not, what is the legal basis for its position?

48. The term “zeroing” has of course only been used in the context of a particular application (through “models”) of the first method described in Article 2.4.2, *i.e.*, the comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions. Regardless, there is no basis in Article 2.4.2’s directions with respect to the transaction-to-transaction methodology to overcome the clear mandate that Article 2.4.2 provides with respect to the average-to-average methodology. Article 2.4.2 does not speak in terms of a particular stage of a methodology, it speaks in general terms only. Thus, whatever directions are given in Article 2.4.2 apply generally, to every stage of a methodology if it requires more than one stage to be accomplished. Any ambiguity arising in Article 2.4.2 as to the second methodology must be interpreted in the context of Article 2.4’s mandate that a “fair comparison shall be made between the export price and the normal value”.

49. As discussed below in response to Question 108, a comparison that involves zeroing cannot be “fair” because it unjustifiably gives less weight to some transactions than to others in the calculation of an overall dumping margin. Were the United States correct, the transaction-to-transaction language in Article 2.4.2 would mean an investigating authority, when calculating an overall dumping margin, could ignore relevant transactions simply because they were not dumped. Such a results-orientated approach cannot comport with the text of Article 2.4, nor with the obligation under Article 2.1 to calculate a dumping margin for the product under investigation (rather than for any portion thereof). Thus, even with the transaction-by-transaction methodology all export price transactions must be included in the calculation; the dumping margin still must be calculated based on an average of all transactions included, and there is no basis for excluding or altering the values of transactions where the price comparisons revealed no dumping.

50. Ultimately, each method stands on its own. Even if it were the case that the second methodology in Article 2.4.2 lacked disciplines on its application, that would not justify reading out or ignoring the disciplines applied to the first methodology. It is agreed by both Parties to the current proceedings that Canada’s claim concerns the application by the United States of the first method described in Article 2.4.2 (weighted average to weighted average). It is in the context of the particular application by the United States of the first method described in Article 2.4.2 that Canada’s claim with respect to “zeroing” has arisen. What is permitted or not permitted pursuant to the second method described in Article 2.4.2 is not at issue here.

105. Please comment on paras. 53, 54 and 62 of the US Second Oral Statement.

51. The US argument as advanced in paragraphs 53-54 is based on a false premise: that Canada claims that the meaning of “all” and “comparable” change between the first and final stages of the first methodology. The paragraphs of Canada’s submission which the United States contests are not intended to provide a definition of the terms “all” and “comparable” in any way other than their ordinary meaning. Rather, the paragraphs describe how those terms must be *applied* by an investigating authority in each of the two stages of a comparison such as that performed by Commerce in this case. The fact that the standard in Article 2.4.2, prescribed by the words “all” and “comparable”, applies in the case of both simple and complex transactions does not mean that the meaning of either “all” or “comparable” changes. To the contrary, the ordinary meaning of these words is retained, and only their application changes. Canada’s submission demonstrates that both “all” and “comparable” can and must be applied during both stages of the comparison, in keeping with their ordinary meaning, and have operational significance at both stages.

52. More generally, the US attack on *EC – Bed Linen* is ill-founded as it attacks the Appellate Body for failure to discuss the requirements of Article 2.4.2 as they apply to each stage of a methodology. The stage or stages in a methodology are simply way points *en route* to calculating a proper margin of dumping. The disciplines imposed by Article 2.4.2 with respect to the first methodology ensure a certain result at the final stage, based on the rule that must be employed in using that methodology, *i.e.*, to use all comparable export transactions. There was no need for the Appellate Body to proceed stage by stage for each methodology in Article 2.4.2. It is worth noting, however, that the panel decision in *EC – Bed Linen* does discuss the stages of the first methodology, and reaches the same conclusion as the Appellate Body.

53. Claims made by the United States in paragraph 62 of its opening statement are addressed in Canada’s response to Question 108, below.

106. Please comment on para. 56 of the US Second Oral Statement that:

“[u]nder Canada’s argument, the first basis for establishing dumping margins — the weighted-average-to-weighted-average basis — would apply to both stages of the calculation. However, the other two bases for establishing dumping margins plainly apply only to the first stage. Thus, Canada’s theory leads to an interpretation of Article 2.4.2 in which the scope of the obligation differs depending on the basis for establishing dumping margins. Yet, the provision itself does not support such differential interpretation.”

54. The US statement assumes what must be proven: that Article 2.4.2 concerns only the first stage of a comparison, and not all stages, even though the language of Article 2.4.2 is general and not limited. The United States seeks to portray it as peculiar that the first methodology should have application in both stages of a comparison using the first methodology, but that is only because it has posited that the rules apply only at the first stage. As noted above, Article 2.4.2 applies generally. The differences among the methodologies are differences in detail, not differences in generality of application. The fact that one methodology lacks the specific disciplines of another does not negate the existence of those disciplines in the latter.

55. The US interpretation of Article 2.4.2 would suggest that Article 2.4.2 does not apply at all in a case in which there is only a single stage involved in computation of the dumping margin. Not only would such a reading not comport with the text, it would presume that no discipline is imposed upon investigating authorities in respect of single-stage calculations. This is simply not credible, given the clear obligations imposed in both Articles 2.4 and 2.4.2.

56. Canada's interpretation leaves WTO Members free to apply the first method (weighted average to weighted average) in one stage or multiple stages. In the case of a two-stage process, the wording of Article 2.4.2 has as a consequence that zeroing is not permitted. Contrary to what the United States has argued, this is not a situation in which Canada argues that treaty terms take on a different meaning at different stages of the calculation of the dumping margin. Rather, the Panel is dealing with a general description of one methodology that is provided for in Article 2.4.2 to establish the margin of dumping and the question of what the legal consequences are of that legal provision when a WTO Member decides to apply that methodology through two stages (separate models and subsequent aggregation). The Appellate Body has already pronounced, in *EC – Bed Linen*, that in such a two-stage process, a WTO Member is not permitted to apply zeroing. Canada urges the Panel to follow the Appellate Body's interpretation.

107. Please comment on the US statement that the *AD Agreement* does not recognise a concept of “negative” dumping.

57. Canada would agree that the *Anti-Dumping Agreement* does not *refer* to “negative” margins of dumping. However, the US claim that this fact permits Commerce to ignore certain transactions when aggregating intermediate comparisons into the overall margin is founded on a fundamentally flawed premise: that the *Anti-Dumping Agreement* recognizes “margins of dumping” at all at the first stage of a dumping calculation. A “determination of dumping” under Article 2 is made for a product, not for a particular model. This is clear from the terms of Article 2.1, which states that the comparison governed by Article 2 establishes whether “a *product* is to be considered as being dumped”.²⁵ Nowhere does the *Anti-Dumping Agreement* recognize the concept of intermediate stage margins of dumping. Nor does it permit the artificial generation of a dumping margin by denying the existence of sales at prices above normal value. Both the panel and the Appellate Body in *EC – Bed Linen* found that the term “negative” in respect of margins of dumping served simply to illustrate the very obligation that the United States attempts to circumvent.

108. Given that Canada bears the burden of proof of presenting a *prima facie* case of violation:

(a) Could Canada indicate why it considers the results of a dumping margin calculation that includes zeroing to be unfair?

58. A dumping margin calculation that includes zeroing cannot be considered to produce a “fair comparison” within the meaning of Article 2.4 because it unjustifiably operates to give greater weight to transactions included in intermediate models for which export price is less than normal value, than to those for which export price is greater than normal value. The ordinary meaning of “fair” is “just, unbiased, equitable, impartial; legitimate, in accordance with the rules or standards”.²⁶ A comparison conducted on the basis of zeroing results in unequal treatment of those transactions for which export price is deemed to exceed normal value at the intermediate stage. Zeroing gives these transactions less weight in the calculation of the overall dumping margin, and thus results in a comparison that is biased in favor of those transactions for which export price is less than normal value. It thus does not produce the “equitable, impartial, unbiased” comparison mandated by Article 2.4. Also, when certain export transactions are disregarded, the figure arrived at is no longer a “weighted average”.

(b) Could Canada elaborate on the legal basis for its claim that “zeroing” violates the obligation under Article 2.4 to carry out a “fair comparison”, other than the mere reference to the *obiter dictum* of the AB in its *EC – Bed Linen* report?

²⁵ Emphasis added.

²⁶ *New Shorter Oxford English Dictionary*, 3rd Ed. (Oxford: Clarendon Press, 1993), at 907 (Exhibit CDA-180).

What is the benchmark against which Canada tests whether a comparison is fair or unfair?

59. The legal basis for Canada's claim that zeroing violates Article 2.4, and the benchmark against which the conduct of the investigating authority must be judged, is the ordinary meaning of the terms of Article 2.4, as described above. A "fair comparison" requires equitable, unbiased treatment of all transactions being compared. Zeroing does not produce a fair comparison because it arbitrarily eliminates certain transactions from the calculation, resulting in a margin that does not equally reflect all transactions. The US reading of Article 2.4 in paragraph 62 of its Second Oral Statement as simply setting forth the factors requiring adjustments to ensure price comparability would render inutile the term "fair comparison." Given that Article 2.4 itself deals with subjects other than price adjustments – such as which sales should be compared and at what level of trade – the US reading of this provision is overly narrow on its face.

60. Article 2.4 sets forth several discrete obligations with respect to comparisons of export price and normal value: (1) that it be "fair" (in keeping with the ordinary meaning of that term); (2) that it be made at the same level of trade and in respect of sales made at as nearly as possible the same time; and (3) that due allowance be made for differences which affect price comparability. The "fair comparison" requirement stands alone, and is not dependent on other statements in that provision. Moreover, the "fair comparison" requirement is directly incorporated into Article 2.4.2 by express reference in Article 2.4.2's introductory clause, which states that the provision is "subject to the provisions governing fair comparison in paragraph 4".²⁷

61. The fair comparison of Article 2.4 is conducted so as to account for all appropriate factors and thereby reflect accurately the relationship between prices and variables that affect prices. The measure by which authorities gauge dumping is the price differential between export price and normal value. That differential can be calculated in various ways under Article 2.4.2, but the sole objective of the calculation is to establish whether or not dumping has occurred. Anything that would exaggerate or distort that differential, thereby affecting the final determination by an investigating authority of whether or not dumping exists, would by definition be unfair.

G. ABITIBI

To Canada:

110. Based on information on record, how does Abitibi allocate financial expenses to various products in its normal cost accounting? Was this methodology "historically utilized"?

62. Under generally accepted accounting principles (GAAP) in both Canada and the United States, for financial and thus cost accounting purposes, financial expenses are regarded to be "period" expenses and not "product" expenses. A period expense is one that must be reported in full as belonging to the reporting period at issue, for example, the fiscal year in the current context. Thus, for financial and cost accounting purposes, Abitibi does not allocate financial expenses to its products on its books and records, and is not permitted to do so.

63. Financial expenses are simply reported as an independent line item on the income statement, below operating results. Even though GAAP does not permit financial expenses to be allocated to

²⁷ Indeed, this is in contrast to the provision at issue in the recent panel decision in *United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan*, where the panel found that the absence of an express reference to 2.4 in Article 11.3 precluded a claim of violation of the "fair comparison" requirement in the application of Article 11.3. (WT/DS244/R, 14 August 2003 (not yet adopted), at para. 7.166.)

specific products sold or produced during a period, Commerce does so in computing its costs of production.

64. The rules for financial accounting are driven by the goal of portraying accurately the financial position of the company. Because financial expenses such as interest expenses are recurring and not dependent upon what is produced or sold in a period, financial accounting rules generally require that they be treated as an expense in the period as incurred, in effect matched to the revenues of the same period for purposes of determining the company's profitability.

65. Significantly, financial accounting does not permit financial expenses to be reported as a cost of sales, because financial accounting recognizes that financial expenses bear no direct relationship to cost of sales.

111. In para. 71 of its Second Oral Statement, Canada alleges that DOC "allocated twice the interest expense actually incurred by relying on an unreasonable and unsupportable methodology". Could Canada please elaborate?

66. Canada's statement was based on the difference for Abitibi between the amount of interest expense allocated to lumber employing Abitibi's total asset-based methodology and the amount allocated to lumber by Commerce employing its cost-of-goods-sold (COGS) methodology. Exhibit CDA-91 compares Commerce's calculation to Abitibi's calculation for interest expense.

67. Under Commerce's methodology, 13.6% of Abitibi's total financial expenses were allocated to lumber compared to the 7.6% that would be allocated under the asset-based allocation methodology. This means that almost twice the expense was attributed to lumber by Commerce than actually incurred, as demonstrated in Abitibi's calculation based on the financial requirements of its different product lines.²⁸

112. In paras. 76-79 of its Second Oral Statement, Canada makes a number of allegations in support of its statement in para. 75 that DOC's "methodology is unreasonable because it considers the first only in part and does not consider the second at all." Please explain in detail why Canada would regard the asset-based methodology as being the only methodology that should be applied.

68. At paragraph 75 of Canada's Second Oral Statement, Canada notes that the COGS allocation methodology only considers "the amount of money needed to produce and sell a product" in part and does not consider "the amount of time for which that money is needed" at all. Therefore, it could not accurately or adequately capture the amount of Abitibi's total financial expenses associated with the production and sale of softwood lumber as opposed to Abitibi's other products.

69. As financial and cost accounting do not address how financial expense should be allocated to products, it is useful to return to basic principles to understand what financial expenses relate to. For example, suppose a person wanted to start a company to produce lumber and newsprint. Investors provide some capital, and the remaining money needed for this company is borrowed. Capital outlays would come first. For lumber, the company would need to buy land, construct a sawmill, and install all the necessary equipment and infrastructure. For newsprint, the company would need to buy land, construct a paper mill, and install all the necessary equipment. The funds needed for each of the two distinct product lines are directly proportional to the relative assets employed for each distinct business segment. Because money is fungible, the debt is not regarded to be tied to particular assets, but instead is regarded as relating to all assets equally. The financial expenses resulting from that debt thus are directly proportionate to asset values, not depreciation expenses, and not cost of sales.

²⁸ See Canada's Second Written Submission, at paras. 195-196.

Therefore, only the asset-based methodology reflects the financial expenses “associated with” or “pertaining to” each product line.

70. Next, operations begin. Raw materials for production are purchased, workers are hired, and energy and other expenses are incurred, as products are produced and sold. But the amount of funds required for such ongoing operations are not proportionate to the *total* current expenses for any given period of time. As lumber and newsprint are sold, customers pay for it. Thus, the funds needed for each of the two product lines depend on the expenses “outstanding” at any given point in time. As illustrated and explained in the flowchart provided in response to Question 115 below, these amounts consist of the actual expenses incurred for the raw material inventory that must be maintained, the actual expenses incurred for the work-in-process and finished good inventory that must be maintained to fill orders, and the value of the accounts receivables outstanding for sales of each product. These asset values alone reflect the cash needed to operate the two product lines on an ongoing basis. Again, the amount of money needed to establish and operate the two business segments – and thus the financing expenses incurred – is proportionate to asset values. In no way are financing expenses incurred in proportion to cost of sales. Again, only the asset-based methodology reflects the financial expenses “associated with” or “pertaining to” each product line.

71. Canada’s argument here is based on how companies actually utilize money. The US’ COGS methodology is not based on financial or cost accounting, and is not based on how companies utilize money. Indeed, the United States has not articulated any principled basis at all for allocating interest expenses in proportion to cost of goods sold.

72. In short, in light of Abitibi’s factual circumstances – the fact that it produces multiple, varied product lines, which lines have dramatically different asset requirements, and that its total asset needs far outstrip its annual cost of sales – the asset-based methodology is the only methodology that reasonably reflects how Abitibi actually utilizes its capital and money. Only the asset methodology fully considers:

- the complete range of activities for which companies expend funds,
- the amount of funds required for such activities, and
- the amount of time such funds are required.

73. Because the amount of a company’s interest expense is a function of all three of these elements, any methodology that fails to consider all such elements may not, depending on the particular circumstances, properly reflect the amount of interest expense “associated with” or “pertaining to” the production and sale of subject merchandise as required by Articles 2.2.1.1 and 2.2.2. of the *Anti-Dumping Agreement*.

74. In light of the factual evidence submitted by Abitibi to Commerce, the Panel is not presented with a choice between two “reasonable” allocation methodologies.²⁹ The COGS methodology, as applied to Abitibi, was unreasonable because it failed to meet the requirements of Articles 2.2.1.1 and 2.2.2, in multiple, independent respects that Canada has discussed in its prior submissions.³⁰ We highlight two examples here.

²⁹ Canada’s First Written Submission, at paras. 191-196; Canada’s First Responses to Questions, Annex 1, Abitibi Response; Canada’s Second Written Submission, at paras. 193-198.

³⁰ Canada’s First Written Submission, at paras. 190-199; Canada’s First Oral Statement, at paras. 80-85; Canada’s Second Written Submission, at paras. 200-208; Canada’s First Responses to Questions, at paras. 130-138; Canada’s Second Oral Statement, at paras. 74-78.

75. First, the plain language of both Articles 2.2.1.1 and 2.2.2 requires use of an allocation methodology that considers expenses associated not only with the *production* but also with the *sale* of the product under investigation. Commerce's COGS methodology, however, considers only production expenses (and even then, only current expenses without regard to the value of assets required for such production). Yet, because Abitibi is not paid immediately upon making a sale, Abitibi necessarily finances *sales* to its customers by the extension of credit until the customer pays.

76. The record evidence showed that this was an important consideration in regard to Abitibi's financing needs. Abitibi demonstrated to Commerce that it offered far more generous credit terms to its newsprint, pulp and paper customers than to its lumber customers, and that its lumber customers paid much more quickly.³¹ The shorter time period for payment meant lumber sales generated less financing needs. Commerce's COGS methodology utterly ignores the different financing expenses associated with the *sale* of lumber as opposed to pulp, paper, and newsprint, in violation of the plain language of Articles 2.2.1.1 and 2.2.2. The asset-based methodology, on the other hand, fully captures the different financial expenses associated with the *sale* of different products, because the value of accounts receivable for different products reflects differences in credit provided for different products, and accounts receivable are an asset included in the asset-based allocation. Commerce's methodology ignores the financing costs of accounts receivable entirely.

77. Second, and relatedly, is the distortion referenced in the question itself. The United States conceded in its First Written Submission that financial expense related both to cash outlays needed to acquire assets and to cash outlays needed to fund current expenses. But COGS only considers the latter – and considers even that incorrectly, as it simply totals the expenses without examining the actual amounts required to support such recurring expenses that are outstanding only until payment is received for the merchandise sold. Abitibi's evidence showed that in its case, the first use – assets – was far more significant than the second – current expenses – and, more importantly, that the relative asset needs of its different product lines differed dramatically. Therefore, assets could not simply be ignored.³²

78. During the period of investigation that Commerce examined, Abitibi had \$11 billion in assets but only \$4 billion in COGS. Yet, after acknowledging that Commerce had to consider both assets and current expenses, the United States is left to defend Commerce's COGS methodology which

³¹ See Canada's First Written Submission, at para. 195; Canada's First Responses to Questions, Annex 1, Abitibi Response; Canada's Second Written Submission, at paras. 205-206; Abitibi's 23 July 2001, Section D Response, at D-45 (Exhibit CDA-83 - Contains Business Confidential Information).

³² In *Final Determination of Sales at Less than Fair Value: Dynamic Random Access Memory Semiconductors of one Megabit and Above from the Republic of Korea*, Commerce's provides reasons for applying, in that case, an interest allocation in proportion to the fixed asset requirements of different product lines. These reasons are equally applicable here:

The Department generally accepts interest expense allocated by the cost of sales because that methodology often approximates the interest expense related to the production of the investigated merchandise. However, the Department has used other allocation methodologies when the facts of particular cases have required a change. After reviewing the facts in this case, we have found that for Samsung and Hyundai, a larger proportion of total fixed assets are related to the semiconductor line of business than to other lines of business. While the Department acknowledges that not all assets are financed through borrowings, it also recognizes that funds obtained from debt and equity are fungible and that the method used to finance the purchase of an asset is not relevant to the appropriate allocation basis. For these companies, because of this disproportional amount of fixed assets related to semiconductors, allocation of interest expense based on cost of sales would not appropriately recognize the expense related to the capital investment necessary for semiconductors compared to the other lines of business. Thus, the Department reallocated interest expense on the basis of proportional fixed assets to account for these facts.

58 Fed. Reg. 15,467 (Dep't of Commerce 23 March 1993), at 15,471-15,472 [hereinafter *DRAMS from Korea*] (Exhibit CDA-145).

considers only the less significant current expenses and ignores the more significant \$11 billion in assets. Absent some explanation of why it was necessary or appropriate to ignore \$11 billion in assets, it cannot be reasonable both to acknowledge that assets are financed and then ignore asset values in allocating financial expenses.

79. Moreover, the US argument that depreciation expense accounts for the differences in financing requirements generated by the different asset needs of different products, is completely incorrect. As Canada has demonstrated, when Abitibi purchases an asset it must pay for and finance the full value of that asset, not just its depreciation expense.³³ This means that by valuing financing requirements at the amount of a products' depreciation expense, the COGS methodology fails to consider the full amount that a company must finance to acquire an asset. Indeed, the distribution of Abitibi's depreciation expenses, by product line, is not even proportionate to the distribution of its asset values, by product line.³⁴ In no way can depreciation expenses serve even as a surrogate for asset values.

To the US:

114. Please comment on Canada's Second Oral Statement, para. 72 which states that:

"Commerce: asserted in the Final Determination that it used COGS, not because it was the proper methodology for Abitibi's facts, but because it was Commerce's "established practice" and was "consistent and predictable"."

80. Canada notes that the Final Determination contains no reference to any of the factual evidence submitted by Abitibi concerning the proper allocation of financial expenses, and that Commerce made no factual findings at all based on such evidence.³⁵

To both parties:

115. The Panel understands Canada to argue in para. 80 of its Second Oral Statement that an asset-based methodology can capture the flow elements through inventory. Please comment.

81. The Panel is correct in its understanding.

82. Throughout this proceeding, the United States has presented the Panel with a false argument: that assets are but one type of "activity" or "investment," and that Abitibi's asset-based methodology is flawed because it is a "limited basis," that fails to consider other, unidentified investments or activities and thus does not reflect Abitibi's "overall borrowing needs."³⁶ On the other hand, the United States has characterized Commerce's COGS methodology as "covering a wide range of costs,"³⁷ implying that it somehow is a broader basis than assets thereby justifying the COGS methodology.

³³ Canada's First Responses to Questions, at paras. 130-138, Annex 1 - Abitibi Response; Canada's Second Written Submission, at paras. 201-206.

³⁴ See Canada's Second Written Submission, at para. 195 (table showing lumber business segment required 7.6 per cent of Abitibi's total, company-wide assets but accounted for 10.6 per cent of company-wide depreciation expenses).

³⁵ IDM, Comment 15 (Exhibit CDA-2).

³⁶ See US Second Oral Statement, at para. 67; US Second Written Submission, at para. 74; US First Responses to Questions, at para. 61.

³⁷ US Second Written Submission, at para. 74.

83. Exhibit CDA-176 and paragraph 80 of Canada's Second Oral Statement demonstrate the falsity of that argument by showing (1) that "assets" is not simply one activity or type of investment, but rather comprehensively reflects all activities and expenditures in which a company engages, and (2) as an illustration, that *every single type of expense included in COGS also is included in the asset-based methodology*. Thus, applying the United States' own suggestion that limited allocation bases for financial expenses should be rejected in favour of broadly based allocations, the COGS methodology fails.

84. Exhibit CDA-181 explains further how every single item of expense in COGS is captured using an asset-based allocation.³⁸ This is a flowchart showing how all current production expenses flow through and thus are captured in asset values, at the same value as they are in COGS, for the precise amount of time in which the expense is outstanding and thus is financed, *i.e.*, before the lumber, newsprint, pulp, or paper that is sold is paid for by the customer. The flowchart uses lumber production as an illustration; similar charts could be created for Abitibi's other products showing their raw material inputs and production processes also flowing into asset values.

85. At the bottom of the chart, are listed all ongoing production expenses that are included in COGS and thus in Commerce's COGS allocation. The flowchart reflects the accrual accounting for lumber production and sale.

- The first step in the production process is the acquisition of raw materials – in the case of lumber, logs. As Abitibi harvests or purchases logs, and transports them to its sawmill, all of the actual expenses incurred – including labour, stumpage, fuel, and depreciation on logging equipment – are cumulated and booked to an asset account for raw materials/log inventory. They are NOT treated as an expense when incurred; as explained below, an expense is recognized only after the logs are used in production and the final product has been sold. As long as the logs remain in inventory, their cost remains in the value of raw materials/logs inventory.
- As logs are brought into the sawmill for manufacturing into lumber, the costs for those logs are subtracted from the raw materials inventory asset account, and other expenses are incurred for all the processing operations necessary to manufacture finished lumber. *All* of these additional expenses – for labour, plant and machinery depreciation, energy, overhead, etc. – are cumulated, added to the log costs, and booked to another asset account – finished goods inventory/lumber. Again, none of these costs are treated as an expense at the time they are actually incurred. Again, all of the actual costs remain in the value of finished goods inventory.
- When the lumber is sold, all of its costs of production, which have been held in the finished goods/lumber asset account, are transferred in Abitibi's records from that asset account to cost of goods sold, and recognized as an expense at that time. It is only at this time that all of these costs – which required cash at the time they were generated – are treated as an expense. The sales price of the lumber is recognized as revenue at the same time, and the difference between the sales value and the cost of goods sold is the operating profit.
- Importantly, the amount of the expense booked to cost of goods sold is *exactly the same* as the cost captured in finished goods inventory. That is, the COGS method and the asset-based method are using the same ongoing production costs.

³⁸ Flowchart Showing How All Expenses Flowing to COGS Also Flow to Assets at Equal Value, (Exhibit CDA-181).

- Also at the time of sale, the sale price of the lumber is booked to another asset account, the purchasing customer's accounts receivable for lumber. When Abitibi receives payment from the customer, the accounts receivable asset account is reduced by the amount of the payment, and the cash account is increased by the amount that Abitibi has received.

86. Thus, every single expense considered by Commerce in its COGS methodology is considered, at the same value, in the asset-based methodology.

87. In addition, the asset-based methodology – which the United States argues is less comprehensive than the COGS methodology – considers additional assets that Commerce's methodology considers either fractionally or not at all. These are all the asset categories identified in the top row of the flowchart. The flowchart thus demonstrates that the asset methodology, and not the COGS methodology, is comprehensive, and that the COGS methodology unjustifiably fails to consider entire categories of cash expenditures to which financial expenses need to be allocated. These are identified not only on the flowchart but also in Exhibit CDA-176.

88. Finally, as the above explanation makes clear, the US argument that COGS reflects all of the ongoing production expenses incurred during the year, simply is not true. COGS does not reflect the current expenses, or even expenses for products produced in the period. COGS instead reflects only the production expenses for products sold in the period. This creates yet another distortion, since Commerce's cost of production calculation is for products produced during the period.

116. Please indicate the advantages/disadvantages in this context, of the two approaches (COGS; asset-based) for allocating interest expenses.

89. The fact that Commerce did not even purport to answer this question in its Final Determination establishes Canada's claim that Commerce failed to consider all available evidence on the proper allocation of Abitibi's interest expense, contrary to Article 2.2.1.1. Canada submits that Commerce could not have "consider[ed] all available evidence on the proper allocation of costs" without assessing the advantages and disadvantages of the COGS and asset-based allocation methodologies in light of that evidence. Indeed, Commerce in its Final Determination nowhere identified any specific disadvantages of the asset-based methodology.³⁹ The only "advantage" it identified for the COGS methodology was that it was "consistent and predictable."

90. The starting point for answering this question must be to define a reference standard, or the objective of the interest expense allocation. An allocation methodology cannot possess advantages/disadvantages, or be considered to be "reasonable", in the abstract.

91. Canada has suggested several such reference standards. It has contended that a financial expense allocation methodology can be reasonable only if it achieves the objectives of Articles 2.2.1.1 and 2.2.2; that is, that it results in an allocation of interest expense to lumber that reasonably reflects the financial expenses with the production and sale of lumber. Relatedly, Canada has suggested as a reference whether or not the allocation methodology reflects the basis on which the expense to be allocated is incurred. For financial expenses, that basis would include consideration of (1) the full amount of the expenditure regarded as having been financed, and (2) the period of time for which it must be financed.

92. Tellingly, the United States, in contrast, offers the Panel no coherent reference standard, contending in its Second Written Submission only that Commerce's COGS methodology is reasonable because it "allocated interest costs across a wide range of costs."⁴⁰ There is no explanation

³⁹ IDM, Comment 15 (Exhibit CDA-2).

⁴⁰ US Second Written Submission, at para. 74.

as to why that should be the standard, nor is there even an argument that the COGS methodology uses the widest range of costs possible.

93. In light of the reference standards suggested above, Canada offers the following list of advantages and disadvantages based on its earlier submissions:

	ADVANTAGES	DISADVANTAGES
ASSET-BASED	<ol style="list-style-type: none"> 1. comprehensively considers all categories of company-wide expenditures, including all expenses included in COGS, and numerous expenditures not included in COGS 2. considers financial expenses associated both with the <i>production</i> and <i>sale</i> of the product under consideration 3. fully values all assets 4. considers time period for which expenditure is outstanding, consistent with how financing expenses are incurred 5. consistent with basis on which financial expenses are incurred 6. broadest allocation basis possible 7. accurately reflects the relative borrowing needs for different product lines, and thus results in an allocation to lumber of the financial expenses associated with and pertaining to the production and sale of lumber 	<ol style="list-style-type: none"> 1. can be used only for companies such as Abitibi that segregate assets by business line
COGS	<ol style="list-style-type: none"> 1. very simple to apply, and can be applied in every case because all financial statements state cost of good sold 	<ol style="list-style-type: none"> 1. considers current production expenses only 2. fails to consider financial expenses associates with the <i>sale</i> of the product under consideration 3. ignores entirely, for no stated reason, non-depreciable assets, like accounts receivable, land, investments in other companies, and, also with no stated justification, considers depreciable assets fractionally, at their depreciation expense rather than the full value that must be financed 4. fails to take into account the time period for which the expenditure is outstanding, and thus overstates financing requirements of current production expenses for products sold and paid for

	ADVANTAGES	DISADVANTAGES
		<p>5. results in a cost mismatch, in that an allocation based on products <i>sold</i> during the period is applied to the costs of products <i>produced</i> during the period</p> <p>6. bears no rational relationship to the basis on which financial expenses are incurred, and thus cannot determine the financial expenses associated with the production and sale of the product under consideration</p>

94. Canada also wishes to address two supposed disadvantages to the asset-based approach that have been suggested during the course of this proceeding, neither of which are correct. First, the United States has suggested that the asset-based methodology is inappropriate because it looks at values at one time only. This is an *ex post facto* argument not suggested by Commerce anywhere in its Final Determination. Indeed, if Commerce had actually raised this issue during the investigation, Abitibi could have provided quarterly or monthly data from which Commerce could have computed average asset values for the period of investigation.⁴¹

95. More importantly, the proportion of Abitibi's company-wide total assets devoted to Abitibi's different product lines does not change significantly over time. This can be confirmed with reference to data on the record before Commerce. For example, as we have noted, Abitibi's audited financial statement for 2000 evidences that Abitibi's lumber production and sales utilized 7.6 per cent of company-wide total assets.⁴² Abitibi also submitted to Commerce its financial statement for the First Quarter of 2001, which shows that lumber production and sales accounted for 7.4 per cent of company-wide total assets as of 30 April 2001 – the close of Commerce's period of investigation.⁴³ Thus, the US argument regarding "snapshots" is faulty.⁴⁴ Whether annual financial statements are used, or quarterly statements from the entire period of review are averaged, the results are not materially different – and are far from the 13.6 per cent COGS-based share of financial expense allocated by Commerce.⁴⁵

⁴¹ If Abitibi had done so itself, then the United States no doubt would now be arguing against such an approach (incorrectly, in Canada's view) because Abitibi's published quarterly financial statements, and its internal financial statements, are unaudited.

⁴² Abitibi Section A Questionnaire Response (22 June 2001), at 252 (Exhibit CDA-82). See also Canada's Second Written Submission, at para. 195.

⁴³ Abitibi's First Quarter Report, 2001, at 7, submitted to Commerce as Abitibi Section A Questionnaire Response (22 June 2001), Annex 12, at 302 (Exhibit CDA-182).

⁴⁴ US First Written Submission, at footnotes 220 and 223.

⁴⁵ Moreover, Abitibi's suggested approach was consistent with the approach Commerce itself has used previously. In *DRAMS from Korea* – the one case in which Commerce used an asset allocation methodology for financial expenses – Commerce calculated the percentage of assets devoted to the subject merchandise by averaging asset distributions measured on two days. Commerce looked to the company's audited financial statement alone and averaged the asset distribution on the close of that fiscal year and the close of the prior fiscal year. *DRAMS from Korea* (Exhibit CDA-145). Abitibi could not reasonably average its 31 December 2000 and 31 December 1999 data as the United States had suggested in its First Written Submission at footnote 223, however, because the 1999 data bore no relationship to the company that existed during the 1 April 2000 to 31 March 2001 period of investigation. In April 2000, Abitibi acquired a larger company, Donohue Inc., thereby almost tripling its assets. Commerce included both Abitibi and Donohue costs for the entire period of investigation, and therefore 1999 data were unrepresentative of the merged company for

96. Second, during the Second Substantive Meeting, the Chairman queried whether the asset-based methodology might be flawed because an asset could be fully depreciated yet still be incurring a financing expense. As an initial matter, Canada notes that this is not an issue that distinguishes the two allocation approaches. Under either methodology, no financial expense would be allocated to the business line utilizing that asset because the asset had no value (asset-based approach) and, because it had been fully depreciated, it would have no depreciation expense (COGS approach). More importantly, however, the scenario posed rests upon a faulty premise. Both Canada and the United States agree that money and debt are fungible. As a consequence, both Parties agree that financial expenses should not be tied directly to specific assets or activities, but instead must be allocated to the company's assets and activities as a whole. Moreover, nothing in Abitibi's financial statements or elsewhere on the record indicates that any of its debt is tied to specific assets.

97. In sum, although COGS may in some situations be acceptable, an asset-based allocation was the only reasonable methodology applicable in Abitibi's circumstances. Abitibi's different product lines had significantly different asset requirements, significantly different accounts receivable turnover, and therefore significantly different financing requirements. In these circumstances, the COGS-methodology did not result in an allocation of financial expenses that reasonably reflected the cost of production and sale of softwood lumber.

H. TEMBEC (G&A)

To Canada:

117. Based on information on record, how did Tembec allocate G&A expenses to the Forest Products Group? Was this methodology "historically utilized"? Please point to relevant documents submitted to the Panel or provide them.

98. Except for the cost category "administration fee – Head Office," all expenses falling within each of the cost categories comprising the Forest Products Group general and administrative expense (G&A) amount were, in fact, incurred at the divisional level.⁴⁶ For example, there is a human resources department within the Group whose salaries relate solely to the Forest Products Group and comprise a part of the G&A for the Group.

99. The cost category "administration fee – Head Office" represents the Forest Products Group's share of head office G&A, which in Tembec's normal books and records is allocated among its business segments according to the sales revenues of each business segment. This cost category represents a relatively small proportion of the total G&A of the Forest Products Group. Thus, G&A expenses are recorded for the Forest Products Group as part of Tembec's normal accounting procedures and there was no need to "allocate G&A expenses to the Forest Products Group" for purposes of the anti-dumping investigation.

100. The methodology Tembec used to report its G&A expenses for the Forest Products Group is the methodology that it uses in its normal books and records consistent with the accounting practice that Tembec has followed for many years. The accounting policies used in the business units are the same as those described in the summary of significant accounting policies for the entire company in Tembec's Annual Reports.⁴⁷ Tembec's Annual Report from 1994 describes the same accounting

which Commerce was computing costs of production. See Abitibi Section A Questionnaire Response (22 June 2001), at 252 (Exhibit CDA-82).

⁴⁶ The following cost categories comprise the submitted G&A costs: [[

]]. Tembec's Section D Questionnaire Response (23 July 2001), at D-28-29 (Exhibit CDA-183 – Contains Business Confidential Information).

⁴⁷ Tembec Section A Questionnaire Response (22 June 2001), Exhibit A-15, at 44 (Exhibit CDA-94).

methodology for business segments as the one described in Tembec's Annual Report from 2000.⁴⁸ Tembec has followed this same approach for more than ten years. Through the years, Tembec's internal accounting methodology has been consistent and reliable in calculating G&A expenses specific for each of its five business units.

101. Tembec provided detailed information to Commerce on the makeup of its Forest Products Group G&A in its first questionnaire response.⁴⁹ The financial statements of the Forest Products Group did contain complete G&A information, which Tembec provided to Commerce, including its fully allocated share of the head office G&A. Commerce officials, during verification, traced Tembec's G&A calculation to Tembec's Annual Report for 2000 as well as Tembec's detailed statement of costs through the company's consolidation software (*i.e.*, Hyperion).⁵⁰

118. Please comment on para. 70 of the US Second Oral Statement:

“unlike audited financial statements, internal, division-specific records are not intended as objective measures of a company's performance. Instead, the function of division-specific records is to “enable financial statement users to see the business through the eyes of the management.””

102. It is not obvious what distinction the United States is attempting to make in the above-quoted paragraph. Canada assumes the distinction is between audited accounting records and separate non-audited reports that management frequently creates for managerial as opposed to financial accounting purposes.

103. This distinction is not relevant to the G&A issue currently before the Panel. The statements from which Tembec derived its Forest Products Group G&A data are not managerial reports. They are part of Tembec's financial accounting records. As noted on page 44 of Tembec's Annual Report, the same accounting policies were used in preparing the Forest Products Group's statements as were used in preparing the consolidated company-wide financial statements.⁵¹ The Forest Products Group's accounting records tie directly into the consolidated company-wide financial statements and were reviewed by Tembec's auditors as part of the audit of the consolidated financial statements.⁵² As such they are an objective measure of the Forest Products Group's performance.

104. Commerce has relied upon these data in every other calculation methodology and Commerce officials personally verified their accuracy at Tembec. There is nothing in Article 2.2.1.1 or 2.2.2 that expresses a requirement or preference for audited records or consolidated statements. Further, nowhere in the Final Determination does Commerce state that its decision to reject the Forest Products Group data was based on the fact that the segmented statements were not audited or that

⁴⁸ Tembec Inc. 1994 Annual Report, at 20-22 and 38-39 (Exhibit CDA-184); Tembec Section A Questionnaire Response (22 June 2001), Exhibit A-15, at 44 - 45 (Exhibit CDA-94).

⁴⁹ Tembec's Section D Questionnaire Response (23 July 2001), at D28-29 (Exhibit CDA-183 – Contains Business Confidential Information).

⁵⁰ Tembec Cost Verification Exhibit 10 (Exhibit CDA-96) contains a consolidation worksheet from Hyperion which shows the aggregation of each of the function groups in addition to the aggregation of individual entities within the Forest Products Group. See DOC Verification Report on the Cost of Production and Constructed Value Data Submitted by Tembec Inc. (29 January 2002) at 8 (Contains Business Confidential Information) (Exhibit CDA-112). Tembec Cost Verification Exhibit 20 (Exhibit CDA-95) details the calculation of Tembec's G&A. The Commerce verifiers made handwritten notes on the exhibit stating the values used to derive the G&A expense ratio were traced to Tembec's FY 2000 Annual Report as well as the Hyperion Consolidated software.

⁵¹ Tembec Section A Questionnaire Response (22 June 2001), Exhibit A-15, at 44 (Exhibit CDA-94).

⁵² Tembec Section A Questionnaire Response (22 June 2001), Exhibit A-15, at 29 (Exhibit CDA-173).

segmented statements are, supposedly, only for managerial purposes. The attempt by the United States to do so now is simply an *ex post facto* rationalization.

To both parties:

121. Was the “internal accounting methodology” referred to in Comment 33, p. 105, of the Memorandum of 21 March 2002 an allocation methodology “historically utilized by the exporter”? Please refer to the record.

105. What Commerce referred to as Tembec’s “internal accounting methodology” is the accounting methodology that Tembec has used historically. Tembec has calculated its G&A expenses consistent with that methodology for at least the past 10 years. Canada refers the Panel to Canada’s answer to Question 117 for a more detailed description of Tembec’s historical utilization of its accounting methodology.

I. WEYERHAEUSER

To Canada:

122. On page 51 of the year 2000 annual report of Weyerhaeuser Company, it is stated under the heading “Contingencies” that “[t]he company is a party to legal proceedings and environmental matters generally incidental to its business. (...) (See Note 14 of Notes to Financial Statements)”. On page 53 of that document, note 14 appears immediately after the words “Charges for settlement of hardboard siding claims”. On page 74 of the same document, the title reads “Note 14. Legal proceedings, commitments and contingencies”. A statement to the same effect as that contained on the above-cited page 51 appears on page 74 of Weyerhaeuser’s annual report. Bearing this in mind, does not note 14 – and the comments contained therein – refer to all legal proceedings in which Weyerhaeuser Company was involved during year 2000? Does the amount of USD130 million reported on page 53, after the words “Charges for settlement of hardboard siding claims”, include the charge for settlement of hardboard siding claims only? Or, does it also include charges for legal proceedings, commitments and contingencies detailed in note 14?

106. As the Panel has noted, Note 14 on page 74 of Weyerhaeuser’s financial statement refers to all legal proceedings in which Weyerhaeuser Company was involved during 2000.⁵³ In discussing the hardboard siding expense, the Note states specifically that the hardboard siding expense amounted to an \$82 million after-tax charge. As stated on page 51 of Weyerhaeuser’s financial statement, the \$82 million after-tax charge is equivalent to a \$130 million pre-tax charge.⁵⁴ The \$130 million figure traces directly to page 53 of Weyerhaeuser’s consolidated statement of earnings, which includes a \$130 million charge related solely to the estimated cost of the hardboard siding settlement and related costs;⁵⁵ the \$130 million figure does not include charges for any other legal proceedings, commitments or contingencies.

107. The relationship between the \$130 million charge and the hardboard siding settlement expense is unambiguous. Commerce never expressed any doubt that the \$130 million charge related to the hardboard siding charge alone.

⁵³ Weyerhaeuser Section A Questionnaire Response (25 June 2002), Exhibit A-15 (Audited Financials), at 74 (Exhibit CDA-101).

⁵⁴ Weyerhaeuser Section A Questionnaire Response (25 June 2002), Exhibit A-15 (Audited Financials), at 51 (Exhibit CDA-166).

⁵⁵ Weyerhaeuser Section A Questionnaire Response (25 June 2002), Exhibit A-15 (Audited Financials), at 53 (Exhibit CDA-101).

108. The United States in its Second Oral Statement expressly stated that Commerce, as a matter of practice, does not allocate any parent company G&A to a subsidiary where the parent performs no functions on behalf of the subsidiary.⁵⁶ In other words, the allocation of parent G&A to the subsidiary is not automatic, but rather depends on the extent to which the G&A relates to activities of the parent performed on behalf of the subsidiary. Indeed, Commerce at Comment 48(a) of its Issues and Decisions Memorandum – in respect of certain Weyerhaeuser US G&A expenses related to real estate – stated that it was proper to allocate only those headquarters G&A incurred on behalf of its subsidiaries.⁵⁷

109. The hardboard siding expense was not a general expense for Weyerhaeuser Canada and was not an expense incurred by Weyerhaeuser US on behalf of Weyerhaeuser Canada. The expense does not even relate to softwood lumber. Yet despite this Commerce included the hardboard expense as a cost attributable to softwood lumber production. Commerce's inclusion of a charge related to hardboard siding – a non-like product that was outside the scope of its investigation – in its G&A expense calculation clearly violated Articles 2.2.1.1 and 2.2.2 of the *Anti-Dumping Agreement*.

J. TEMBEC (BY-PRODUCT REVENUE)

To the US:

129. Canada draws an analogy between the present case and the finding in para. 148 of the AB in *US - Hot-Rolled Steel* that “discretion must be exercised in an even-handed way that is fair to all parties affected by an anti-dumping investigation.” Please comment.

110. In *United States – Hot Rolled Steel*, the Appellate Body considered Commerce's test for reviewing affiliated transactions for purposes of calculating Normal Value.⁵⁸ It concluded that the discretion afforded to investigating authorities must be exercised in an even-handed manner. It found that Commerce's test was not even-handed because it “operated systematically to raise normal value, through the automatic exclusion of marginally low-priced sales, coupled with the automatic inclusion of all high-priced sales”.⁵⁹

111. Commerce applied a *nearly identical* test, but in reverse, to assess whether to use Tembec's internal transfer prices.⁶⁰ This test also suffers from the same lack of even-handedness. In relation to West Fraser, Commerce rejected affiliated transactions as preferential after concluding that these transactions were slightly above the unaffiliated benchmark. In contrast, Commerce found that Tembec's internal transfer prices were non-preferential even though they were significantly below the unaffiliated benchmark. This inconsistent approach was not even-handed and served only to prejudice these exporters by raising their dumping margins.

130. Please comment on para. 107 of Canada's Second Oral Statement.

112. Canada would like to comment briefly on paragraph 107 and Exhibit CDA-175. Canada reviewed a considerable amount of accounting literature, none of which supported the distinction that the United States attempts to draw between internal transfers and affiliated transfers for by-product

⁵⁶ US Second Oral Statement, at para. 73.

⁵⁷ IDM, Comment 48(a), at 133 (Exhibit CDA-2).

⁵⁸ *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, Report of the Appellate Body, WT/DS184/AB/R, adopted 24 July 2001 [hereinafter *US – Hot Rolled Steel*].

⁵⁹ *Ibid.*, at paras. 148 and 155.

⁶⁰ *Ibid.*, at paras. 154-158.

revenue offsets.⁶¹ Canada provided Exhibit CDA-175 as an example of the accounting literature discussing the proper treatment of this type of revenue offset *within a corporation*. The exhibit draws no distinction between internal transfers and affiliated transfers.

113. In the Second Substantive Meeting, the United States attempted to assert that this exhibit supported its position that there is a cost of production for a by-product. It referred to the use of the word “cost” in the exhibit in support of its position. A careful review of the exhibit, however, demonstrates that it undermines, rather than supports the US position.

114. This text discusses the miscellaneous income approach and the net realizable value method for accounting for the value of waste, scrap and by-products. The first method is only appropriate as an accounting “short-cut” when the value of the by-products or scrap is uncertain or very small.⁶²

115. The second method was selected by Commerce in the underlying investigation. In this method, the *net realizable value* of the by-product (wood chips) is offset against the cost of production of the major product (softwood lumber). The net realizable value method is used to measure the value of: (1) by-products; and (2) waste or scrap that is processed subsequently into a saleable product.

116. The net realizable value method values by-products at their “selling price” or market value. After the “split off” from the major product some forms of waste may be further processed into by-products. In this situation, the net realizable value method values the by-product produced from the waste at market value less the cost of any further processing that was required after the “split off” from the major product.⁶³ Applied to the present situation, wood chips are by-products that do not require further processing to become a saleable product. Accordingly, wood chips must be valued at market value.

117. Canada reserves its right to comment on any explanation the United States provides concerning its internal transfer methodology.

K. WEST FRASER

To Canada:

131. Based on information on the record at the time of the investigation, please provide the total volume (in ODTs) of wood chips sold by West Fraser in British Columbia. Please provide separately for the same market, the volume (in ODTs) of wood chips sold to affiliated and unaffiliated parties.

118. The total quantity of wood chips sold by West Fraser in British Columbia during the period of investigation amounted to [[]].⁶⁴ Of this total quantity, [[]] (which accounted for 99.7 per cent of West Fraser’s total wood chip sales) were sold in affiliated transactions.⁶⁵ In contrast, only [[]] were sold in unaffiliated transactions (an amount that a large pulp mill would consume in less than one day).⁶⁶ As outlined in Canada’s previous submissions, these unaffiliated

⁶¹ The US methodology would even distinguish between internal transfers and transfers between a parent corporation and a wholly owned subsidiary.

⁶² W.J. Morse and H.P. Roth, *Cost Accounting: Processing, Evaluating, and Using Cost Data*, 3rd ed. (Reading, Mass.: Addison-Wesley, 1986), at 158 (Exhibit CDA-175).

⁶³ *Ibid.* (Example 5-7).

⁶⁴ West Fraser Cost Verification Exhibit C5, WF-Cost-007503, Appendix D-2 Revised, “Residual Chip Sales” (Exhibit CDA-106).

⁶⁵ *Ibid.*

⁶⁶ *Ibid.*

transactions only amounted to less than 0.3 per cent of record evidence concerning B.C. market prices during the period of investigation.

132. Canada has stated in the Second Substantive Meeting that prices concerning the long-term contract of the McBride mill fluctuate. Could you please confirm that?

119. As a threshold matter, Canada would like to observe that the record evidence is limited concerning the exact details of the McBride wood chip contract. Commerce's Cost Verification Report shows that West Fraser officials discussed the wood chip issue with Commerce's verification team and made those officials aware that a long-term contract (entered into before West Fraser purchased the mill) obligated McBride to sell wood chips at a lower contracted price when market prices began to increase in May 2000.⁶⁷

120. In the interest of responding to the Panel's question, however, Canada can confirm that prices under the long-term contract of the McBride mill did in fact fluctuate. The McBride contract set prices at the beginning of each calendar quarter based on market conditions in the previous quarter. As wood chip prices had already been set for the second quarter of 2000, McBride was unable to increase its prices when the market value of wood chips increased in May 2000⁶⁸, as reflected in Commerce's cost verification report. It is important to note that all wood chip sales from McBride during the period of investigation occurred in the first two months (*i.e.*, April and May 2000).

L. SLOCAN

To Canada:

134. Based on information on record, where in Slocan's books is the revenue generated by, and cost associated with, the sale of a futures contract accounted for? Please explain it in detail.

121. As explained in Canada's response to the first questions, Slocan treated liquidated hedging contracts as US lumber sales and listed the Chicago Mercantile Exchange (CME) as the customer.⁶⁹ In Commerce's sales verification report the verifiers misstate that these futures revenues were recorded as a form of investment profit.⁷⁰ Afterwards, Slocan clarified its treatment of futures revenues explaining that:

The Sales Verification Report is somewhat unclear in its statement on page 8 that Slocan records the profits or losses realized from futures contracts as investment income. In all cases, including where no physical delivery is made, Slocan records the profits or losses as a credit or debit to lumber sales revenue. These profits or

⁶⁷ DOC Verification Report on the Cost of Production and Constructed Value Data Submitted by West Fraser Mills Ltd. (4 February 2002) at 23 (Contains Business Confidential Information) (Exhibit CDA-110).

⁶⁸ See 2000 Chip Prices for Purchases by Quesnel River Pulp (Contains Business Confidential Information) (Exhibit CDA-174). This exhibit reflects the increase in wood chip prices in April and May of 2000.

⁶⁹ Canada's First Responses to Questions, Question 79, at para. 198.

⁷⁰ DOC Memorandum on Verification of the Sales Response of Slocan Forest Products Ltd (28 January 2002), at 8 [hereinafter "Slocan Sales Verification Memorandum"] (Exhibit CDA-117). The verifiers may have been attempting to reconcile Slocan's records with Commerce's Preliminary Determination Analysis Memorandum, which had concluded that Slocan's futures activities were a form of investment revenue. See DOC Analysis Memorandum for Slocan Forest Products Ltd. for the Preliminary Determination in LTFV Investigation on Certain Softwood Lumber Products from Canada (30 October 2001), at 7 (Exhibit CDA-116).

*losses are not recorded in an investment account in Slocan's books and financial statements.*⁷¹

122. Slocan treated futures revenues as an integral portion of lumber selling activities. As Commerce concluded in the Final Determination "Slocan's lumber futures hedging activity is related to its core business of selling lumber".⁷²

135. Did Slocan argue and demonstrate in the context of the investigation that, because of its engagement in futures trading activities, price comparability was affected? If so, please provide relevant document/s substantiating it.

123. Slocan argued and demonstrated that its futures activities affected price comparability in the underlying investigation. In its questionnaire response Slocan requested an adjustment for its futures revenues, which by definition meant that Slocan was taking the position that price comparability was affected by its futures hedging activities.⁷³ Slocan also undertook to explain the significance of its futures hedging activities to both Commerce's sales verification and cost verification teams. It is for this reason that these activities are described in both reports, and why both reports contain materials explaining the purpose and significance of hedging, as well as detailed data concerning Slocan's actual futures activities.⁷⁴ Slocan also argued that futures hedging affects price comparability in its Case Brief:

*Slocan relies on futures sales as part of its sales profile to hedge against price movements. Slocan locks in a certain portion of its sales at a guaranteed price through futures contracts with the Chicago Mercantile Exchange (CME), and Slocan thereby forgoes possible increased profits in order protect (i.e., hedge) against possible future price declines. ... While futures contracts can be used for speculation, Slocan uses the CME for exactly the opposite reason, as price protection to reduce its risk by locking in a certain portion of its sales.*⁷⁵

124. This hedging occurred, of course, only with respect to the US market, price protection being unavailable in the Canadian market.

125. Slocan also provided the following evidence to demonstrate the effect of futures hedging:

- Evidence concerning the existence and amount of the futures revenues;⁷⁶

⁷¹ Slocan Case Brief (12 February 2002), at 70 footnote 24 (Contains Business Confidential Information) (Exhibit CDA-156) (emphasis added).

⁷² IDM, Comment 21, at 94 (Exhibit CDA-2).

⁷³ Slocan Section C Questionnaire Response (23 July 2001), at C-35 - C-36 (Exhibit US-71). Commerce questionnaires require that respondents report adjustments that should be made. Commerce chose, however, not to make this adjustment, despite evidence that Slocan placed on the record concerning its futures trading activities, and Commerce's conclusion that these revenues constitute an offset to indirect selling expense under US law.

⁷⁴ Slocan Sales Verification Memorandum, at 7-8 (Exhibit CDA-117); and DOC Verification Report on the Cost of Production and Constructed Value Data Submitted by Slocan Forest Products Ltd. (1 February 2002), at 26 [hereinafter "Slocan Cost Verification Report"] and Slocan Sales Verification Exhibit 21 (Exhibit CDA-118 and 119). Sales Verification Exhibit 21 provides an explanation of the purpose and effect of lumber futures contract. It also contained much of the standard documentation for lumber futures activities.

⁷⁵ Slocan Case Brief (12 February 2002), at 67-68 (Exhibit CDA-156) (emphasis added).

⁷⁶ Slocan Section C Questionnaire Response (23 July 2001), at C-35 - C-36 (Exhibit US-71). This futures revenue was reported in a US sales database field labelled DIRSELU2. Commerce also verified that Slocan had accurately reported this data. See Slocan Cost Verification Report, at 26 (Exhibit CDA-118). There was never any dispute concerning the existence or amount of the futures revenues.

- Evidence that these futures revenues only relate to the US market;⁷⁷
- Slocan's treatment of futures revenue in its books and records as lumber sales revenue;⁷⁸
- An explanation of the purpose and effect of futures hedging contracts for lumber prepared by the CME;⁷⁹
- Slocan's hedge approval for the CME (demonstrating that Slocan was a hedger rather than a speculator);⁸⁰
- Slocan's standard futures hedging contract;⁸¹ and
- Slocan's hedging account designation agreement with its broker.⁸²

126. Most tellingly, as the United States conceded in the Second Substantive Meeting, Commerce has concluded that these futures revenues constitute an offset to indirect selling expenses. This concession is itself an admission that Commerce in fact concluded that Slocan had *demonstrated an effect on price comparability*. Consequently, Commerce was required to make an adjustment of some kind to ensure a fair comparison.

127. The United States repeatedly refers to irrelevant aspects of its own domestic law to argue that Commerce was not required to provide an adjustment. In effect, the United States claims that Slocan was required to "guess" the right type of US domestic law adjustment, before Commerce would provide this adjustment. This is not, however, a prerequisite to a proper adjustment for a difference affecting price comparability under Article 2.4 of the *Anti-Dumping Agreement*.

128. In *United States – Hot Rolled Steel*, the Appellate Body found that Article 2.4 requires that appropriate "allowances" must be made to ensure a "fair comparison".⁸³ The Appellate Body also explained that "under Article 2.4, the obligation to ensure a 'fair comparison' lies on the *investigating authorities*, and not the exporters."⁸⁴ As the panel in *Egypt – Steel Rebar* concluded, this type of explicit obligation must be "performed by the investigating authority on its own initiative, and exactly as specified in the *Anti-Dumping Agreement*".⁸⁵ Finally, Article 2.4 also places the obligation on the investigating authority to "indicate to the parties in question what information is necessary to ensure a fair comparison" if the requisite information has not been provided. At no point in time did Commerce request additional evidence from Slocan to demonstrate an effect on price comparability.

⁷⁷ *Ibid.* The database field DIRSEL2 was only found in the database relating to US sales. There is no futures market that is comparable to the CME in Canada.

⁷⁸ Slocan Case Brief (12 February 2002), at 70 fn 24 (Exhibit CDA-156). Also see US First Written Submission, at para. 246; US First Answers to Questions, at fn 77 and para. 138; and IDM, Comment 21, at 94 (Exhibit CDA-2).

⁷⁹ Chicago Mercantile Exchange, "An Introductory Hedge Guide - Random Lengths" (Chicago: Chicago Mercantile Exchange, 2000), Slocan Sales Verification Exhibit 21, at VE02362 - VE02380 (Exhibit CDA-119).

⁸⁰ Chicago Mercantile Exchange, "Year 2001 Hedge Approval" (29 December 2000), *ibid.*, at VE 02428 – VE02429.

⁸¹ Merchants Trading Company, "Customer Information Sheet – Customer Agreement", *ibid.*, at VE0281 – VE02382.

⁸² Merchants Trading Company, "Hedging Account Designation", *ibid.*, at VE 02386.

⁸³ *US – Hot Rolled Steel*, at para. 176.

⁸⁴ *Ibid.*, at para. 178 (emphasis in original).

⁸⁵ *Egypt – Definitive Anti-Dumping Measures on Steel Rebar from Turkey*, Report of the Panel, WT/DS211/R, adopted 1 October 2002, at para. 7.2.

129. As outlined above, Commerce has determined that these futures revenues were an offset to “indirect selling expenses” that affect price comparability. As there was an effect on price comparability, Article 2.4 required Commerce to provide an adjustment of *some kind*. Further, Commerce was required to provide this adjustment even if it determined that “direct selling expenses” were not the proper form of adjustment under US domestic law. Commerce was not free, however, to ignore the effect on price comparability altogether, and to make no adjustment whatsoever.

130. Finally, the United States attempts to argue that “direct selling expenses ...[are] a type of adjustment for differences in conditions and terms of sale.”⁸⁶ Although “direct selling expenses” might often constitute “conditions and terms of sale” these expenses will sometimes more properly relate to other listed differences in Article 2.4. A simple example is illustrative. In the underlying investigation, Softwood Lumber Agreement (SLA) taxes were deducted as “direct selling expenses”.⁸⁷ Article 2.4 requires that due allowance is made for differences relating to “taxation”. As an export tax these SLA tax revenues more properly relate to “taxation” rather than “conditions and terms of sale”. Moreover, Commerce’s treatment of these revenues confirms that the SLA taxes are a difference in “taxation”. Commerce deducted SLA taxes as “direct selling expenses” from all sales, including sales for which there were *no SLA taxes applied*. As a result, these SLA taxes could not constitute a “condition or a term of sale” in any ordinary understanding of this term.⁸⁸ In a similar manner, “direct selling expenses” that do not constitute “conditions and terms of sale” might also fall under the ambit of “other” differences affecting price comparability.

131. Which particular adjustment should have been made under US domestic law is a matter that this Panel need not decide, and it is not a matter that Canada has asked this Panel to decide. What *is* a matter for this Panel to decide is whether Commerce was free to make no “due allowance” whatsoever for a difference that, the United States now acknowledges, affected price comparability.

136. Please comment on para. 138 of the US reply to Question 83 of the Panel:

“as noted in paragraph 246 of the US First Written Submission, it would have been inappropriate for Commerce to disregard Slocan’s own treatment of the profits as linked, albeit indirectly, to lumber sales and instead treat them as offsets to cost of production.”

132. Although Slocan’s treatment of futures revenues in its records is persuasive as to the proper treatment of these revenues, it is not conclusive.

133. Commerce’s reliance on these records was not consistent. As outlined above, Slocan treated liquidated hedging contracts in its records as a form of lumber sales revenue. If Slocan’s records were determinative of the treatment for futures revenues then Commerce should have provided a “direct selling expense” adjustment. Instead, Commerce ignored these records and refused a “direct selling

⁸⁶ US First Answers to Questions, Question 83, at para. 145.

⁸⁷ SLA taxes were an export tax collected by the Canadian government on lumber exports in excess of predetermined quota limits.

⁸⁸ “[T]he phrase ‘conditions and terms of sale’ refers to the *bundle of rights and obligations created by the sales agreement*, and ‘differences in conditions and terms of sale’ refers to differences in that bundle of contractual rights and obligations.” (emphasis added) *United States – Anti-Dumping Measures on Stainless Steel Plate from Korea*, Report of the Panel, WT/DS179/R, adopted 1 February 2001, at para. 6.75. In this proceeding, the United States took the position that “conditions and terms of sale” has a much broader significance. If that was the US position under its domestic law during the investigation, then the futures revenue should have been considered a condition and term of sale and the revenue treated as a “direct selling expense.”

expense” adjustment.⁸⁹ It then used the same records to support its determination that futures revenues were not a form of investment income.⁹⁰ This selective reliance on Slocan’s records is neither even-handed nor objective.

To both parties:

140. Please provide in diagram format the company structure of Weyerhaeuser International Inc., showing the relationship between Weyerhaeuser Canada, Weyerhaeuser US and Weyerhaeuser International Inc. In addition, could Canada provide the structure of the financial records of the different entities, that is, at which level are they audited/consolidated.

Corporate Structure

134. The respondent in the softwood lumber investigation was Weyerhaeuser Company, a US company based in Washington State.⁹¹ Weyerhaeuser Company owns [[]] of Weyerhaeuser International Inc., which is also a US company. Weyerhaeuser International Inc. owns [[]] of Weyerhaeuser Canada Limited, which produced and exported the Canadian softwood lumber that was subject to the investigation.⁹² The remaining [[]] of Weyerhaeuser Canada Limited is owned by Weyerhaeuser Holdings Limited, a British Columbia (Canada) company that is [[]] owned by Weyerhaeuser International Inc. This relationship is depicted in the attached Exhibits.

135. Attached as Exhibit CDA-189 is a set of four diagrams of Weyerhaeuser's corporate structure. The first three documents are linked.

- The first page includes all of Weyerhaeuser Company’s US organization. Weyerhaeuser International Inc. is listed on this page.
- The second page is a breakdown of Weyerhaeuser International. Weyerhaeuser Canada is on this page, as is a breakdown of Weyerhaeuser Canada.
- The third page is simply an enlarged version of the Weyerhaeuser Canada Limited section of the chart shown on page 2.
- The fourth page is a simplified version of the overall corporate structure involving these companies.

Financial Records

136. Weyerhaeuser Company, the overall US parent company, prepared consolidated financial statements. Since Weyerhaeuser Company is both an operating unit (managing the company’s US operations) and corporate headquarters for the company’s global operations, operating expenses and corporate expenses appear on Weyerhaeuser Company’s financial statements. Commerce’s task

⁸⁹ IDM, Comment 21, at 94 (Exhibit CDA-2).

⁹⁰ US First Written Submission, at 246; US First Answers to Questions, at fn 77 and para. 138; and IDM, Comment 21, at 94 (Exhibit CDA-2). The IDM states that “While we agree that Slocan’s lumber futures hedging activity is related to its core business of selling lumber as opposed to speculative investment activity, it is for this very reason that we disagree that the futures contracts are related to Slocan’s financing activity.”

⁹¹ This company was referred to as Weyerhaeuser US for the purposes of the submissions filed in this dispute.

⁹² Weyerhaeuser Canada Limited was referred to as Weyerhaeuser Canada for the purposes of the submissions filed in this dispute.

during the investigation was to isolate those corporate expenses that were attributable to the production and sale of softwood lumber by Weyerhaeuser Canada Limited, its Canadian business.

137. Weyerhaeuser International did not prepare consolidated financial statements.

138. Weyerhaeuser Canada Limited prepared financial statements for its own operations, in accordance with US Generally Accepted Accounting Principles, that Commerce relied on during the investigation.⁹³ All G&A expenses associated with the production and sale of Canadian softwood lumber appeared on Weyerhaeuser Canada's financial statements. The hardboard siding expense did not appear on Weyerhaeuser Canada's financial statement because it was an expense related solely to Weyerhaeuser Company's US operations.

139. Commerce committed an error when it attributed the hardboard siding expense to the production and sale of softwood lumber because the hardboard siding expense related to Weyerhaeuser Company's US operations; it was not a Company-wide headquarter expense incurred on behalf of Weyerhaeuser Company's global business.

140. Attached as Exhibit CDA-190 is a narrative portion from Weyerhaeuser's Section A Response to Commerce⁹⁴, discussing the financial statements produced by Weyerhaeuser Company.

⁹³ Weyerhaeuser Section A Questionnaire Response (22 June 2001) at A-52 (**Contains Business Confidential Information on page A-52**) (Exhibit CDA-190).

⁹⁴ Ibid., at A-52 – A-54.

ANNEX B-2

RESPONSES OF THE UNITED STATES TO QUESTIONS POSED IN THE CONTEXT OF THE SECOND SUBSTANTIVE MEETING OF THE PANEL

(26 August 2003)

1. The following responses of the United States answer the 13 August 2003 questions to the United States and to both parties. In several instances, the United States has also addressed questions posed by the Panel to Canada.

A. GENERAL QUESTIONS

To the US:

86. The Panel refers to paras. 2 and 3 of the US Second Oral Statement. The Panel requests the US to note all the "misstatements" that it has identified in Canada's submissions, in addition to those mentioned in the Second Oral Statement. Further, in its replies to the questions posed by the Panel, Canada's Second Written Submission and Second Oral Statement, Canada made detailed factual presentations relevant to its claims. The US is requested to identify and substantiate all factual aspects with which it disagrees with Canada.

2. In response, the United States refers the panel to the chart at the Attachment hereto.

3. The United States has diligently reviewed each of Canada's submissions and statements to respond to the Panel's question. In that process, the United States identified numerous misstatements and factual aspects of Canada's argument with which it disagrees. Each of these is catalogued in the Attachment. However, the absence of a particular statement by Canada from the Attachment should not be construed as a concession or as agreement with the substance of that statement.

4. Canada's statements that the United States would describe as "misstatements" or with which the United States disagrees are too numerous to be comprehensively catalogued. For example, inasmuch as the United States disagrees with Canada's interpretations of AD Agreement articles, the United States would describe Canada's statements concerning those articles as "misstatements." The United States has addressed those arguments in its prior submissions and statements and does not separately identify them in the Attachment.

B. ARTICLE 5.2:

To Canada:

87. The Panel notes that Canada has made a number of allegations on shortcomings of the data in the application in Section II of its Second Oral Statement. In Canada's view, does the examination it claims should have been done by the DOC, require a pre-initiation investigation?

5. The United States has argued that Canada's interpretation of Article 5.2 effectively would require an investigating authority to undertake a pre-initiation inquiry. Under Canada's theory, an authority would have to satisfy itself that an application contained *all* information reasonably available to the petitioner on the subjects specified in Article 5.2. Put another way, the authority would have to determine what information was reasonably available to the petitioner (potentially, a very broad universe of information) and whether any of that information had been excluded from the application. The only way to make such a determination would be to conduct an investigation. The United States has observed, in general, the impracticality of requiring such an investigation, as well as the absence of any such requirement in the AD Agreement.¹ The United States would only add that, under Canada's theory, this requirement would not be limited to information on dumping. It presumably would extend to each of the other categories of information specified in Article 5.2. This would include, for example, information on impact of the imports on the domestic industry. A petitioner's information on that particular issue is likely to be very expansive. It is inconceivable and illogical that Article 5.2 would require a petitioner to provide *all* information reasonably available to it on that topic.

C. ARTICLE 5.3:

To Canada:

88. In paras. 34 to 43 of Canada's reply to Question 8, Canada has made certain allegations regarding the information contained in the application as submitted by the US domestic industry, and which formed the basis for the initiation of the investigation. In its Second Oral Statement, Canada has also alluded to some of these issues. Could the US please comment in detail on these allegations?

6. Canada's 30 June 2003, response to Question 8 included claims regarding the alleged failure of the application "to have costs of significant or representative producers" (paras. 34-35); "to provide costs for a period of time sufficient to objectively assess the reasonableness of the data submitted" (para. 36), and to include "evidence of the method used to calculate manufacturing costs for the SPF species" and evidence of "how company costs were allocated to the specific 2.4 kiln-dried dimension or stud lumber" (paras. 37-38). The same response also included claims related to the alleged failure of the application to "contain adequate information regarding freight costs" (paras. 39-43).

7. The United States addressed each of these issues in its 9 July 2003, Second Written Submission, at paras. 23-32, and refers to those detailed answers and the supporting evidence cited therein. Because Canada's response to Question 8 contained numerous factual misstatements, the United States also refers to the US response to Question 86, set forth as an Attachment to this submission. In brief, the United States addressed the cost and price issues that Canada raised as follows.

8. In response to Canada's claims regarding costs from significant or representative producers:

- The vast majority of the "costs" used in the application were derived from sources Canada has not challenged (including a significant amount of cost data from Canadian government sources). The data from US mills were used primarily to identify production factors, rather than costs.²
- To the extent that Canada is criticizing the sources as a basis for identifying production factor data, the United States explained that what Canada referred to as "the Canadian producers

¹ US First Written Submission, paras. 70-76; US Opening Statement at First Panel Meeting, para. 22; US Second Written Submission, paras. 10-13; US Opening Statement at Second Panel Meeting, paras. 11-21.

² See US Second Written Submission, para. 24.

being modelled” included the entire Canadian softwood lumber industry (not merely the very largest producers that were subsequently selected as respondents). The lumber industry is disaggregated and diverse, and the mills whose production factors were included in the application were among those listed in a US Department of Agriculture publication focusing on “large, permanent operations that make up the bulk of the industry.”³³

9. In response to Canada’s claims regarding costs for a period of time sufficient to objectively assess the reasonableness of the data submitted:

- As reflected in the exhibits it references, Canada’s argument regarding what it broadly terms “cost” data applies, in fact, only to the US mill data on factor usage. Furthermore, taken as a whole, these data, when combined, not only cover the full calendar year 2000 on a country-wide basis, but also include data on both the British Columbia and Quebec markets. The confidential affidavits, furthermore, explain why data for particular months are provided for particular mills, including when particular mills close their financial statements.⁴

10. In response to Canada’s claims regarding a lack of explanation of how manufacturing costs were calculated and allocated:

- The United States has pointed out that the application followed the normal industry practice (as reflected in industry patterns of data collection and cost breakouts) of allocating costs, for the most part, on a per-MBF, species-specific basis. The United States also explained that when a broader species average was used (*i.e.*, for stumpage costs in Quebec), this actually favoured respondents by resulting in lower costs, and, thus, lower margins.⁵ Although the cost allocation methodology used in the application may not have been as refined as that developed in the course of the investigation, it permitted Commerce to reasonably ascertain product costs for purposes of initiation. This can be seen from the fact that the evidence of below-cost sales was corroborated both by the press articles in the application and by the extensive below-cost sales found in the investigation using the respondents’ own cost data and more detailed cost allocation methodologies.

11. In response to Canada’s allegations regarding freight data:

- The United States clarified that, as Quebec producers ship lumber both by truck and by rail, it was appropriate to use a truck shipment rate from a producer that shipped by truck. Commerce also properly relied upon a rail freight rate for “softwood lumber” without seeking out data on the comparative weight of different pine species, especially in view of the fact that the quotation at issue was for transfer over a considerably shorter distance than the delivery distance associated with the export sales for which an estimated freight expense was being calculated. In other words, the quotation likely had the effect of understating the actual cost of transporting lumber for the transactions at issue. Finally, the United States clearly demonstrated from the record that its calculations did not, as Canada claimed, include the cost of freight from the Maritime Provinces in its average cost for freight from Quebec.⁶

12. In its oral statement at the second substantive meeting, Canada addressed almost none of these points or the evidence relied upon by the United States.⁷

³ See *id.*, para. 25.

⁴ See *id.*, para. 26.

⁵ See *id.*, paras. 27-28.

⁶ See *id.*, paras. 29-32.

⁷ In its discussion of these issues in Canada’s Second Oral Statement, the only explicit reference to the US Second Written Submission argues that the US never made a “finding” that the allocation by MBF and species was consistent with “normal industry practice.” Here, also, Canada offers no evidence to contradict this

89. In its reply to Question 8, Canada submits that using the Applicant's Random Lengths price data for Quebec, a comparison of all of the Quebec ex-factory price data for ESPF (2x4, Studs&Btr, KD, RL and 2x4-8', PET, KD) products sold in Quebec and in the US, shows that the US price was consistently higher during the period and that there was therefore no price-to-price dumping demonstrated by the evidence in the Application. It further provides a calculation in footnote 32 to substantiate the allegation. Could the US please comment on this allegation and on the calculations?

13. Both the allegation and the calculation are irrelevant to the question of whether Commerce properly initiated and continued the investigation, because neither the application nor Commerce's decision to initiate was based on price-to-price dumping. As Commerce explained in its initiation checklist, "Because the Canadian prices, when compared to the COP, were demonstrated to be below the COP, petitioners have based their margin calculations on the comparison of {export price} to {constructed value}."⁸ This comparison of export prices to constructed value demonstrated that softwood lumber was sold at prices below the cost of production, *i.e.*, dumped.

90. Please comment on Canada's Second Oral Statement, para. 20 which states that:

"[t]he United States, hiding behind the pretence of confidentiality, has not provided this Panel with any information that was before Commerce about the two US surrogate mills. These US mills were at the heart of Commerce's decision to initiate. Canada has not seen, and the Panel still does not have before it, basic information in the hands of the United States, such as the names of the US mills and what Commerce knew about those mills. The United States has responded to Canada's claims with nothing but assertions."

14. As a preliminary matter, the United States finds it hypocritical for Canada to be accusing the United States of "hiding behind the pretence of confidentiality." Canada understands well the sensitivity of business confidential information and the importance of safeguarding it adequately and not disclosing it without the consent of the submitter.⁹ It comes as a surprise, therefore, that Canada would dismiss as "hiding behind the pretence of confidentiality," Commerce's legitimate protection of the confidentiality of certain information as required by US statutory law.

15. In any event, Canada ignores both the arguments and the supporting record evidence cited by the United States in its Second Written Submission at paragraph 25 and the footnotes thereto, which demonstrate that the mills in question were within the range of the mills which "make up the bulk of the [US and Canadian softwood lumber] industry."¹⁰

practice (which is clearly reflected, for example, in the pricing patterns found in the *Random Lengths* materials in the application). See Canada Second Oral Statement, paras. 16-20.

⁸ See Checklist (Exhibit CDA-10) at 7; see also Initiation Notice (Exhibit CDA-9), at 66 Fed. Reg. 21330 (margin was based on a comparison of export price to constructed value).

⁹ See Contribution of Canada to the Improvement of the WTO Dispute Settlement Understanding, TN/DS/W/41 at p. 2 (24 Jan. 2003).

¹⁰ US Second Written Submission, para. 25, note 38.

D. ARTICLE 2.6:

To the US:

91. The Panel notes in para. 36 of the US Second Oral Statement that "Canada misunderstands the analysis that was actually applied." Could the US expand on what it perceives the misunderstanding of Canada is?

16. The most important point related to Canada's claim under Article 2.6 is that this provision contains no obligation concerning an investigating authority's definition of the product under consideration.¹¹ In various submissions and statements in this dispute, the United States has endeavoured to explain Commerce's administrative practice in defining the product under consideration. It has done so not to defend Commerce's practice in light of Article 2.6 – which contains no obligation on this issue – but instead to demonstrate that Canada's argument fails even on its own terms.

17. The misunderstanding referred to in the US Second Oral Statement is Canada's characterization of the analysis applied in the lumber investigation as different from Commerce's *Diversified Products* analysis. Canada has focused on two sentences taken out of context and leveraged these sentences into an assertion that there are two distinct, alternative tests that Commerce may apply in identifying the scope of the product under consideration. The first such test, Canada asserts, is the familiar *Diversified Products* analysis, with which Canada has no complaint. The second test, according to Canada, is a "no clear dividing line"/"continuum" test. Canada alleges that in the lumber investigation, Commerce applied the latter test in lieu of the *Diversified Products* test.

18. Canada's contention that there are two alternative tests and that Commerce applied something other than its familiar *Diversified Products* analysis in this case is incorrect. Simply put, Commerce applied its *Diversified Products* analysis. In applying that analysis, a question that Commerce considered was whether there were clear dividing lines that distinguished some elements of the putative "product under consideration" from other elements. Canada incorrectly suggests that Commerce thereby "subordinated" the *Diversified Products* analysis to a "no clear dividing line" analysis.¹² In fact, it did nothing of the sort.

19. Similarly, Canada improperly asserts that a passing observation by Commerce about the diversity of softwood lumber products must mean that Commerce abandoned the *Diversified Products* analysis in this investigation.¹³ Yet, in context, it is clear that, notwithstanding this "general observation," Commerce did apply its *Diversified Products* analysis.¹⁴ It did so for each softwood lumber product alleged to be outside the scope of a properly defined product under consideration (*i.e.*, Western red cedar, Eastern white pine, softwood lumber boards used as bed frame components, and softwood lumber boards used as finger-jointed flangestock).¹⁵

¹¹ See US First Written Submission, paras. 85-99; US Opening Statement at First Panel Meeting, paras. 24-28; US Second Written Submission, paras. 33-41.

¹² Canada Second Written Submission, paras. 70, 87.

¹³ *Id.*, paras. 71, 87.

¹⁴ *Final Determination*, Comment 52, at 154 (Exhibit CDA-2).

¹⁵ See, *e.g.*, application of *Diversified Products* analysis to Western red cedar (*Scope Memorandum*, at 24-28 (Exhibit CDA-12); *Final Determination*, Comment 52A (Exhibit CDA-2); application of *Diversified Products* analysis to Eastern white pine (*Scope Memorandum*, at 29-31 (Exhibit CDA-12); *Final Determination*, Comment 52C (Exhibit CDA-2); application of *Diversified Products* analysis to bed-frame components (*Scope Memorandum*, at 32 (Exhibit CDA-12); *Final Determination*, Comment 52E (Exhibit CDA-2); application of *Diversified Products* analysis to finger-jointed flangestock (*Scope Memorandum*, at 31-32 (Exhibit CDA-12); *Final Determination*, Comment 52F (Exhibit CDA-2);

20. Canada's erroneous contention that in this investigation Commerce abandoned its usual practice and applied an unfamiliar analysis appears to be an attempt to compensate for Canada's inability to identify an applicable obligation under Article 2.6. As Article 2.6 is silent on the question of how an investigating authority identifies the product under consideration, Canada has resorted to the suggestion that, whether or not there is an express obligation in this area, Commerce acted unreasonably by deviating from its normal practice. However, the isolated statements on which Canada relies do not support that contention. In identifying the product under consideration in this investigation, Commerce applied its normal *Diversified Products* analysis.

E. PHYSICAL CHARACTERISTICS:

To the US:

94. We refer to the following statement in para. 50 of the US Second Oral Statement:

"for all physical characteristics, except dimension, Commerce had cost data to connect the physical differences to the impact on price, pursuant to its normal methodology."

Could the US confirm that it normally bases adjustments on differences in variable costs and that in this instance DOC could determine adjustments on such a basis for all differences except for dimension?

21. The United States confirms that Commerce normally bases a price adjustment for differences in physical characteristics in the product under consideration on reported differences in the variable cost of manufacturing. This can be seen in Commerce's questionnaire, relevant portions of which were provided in Exhibit US-36, requesting this information from respondents and explaining the basis for the adjustment in the questionnaire's glossary of terms (also provided in Exhibit US-36). The questionnaire's glossary refers respondents to Commerce's regulations regarding this specific price adjustment (Exhibit US-44). Commerce also has a decade-old policy bulletin explaining the basis for the adjustment, available on its website at <http://ia.ita.doc.gov/policy/>, and provided in Exhibit US-77.

22. With respect to the eleven physical characteristics distinguished for purposes of the model match methodology, Commerce never compared different softwood lumber product categories, species or grade groups.¹⁶ Thus, there were never any comparisons for which a price adjustment would be warranted with respect to these three physical characteristics. The respondents reported variable cost of manufacturing data for moisture content, surface finish, end trim and further processing in their questionnaire responses, and Commerce was able to determine adjustments pursuant to its normal methodology for these four characteristics.¹⁷ In Commerce's *Preliminary Determination*, Commerce relied on the respondents' normal books and records, which reported no difference in variable cost between products of differing grades and dimension. Therefore, Commerce was not able to make an adjustment for grade and dimension pursuant to its normal methodology.¹⁸

23. In response to specific comments on the *Preliminary Determination* from the Canadian respondents (addressed in more detail below), Commerce further evaluated price and cost data with

¹⁶ See US First Written Submission, paras. 124-125.

¹⁷ *Id.*, para. 126; Dept. of Commerce, *Notice of Preliminary Determination of Sales at Less Than Fair Value and Postponement of Final Determination: Certain Softwood Lumber Products From Canada*, 66 Fed. Reg. 56062, 56066 (6 Nov. 2001) ("*Preliminary Determination*") (Exhibit CDA-11).

¹⁸ *Preliminary Determination*, 66 Fed. Reg. at 56066 (Exhibit CDA-11).

respect to grade and dimension and determined to allocate certain costs of manufacturing to grade, but not to dimension, using value-based data.¹⁹ Consequently, for the *Final Determination*, Commerce calculated grade-specific variable costs, making a cost-based price adjustment possible when comparing products of different grade. Therefore, dimension remained the only physical characteristic for which an adjustment could not be made pursuant to Commerce's normal methodology.²⁰

95. Could the US explain in detail how the issue of dimension was addressed in the lead-up to the Preliminary Determination and from the Preliminary Determination to the Final Determination, including after the DOC found that there were no differences in variable costs? Was DOC's statement in the Preliminary Determination that dimension has an effect on price comparability made before DOC knew that there was no difference in variable costs? Indicate what made DOC change its position with respect to the effect of dimension on price comparability between the Preliminary Determination and the Final Determination.

24. Commerce did not state that “**dimension** has an effect on price comparability” in its *Preliminary Determination*. The Panel's misapprehension presumably derives from Canada's distortion of a statement in Commerce's *Preliminary Determination* concerning “several” physical characteristics “which affect price.” Canada quoted that statement out of context.

25. As indicated in the United States' First Written Submission, paras. 124-125, and in response to Question 95, above, the dimensional characteristics of width, thickness and length comprised three of eleven physical characteristics that Commerce accepted for purposes of distinguishing between models of softwood lumber in this investigation. Commerce's questionnaire identified the specific product characteristics that Commerce determined, based on the interested parties' comments, should be distinguished in its model match methodology. (Grade was later separated into grade and grade group.)

26. As indicated above, the respondents' questionnaire responses reported the same variable cost of manufacturing for all dimensions. However, Commerce, did not match nonidentical dimensions (or grades) in the *Preliminary Determination*. This was consistent with its practice in many agricultural cases, where Commerce did not match across certain characteristics if there were no cost differences associated with differences in physical characteristics.²¹ This obviated any need for the requested price adjustment. Commerce's explanation concerning its preliminary treatment of the physical characteristics, particularly dimension and grade, is set forth below. Although Commerce acknowledges an impact of physical differences on price, it does so in the context of distinguishing the complex and diverse factors determining price in this case versus another much simpler case, in which Commerce determined that a value-based price adjustment for a single physical difference was warranted:

[F]or this preliminary determination, we have concluded that it is not appropriate to match products that do not have the following identical physical characteristics: grade, thickness, width and length. These are significant physical characteristics that cannot be accounted for by means of a cost-based difference-in-merchandise adjustment. The respondents in this investigation have reported that their methods of tracking costs and the nature of producing lumber do not allow them to distinguish costs by grade or size. Specifically, the respondents have reported that they cannot report costs that distinguish between factors other than moisture, surface finish, end

¹⁹ *Final Determination*, Comment 4 (Exhibit CDA-2).

²⁰ *Id.*, Comment 8 (Exhibit CDA-2).

²¹ *Preliminary Determination*, 66 Fed. Reg. at 56066 (Exhibit CDA-11) (discussing cases involving tomatoes and salmon, respectively).

trim and further manufacturing. Our analysis confirms that most lumber produced within a given species has the same production cost.

The respondents have cited to *UHFC Company v. United States*, 916 F.2d 689 (Fed. Cir. 1990), where the Court of Appeals for the Federal Circuit (CAFC), in that specific case, instructed the Department on remand to match across different strengths/grades, despite the fact that differences in costs could not be calculated. In that case, the product involved was animal glue, where different strength/grades were produced at the same time, using the same production process. The respondents claim that in accordance with the Court's decision in that case, "the Department must calculate a value-based difference-in-merchandise in this case in those instances where similar products are compared and there is no variable cost data available to permit the calculation of a cost-based difmer." Among the suggested bases for a value-based difmer adjustment were data published in Random Lengths, respondents' own reported sales data covering the POI, or historical pricing data.

We disagree that the UHFC decision requires the calculation of a value-based difmer adjustment in this case. First, this investigation is distinguishable from the circumstances in the UHFC case, where there was only a single difference, i.e. glue strength, between the products. ***In the instant investigation, there are several significant differences in physical characteristics which affect price.*** As a result, we have determined that we have no comparable basis on which to adjust for physical differences between similar products based upon market value, as has been suggested by the respondents. By Abitibi's own admission, Random Lengths data are not comprehensive enough to identify all of the differences among the entire range of products.²²

27. As is clear from the above discussion, Commerce *did not make any determination* with respect to the impact, if any, that dimension alone had on price, nor did it focus on *measuring* any appropriate adjustment. Commerce then noted that its decision to match similar products only where it was able to calculate a cost-based price adjustment, and to limit its matches for grade and dimension to identical comparisons, was consistent with agricultural cases.²³ (Moreover, as is apparent from the full discussion of the issue in the *Preliminary Determination*, Commerce did consider making an adjustment pursuant to its normal methodology and did consider the arguments raised by the parties as to other means.)

28. The Canadian respondent companies, in response to Commerce's *Preliminary Determination*, requested that Commerce allocate certain costs, using value data, to grade and dimension, so that a cost-based adjustment for differences in dimension and grade could be made. Alternatively, they requested, once again, that Commerce grant a value-based adjustment for differences in dimension (and grade), rather than limit its comparisons to identical dimension and grade products.²⁴ Indeed, two of the six respondent companies indicated that the result Commerce reached in the *Final Determination* (what they termed a "zero" adjustment) would be an acceptable result.²⁵

29. The Canadian respondent companies requested that Commerce reevaluate its decision to match only identical dimensions and grades based on the available data on the record. Commerce examined the data in the questionnaire responses to determine whether or not it would be appropriate

²² *Preliminary Determination*, 66 Fed. Reg. at 56066 (Exhibit CDA-11) (emphasis added).

²³ *Id.*, (discussing cases involving tomatoes and salmon, respectively).

²⁴ See, e.g., Case Brief of Abitibi, 12 Feb. 2002, 26-29 (Exhibit CDA-142, pp. 93-96); Case Brief of West Fraser, 12 Feb. 2002, 17-19 (Exhibit CDA-142, pp. 140-142).

²⁵ See, e.g., Case Brief of Slocan, 12 Feb. 2002, 24-32 (Exhibit US-74); Case Brief of West Fraser, 12 Feb. 2002, 26-29 (Exhibit US-75).

to allocate certain costs to grade and dimension using value data. As Commerce explained in its *Final Determination*, based on the fact that grade is a quality inherent in the wood, Commerce determined that certain costs could be allocated to grade using value data.²⁶ Unlike grade, Commerce specifically concluded that the facts did not warrant allocating costs to dimension²⁷, a conclusion that Canada has not challenged as inconsistent with the AD Agreement.

30. Using the respondents' home market sales data, which was also used to evaluate whether or not it was appropriate to allocate costs to dimension based on value data, Commerce then examined (a) whether or not it should compare similar dimensions (rather than just identical dimensions) and (b) whether or not, if it compared similar dimensions, it should make a price adjustment for differences in the nonidentical dimensions compared. As indicated above, this analysis was conducted at the behest of the Canadian respondents in light of the results of Commerce's *Preliminary Determination*. Commerce concluded, based on its examination of the data on the record, that it should not be limited to only identical dimensional matches, but that a price adjustment for nonidentical comparisons was not warranted.²⁸ For a more detailed explanation of Commerce's methodology, please see response to Question 99 below.

96. At what stage were the respondents informed of DOC's finding that differences in dimension do not affect price comparability? What opportunities were provided to respondents to comment on that finding?

31. As indicated above, Commerce found no cost differences attributable to dimensional differences and no basis for making price-based adjustments for different dimensions. Given these preliminary findings, it was clear that if Commerce matched different dimensions, as requested by the respondents, the obvious questions were: would an adjustment be warranted and, if so, what should it be? Consequently, it was in the *Final Determination* that Commerce concluded, and the respondents were thereby informed, that differences in prices were not attributable to differences in dimension and that a price adjustment for differences in the dimensions of the products compared was not warranted. Although this was Commerce's *final* conclusion, the parties were given ample opportunity to comment on the issue of price adjustments generally throughout the proceeding, as indicated already in Commerce's *Preliminary Determination*.

32. In its explanation in the *Final Determination*, Commerce responded to the specific requests and comments of both the Canadian and domestic interested parties on this issue.²⁹ The respondents' requests in their case briefs that Commerce match similar dimensions, and grant either a cost- or value-based price adjustment, required Commerce to evaluate the pricing data on the record both for purposes of Commerce's cost methodology and for purposes of a price adjustment. Clearly, it would have been impossible for Commerce to consider the respondents' suggestions without carefully reviewing the effect of dimension on price, as any calculation of a value-based cost or price-based adjustment for dimension would have been necessarily dependent on the relative prices between dimensions.

33. It would be a misreading of the AD Agreement to find that at every decision point in an investigation, an investigating authority must announce each intermediate decision and provide further opportunity for comment. Under such an interpretation, investigating authorities would be effectively prevented from completing investigations within any realistic time period and manageable comment schedule. This interpretation would place a significant obstacle in the way of the rule that investigations be concluded within one year and in no case more than 18 months.³⁰

²⁶ *Final Determination*, Comment 4 (Exhibit CDA-2).

²⁷ *Id.*, Comment 4, note 60 (Exhibit CDA-2).

²⁸ *Id.*, Comments 7 and 8, respectively (Exhibit CDA-2).

²⁹ *Id.*, Comment 8 (Exhibit CDA-2).

³⁰ AD Agreement, art. 5.10.

97. Please comment on Canada's response to Question 22, with reference to the respondents' demonstrating a need for a price adjustment:

"at the beginning, of the period, in April 2000, Abitibi's average net price for No. 2 grade 2x4x8 was around [[]] whereas the No. 2 2x6x16 price was [[]]. The comparable figures for economy grade were [[]] for the smaller size and [[]] for the larger."

34. The above example does not demonstrate a need for a price adjustment. This specific example, provided to Commerce in Abitibi's case brief during the investigation, is flawed because it relies on average prices for only one month. The example says very little about the effect of different dimensions on prices, as it only represents a limited amount of price data (average prices in a single month) and it is not clear what other factors might account for the price differences. Anecdotal price differences such as these may be part of a discernible pattern indicating price differences attributable to dimensional differences, or they may merely reflect coincidental pricing differences unrelated to differences in dimensions.

35. Attached to this submission, at Exhibit US-81, is a chart plotting the actual net sales prices of Abitibi's 2x4x8 No. 2 grade and economy grade softwood lumber and 2x6x16 No. 2 grade and economy grade softwood lumber over the course of the period of investigation. These are the same products as in the example from Abitibi's case brief.

36. What the exhibit strikingly demonstrates is that a price adjustment for dimension is *not* warranted, because no pattern of consistent price differences based on dimension is discernible. The prices, within each grade, for the two different dimensions converge, diverge and overlap during the period of investigation. In stark contrast, prices of the No. 2 grade and the economy grade remain consistently distinct. This example of the distinction between the relative behaviour of grade and dimension supports Commerce's differing treatment of grade and dimension (using value data to allocate certain costs to grade) in the cost methodology for the *Final Determination*.

98. The Panel notes the following statement contained in Canada's response to Question 22:

"Tembec suggested several alternative data sets and methodologies for computing such an adjustment (DIFMER)."

**Was the proposed methodology evaluated? What was the result of this evaluation?
Please indicate where such a result can be found on the record.**

37. The quoted sentence is another example of Canada's mischaracterization of the record. In fact, Tembec's "suggestions" amounted to no more than brief requests to use pricing data on the record, requests that had already been made to and rejected by Commerce in the *Preliminary Determination*. The full quote from Tembec's case brief reads as follows:

The record is sufficient to calculate a value-based Difmer. The Department could use the relative values of the respective CONNUMs as reported in the respondents sales databases, the Publicly Available Published Information from sources such as Random Lengths, or historical value data as submitted by several respondents. Were

the Department to think that other data were required, the Department should have requested such data.³¹

38. Commerce addressed these suggestions in the *Final Determination*.³² With respect to the use of the respondents' own sales pricing data as a basis for calculating a price adjustment, Commerce again noted the large number of sales made outside the ordinary course of trade, as it had in the *Preliminary Determination*: To use respondents' prices "would adjust normal values back to prices already determined to be outside the ordinary course of trade, the whole reason why we would be disregarding such prices and comparing to a similar product."³³ With respect to the use of *Random Lengths* data, Commerce reiterated that the data were not complete.³⁴ In the *Preliminary Determination*, Commerce stated its reservations concerning the use of historical price data, indicating that it had no basis on which to determine whether or not those sales had been made in the ordinary course of trade.³⁵ Commerce concluded that a price adjustment was not warranted based on its evaluation of all the data on the record.³⁶

99. With respect to the consistency in price patterns, the Panel has the following questions:

- (a) **Could DOC explain in detail the methodology it used to carry out its consistency test? Illustrate your explanation with an example from the test that was carried out in this case, including any sampling, selection of dates, etc. Did the US consider using other methodologies?**

39. In deciding how to address dimensional differences in this case, Commerce had four options: (1) calculate a value-based cost across dimension, which would allow the calculation of a cost-based price adjustment for dimensional differences pursuant to Commerce's normal methodology; (2) calculate a value (price)-based adjustment for dimensional differences; (3) calculate no price adjustment; or (4) continue to use the same methodology as in the *Preliminary Determination*, and not match products across dimension.

40. In order to consider the first three options, all of which were suggested by various respondents, it was necessary to examine the relative prices of the various dimensions. As indicated above, Commerce examined relative prices initially in the context of determining whether or not to calculate a value-based cost. Because Commerce was deciding which cost methodology to use, Commerce examined all prices for selected dimensions in its relative price test, even those which would eventually be found to be below cost. Commerce concluded that the random nature of the movement in relative prices between the various dimensions precluded dimension-specific prices from providing a sound basis for a value-based cost allocation.³⁷

41. Using the same relative price tests, Commerce next considered the issue of whether, if it compared products across dimension, it was more appropriate to calculate a price-based adjustment for differences in dimension, or to make the comparisons with no such adjustment. Commerce examined random sales of commonly sold softwood lumber products, comparing products with

³¹ 12 Feb. 2002, Tembec Case Brief, 37-38 (Exhibit CDA-142, pp. 163-164). The United States notes Tembec's first sentence from the quote above: "The record is sufficient to calculate a value-based Difmer." Apparently, Tembec and Canada now disagree, since Canada has attempted to submit a regression analysis of Tembec's data (Exhibit CDA-77 and Exhibit CDA-129) for the first time in this dispute. The United States continues to object to the submission of that data as a violation of Article 17.5(ii) of the AD Agreement.

³² *Final Determination*, Comment 8 (Exhibit CDA-2).

³³ *Id.*

³⁴ *Id.*

³⁵ *Preliminary Determination*, 66 Fed. Reg. at 56066 (Exhibit CDA-11).

³⁶ *Final Determination*, Comment 8 (Exhibit CDA-2).

³⁷ *See id.*, Comment 4, fn. 60.

relatively small dimensional differences. Commerce chose products with small dimensional differences, because its computer programme was designed to match US sales to the above-cost home-market sales with the smallest possible dimensional differences.

42. Examples of the tests Commerce carried out can be found in Exhibit US-76 (replacement), involving two West Fraser products, and in Exhibits US-42 and US-43, involving two Slocan products. Commerce compared the actual home market sales prices for each of the Canadian respondent companies, plotting sales over the entire period of investigation. The sales included both above- and below-cost sales, as the point of the tests was to determine whether a pattern of consistent price differences which could be linked to dimension existed.

(b) Could the US explain in detail how the results of its test were evaluated? Please explain the evaluation leading up to that conclusion.

43. As a result of the above analysis, it was apparent that no reasonable adjustment could be measured or quantified. The prices of the sampled products fluctuated relative to each other over the period of investigation, such that no adjustment could reliably account for the difference in price at any given time. The sample comparisons demonstrated that the price *differences* between the comparable products varied to a significant degree. For example, the price differences between two products were both negative and positive in varying amounts over the course of the period of investigation. The sample West Fraser comparison provided in Exhibit US-76 (replacement) illustrates such fluctuations. In looking at these comparisons, Commerce found that not only would it be unable to quantify any price adjustment, but that given the relative fluctuations, an adjustment was not warranted. For example, if the price differences between two products were negative at some points during the period and positive at others, there was no meaningful way to determine whether an adjustment between those two products should be positive or negative, and therefore, there was no rational basis to conclude that an adjustment was appropriate. Ultimately Commerce concluded, after looking at all of the sample comparisons and seeing the degree of relative price fluctuations between the products most likely to be compared, that price differences could not be attributed solely to differences in dimension, particularly where those differences were minor.

44. Had respondents had other means to demonstrate a more consistent pattern of price differences, Commerce would have considered such data. The respondents had raised the issue themselves and had opportunities to present data in support of their claims.

100. The Panel notes that in Exhibit CDA-2, p. 51 it is stated that:

"as we stated in the Preliminary Determination, we do not believe it would be appropriate to use the respondents' prices as a basis for calculating a difmer adjustment where there were home market sales outside the ordinary course of trade during the POI for certain products involved here. To do so would adjust normal values back to prices already determined to be outside the ordinary course of trade, the whole reason why we would be disregarding such prices and comparing to a similar product."

In response to an oral question by the Panel on 11th August, the US indicated that all the price data – including those prices which had previously found not to be cost-covering – were used for the consistency test. How does this statement reconcile with the above-quoted excerpt from the IDM?

45. The above quote refers specifically to the problem inherent in calculating a price-based adjustment in the face of a large number of sales made outside the ordinary course of trade. Under the

limited-reporting criteria agreed to by all the parties, each sale in the US database had an identical match in the home market database. The only time, therefore, that a US sale matched to a home market sale of a similar, rather than identical product, was when 100 per cent of the sales of the identical product were determined to be outside the ordinary course of trade. Therefore, Commerce was concerned that including sales outside the ordinary course of trade in the calculation of a price-based adjustment would result in establishing normal values that reflected prices of sales outside the ordinary course of trade.

46. This observation did not, however, affect the relative price test that Commerce carried out. (See Response to Question 99 above.) In looking at the movement in relative prices between dimensions, Commerce concluded that “there appears to be little, if any, difference in home market prices that is attributable to differences in dimensions of the products compared, especially where those dimensional differences were minor.”³⁸

101. Please comment on Canada's Second Oral Statement, para. 56 which states that:

“[t]he US International Trade Commission, in the injury inquiry, determined that “lumber prices generally differ substantially depending on grades and dimensions”.”

47. The full statement of the US International Trade Commission (ITC)³⁹, in context, shows the ITC’s recognition of general conditions of competition in the market, with regard to variations in prices among types of softwood lumber. The ITC did not conduct any specific analysis with respect to the impact of dimension on price, nor did it quantify such relationship. The ITC’s statement appears to be an observation about the market and not a finding of fact fundamental to its own determination of whether the US industry was materially injured or threatened with material injury by reason of dumped imports.

102. In paras. 58-60 of Canada's Second Oral Statement, Canada alleged that the average dumping margin for the non-identical comparisons was 2 to 7 times higher than the average margins of dumping for identical comparisons as DOC made numerous comparisons of smaller, low-value lumber sold in the US to larger dimension, high-value lumber sold in Canada, without any adjustment for dimension. Could the US comment on this allegation that this establishes a prima facie breach of the requirement of Article 2.4?

48. Canada erroneously suggests that dimensional differences explain the differences in margins in the comparisons at issue. Canada admits, however, that the non-identical comparisons with high margins included “numerous comparisons of smaller low-value lumber.”⁴⁰ However, as is clear from Exhibit US-76 (replacement) (first four pages), many of these low-value products sold in the United States could only generate high margins if they were sold for prices in the United States that were well below their cost of production.⁴¹ The lowest price for a product that Commerce could ever use in making a fair comparison is one that is at least equal to the cost of production, since Commerce

³⁸ *Final Determination*, Comment 8 (Exhibit CDA-2).

³⁹ The ITC observed, in considering conditions of competition pertinent to the softwood lumber industry, that: “Softwood lumber prices generally differ substantially depending on grades and dimensions, and may differ by species and applications involved, with better grades and wider dimensions usually carrying higher prices than lower grades and narrower dimensions.” US International Trade Commission, Pub. No. 3426, *Softwood Lumber from Canada*, Inv. Nos. 701-TA-414 and 731-TA-928 (Preliminary) (May 2001) at 16 (Exhibit CDA-31).

⁴⁰ Canada Second Oral Statement, para. 59.

⁴¹ The United States notes that Canada is not challenging Commerce’s cost methodology here.

discarded all below-cost sales prior to making price comparisons. The comparison that Commerce actually made was to the most similar product which had any sales which passed the cost test. As Exhibit US-76 shows, the prices of the most similar products were often only marginally above the cost of production. Therefore, it appears that the low-value products which generated high margins were, in fact, the most dumped products. It is for that reason, rather than the dimension of the compared product, that these low-value, low-priced US sales generated high margins.

49. In addition, Canada distorts the effect of these sales on the final margin by emphasizing the number of comparisons, rather than the quantity of lumber involved in the comparisons. Taking quantity of lumber into account, even the fact that the products at issue were heavily dumped (that is, that the margins on those particular sales were high) still had a limited effect on the final margin.

50. Canada has not established a *prima facie* breach of Article 2.4 (paragraph 60 of its Second Oral Statement), simply by claiming that the margins of the nonidentical comparisons were 2 to 7 times higher than the margins of the identical comparisons. Canada's argument rests principally on its claim that all parties acknowledged that dimension affects price. However, the evidence from the record Canada has cited⁴² did not prove that any amount of differences in prices were specifically attributable to differences in dimension. Commerce found that relative prices of otherwise identical products of different dimensions appeared to fluctuate randomly, making it impossible to attribute any differences in price to the dimension of lumber. Therefore, because dimension was not demonstrated to affect price comparability, Commerce was not required to make any allowance for differences in dimension under Article 2.4.

To both parties:

103. Could the parties confirm whether the percentages mentioned in para. 40 and footnote 33 of the US reply to Question 25 of the Panel relate to differences in dimension only?

51. The percentages referred to in paragraph 40 and footnote 33 of the United States First Answers to the Panel's questions relate to all differences in physical characteristics, not just dimension. However, the United States notes that the majority of the "similar" (*i.e.*, non-identical) comparisons will include different dimensions as a result of the model match methodology. Therefore, the United States does not believe that similar matches as a percentage of total comparisons (either weighted by quantity or stated as a raw number) would be significantly different if limited to dimension only.

F. ZEROING:

To the US:

109. Could the US explain how it normally calculates the dumping margin at the two stages and how it afterwards establishes the duty liability, and how this compares to the duties collected definitively.

52. In an antidumping investigation, the United States normally calculates a company's overall dumping margin using price-to-price comparisons through the following two stage process.

⁴² See, *e.g.*, Exhibit CDA-76; Canada's First Responses To Panel Questions, para. 87; Exhibit CDA-142.

Stage 1

- (a) Relevant physical and other (*e.g.*, level of trade) characteristics are identified for sales matching purposes.
- (b) For each combination of relevant physical and other characteristics of products sold in the United States during the period of investigation, the identical or most comparable combination of physical and other characteristics of products sold in the home market is identified.
- (c) Where the combination of characteristics is not identical between the two markets and the differences have been demonstrated to affect price comparability, price adjustments are made.
- (d) For all sales of each combination of relevant physical and other characteristics of products sold in the United States during the period of investigation, and for each most comparable combination of characteristics of products sold in the home market, the weighted-average price per unit (including any adjustments identified in (c) above) is calculated.
- (e) For each set of comparable characteristics, the weighted-average normal value per unit is compared to the weighted-average export price (or constructed export price) per unit. When the weighted-average normal value exceeds the weighted-average export price, the difference is the per unit dumping margin for that comparison. When the weighted-average normal value is equal to or less than the weighted-average export price, there is no dumping margin for that comparison.

Stage 2

- (f) Each per unit dumping margin found in step (e) is multiplied by the volume of the export transactions used in the comparison that resulted in that dumping margin.
- (g) The results of step (f) are summed to create the numerator for the overall dumping margin calculation.
- (h) The result of step (g) is divided by the aggregate value of all export transactions utilized in step (e).

53. The result of step (h) is the overall dumping margin for a given respondent. This overall dumping margin is the provisional measures rate in a preliminary determination and the cash deposit rate (estimated dumping duty) in a final determination.

54. In the absence of an administrative review, the estimated dumping duty is definitively collected. However, if a review is requested, Commerce performs a similar calculation to that identified above in order to calculate an appropriate assessment rate for the importer and a new cash deposit rate for the producer.

55. The differences between a review and an investigation are generally found in stage 1. In a review, rather than compare period-wide weighted averages, Commerce normally compares individual export transactions to a monthly weighted average of the most comparable home market sale. The results of these comparisons are combined in the same manner as described in the stage 2 discussion above to establish a new cash deposit rate.

56. A separate stage 2 calculation is performed to establish importer-specific rates for purposes of assessing definitive duties. For these purposes, the results of the comparisons between export transactions and monthly weighted average normal values are segregated based on the importer involved in the export transaction. The stage 2 calculation is then performed on an importer-specific basis, using the importer's entered value as the denominator.

G. ABITIBI:

To the US:

113. Please comment on Exhibit CDA-176.

57. Exhibit CDA-176 provides in chart form many of Canada's unsubstantiated claims related to Commerce's COGS-based methodology for the allocation of financial costs. Specifically, Canada highlights different kinds of assets that it believes are ignored through the COGS-based methodology. The vast majority of Abitibi's assets are considered through the COGS methodology.⁴³

58. The argument for which Canada relies on in Exhibit CDA-176 is based on at least two false premises. The first false premise is that the costs of producing goods are fully reflected in accounts receivable. Financial costs relate to all the costs a company incurs in relation to the production of goods. As fully discussed in answer to question 115 below, Canada's argument falsely presumes that the only COGS that should be considered in the allocation of financial costs are those COGS captured in inventory. However, there is no evidence that Abitibi only incurs financial costs on inventory. Financial costs relate to all the costs a company incurs, including the costs incurred on producing sold goods as well as the costs incurred on producing goods in inventory. Commerce's COGS-based methodology considers both of these costs, while Canada's methodology considers only the latter. Canada's argument is also based on the false premise that Abitibi finances the full value of its assets in each year of production.⁴⁴ This extraordinary claim is contrary to normal business practices and entirely unsubstantiated. Depreciation expenses included in the COGS-based methodology which represent the cost incurred in using an asset in a given year are a reasonable, and, in fact, a more appropriate basis upon which to consider assets in the allocation of financial costs.

114. Please comment on Canada's Second Oral Statement, para. 72 which states that:

“Commerce: asserted in the Final Determination that it used COGS, not because it was the proper methodology for Abitibi's facts, but because it was Commerce's “established practice” and was “consistent and predictable”.”

59. Canada's statement misconstrues Commerce's determination. In fact what Commerce stated was:

“Finally, we disagree with Abitibi that the Department should depart from its established practice of calculating financial expense ratios based on the financial expenses and cost of goods sold. . . (i.e. because of the fungibility of money). Because there is no bright-line definition in the Act of what a financial expense is or how the financial expense rate should be calculated, the Department has developed a

⁴³ At least C\$8 billion dollars of Abitibi's C\$11 billion total assets were capital assets for which depreciation expenses were realized. *See* Abitibi Consolidated Financial Statement, p. 35 (Exhibit CDA-82).

⁴⁴ *See* Canada's Second Oral Statement, para. 77.

consistent and predictable practice for calculating and allocating financial expenses."⁴⁵

While predictability and consistency are important goals to which any investigating authority aspires, these were by no means the only bases for Commerce's determination. Commerce considered Abitibi's argument relating to an asset-based allocation for financial costs and rejected it. Specifically, after finding that Abitibi's argument was improperly premised on the debt of the company relating to only non-lumber producing divisions Commerce stated:

"[T]he Department's method addresses Abitibi's concern that those activities [*i.e.*, non-lumber production] are more capital intensive. Specifically, those activities would have a higher depreciation expense on their equipment and assets. Thus, when the consolidated financial expense rate is applied to the cost of manufacturing lumber products, less interest will be applied because the total cost of manufacturing for lumber products includes a lower depreciation expense".⁴⁶

Thus, rather than ignoring Abitibi's arguments, Commerce expressly considered them and rejected them.

To both parties:

115. The Panel understands Canada to argue in para. 80 of its Second Oral Statement that an asset-based methodology can capture the flow elements through inventory. Please comment.

60. Canada's assertion in paragraph 80 of its Second Oral Statement is simply wrong. Abitibi's suggested asset-based allocation methodology does not "capture the flow elements through inventory." A company's inventory balance represents the inventory on-hand at any given point in time (generally, at the end of the year). The value of products that passed through the inventory account on the way to being sold during the year are not included in the ending inventory account – which necessarily means the inventory account does not capture the flow elements. That is, the inventory account does not capture the (usually much greater) value of products that have previously passed through inventory accounts during the year.

61. Canada's assertion also incorrectly assumes that only those costs incurred on products in inventory require financing, because sold products have produced revenues that are in turn used to pay for the cost of producing those sold goods.⁴⁷ However, similar to proceeds from a loan, proceeds from sales are entirely fungible and may be used to pay for any of the costs a company incurs (*e.g.* the purchase of fixed assets). Thus, financial costs relate to all the costs a company incurs, including the costs incurred on producing sold goods as well as the costs incurred on goods in inventory. Commerce's COGS-based methodology considers both of these costs, while Canada's methodology considers only the latter.

62. The balance sheet is not the correct place to look for cash flows. The correct place is the cash flows statement from Abitibi's financial statement.⁴⁸ This cash flow statement illustrates the numerous sources of cash, most significantly the net cash from operating activities, as well as the numerous uses of cash. This cash flow statement fully supports the concept of fungibility of money and that

⁴⁵ *Final Determination*, Comment 15 (Exhibit CDA-2).

⁴⁶ *Final Determination*, Comment 15 (Exhibit CDA-2).

⁴⁷ See Second Written Submission of Canada, para. 205 (arguing that cost of producing goods need only be financed until payment is received).

⁴⁸ See Abitibi's Financial Statement p. 34, "Consolidated Statement of Cash Flows" (Exhibit CDA-82).

financing costs cannot be traced to one particular activity of the company, such as the acquisition of assets.

116. Please indicate the advantages/disadvantages in this context, of the two approaches (COGS; asset-based) for allocating interest expenses.

63. Allocation of financial costs based on cost of goods sold results in a reasonable allocation of financial costs to softwood lumber, consistent with Article 2 of the AD Agreement. COGS is a broad category that includes the costs associated with the production of goods in a given year, including assets through the inclusion of depreciation expenses. Because COGS is specific to a given year, it is a reasonable basis upon which to allocate financial costs specific to the same period. Total asset values, on the other hand, relate to assets that exist over multiple years and are, thus, a less appropriate basis upon which to allocate current financial costs. In addition, an allocation of a financial costs based on asset-values falsely assumes that financial costs are a function of the value of assets at a particular point in time. There is no basis for such an assumption that could grossly distort the allocation of financial expenses. Finally, financial costs relate to all the costs a company incurs, including the costs incurred on producing sold goods as well as the costs incurred on goods in inventory. Commerce's COGS-based methodology considers both of these costs, while Canada's methodology considers only the latter.

64. For the reasons set forth here and in its prior submissions, the United States believes that the COGS methodology was the more reasonable of the two methods in this case. However, the question before the Panel is not whether one methodology was more reasonable than the other. Under the Article 17.6 standard of review, the only question is whether Commerce properly established the facts and evaluated the facts in an objective and unbiased manner. The United States has demonstrated that Commerce did so and, accordingly, its application of the COGS methodology conformed with the applicable WTO obligations.

H. TEMBEC (G&A):

To the US:

119. In its reply to question 56, the US refers to the "reliability of cost data". Based on the record, did DOC find in the context of the investigation that data submitted by Tembec for the Forest Products Group was not reliable? If so, please point to relevant documents submitted to the Panel – including cost verification reports – or provide them.

65. Commerce found that the use of Tembec's internal, division-specific books and records could have resulted in distortions.⁴⁹ Thus, reliability was a principal basis for Commerce's determination. Consistent with Article 2.2.1.1 of the AD Agreement, Commerce determined that cost data kept in accordance with GAAP were more reliable than cost data not kept in accordance with GAAP. No evidence was presented that Tembec's divisional data were kept in accordance with GAAP.⁵⁰ Moreover, the United States has provided evidence that Tembec's divisional data were not required to be kept in accordance with GAAP nor were they required to be an objective measures of costs.⁵¹

120. Please comment on paras. 84-88 of Canada's Second Oral Statement, specially on the last sentence of para. 85.

⁴⁹ *Final Determination*, Comment 33 (Exhibit CDA-2).

⁵⁰ See Tembec's Annual Report, "Auditor's Report," p. 34 (Exhibit US-12) (stating that only the company-wide statements were audited).

⁵¹ See Exhibit US-80, p. 2.

A. *No factual basis for assertion that Tembec's lumber producing division incurred less G&A:*

66. Canada has failed to provide any reasonable factual basis for its assertion that Tembec's lumber producing division incurred less G&A than its non-lumber producing divisions. For instance, in its Second Written Submission, Canada asserts that, "Tembec submitted documented evidence that its pulp and paper operations incurred significantly higher G&A expenses than its lumber operations."⁵² However, Canada's basis for this assertion makes no sense. Canada's claim rests only on the fact that its Forest Products Group requires a smaller amount of Tembec's total assets while accounting for relatively more of Tembec's total sales.⁵³ There is no logical nexus between the productivity of assets and G&A. Moreover, the fact that Tembec internally assigned costs to various divisions in a certain manner for its own purposes does not mean that such expenses were in fact incurred by those divisions in those amounts. Therefore, there is no basis upon which to find that Tembec's lumber producing division incurred less G&A than Tembec's non-lumber producing divisions.

B. *Commerce rejected Tembec's divisional data for multiple reasons:*

67. Contrary to Canada's assertion, Commerce did not reject Tembec's data simply because Commerce's standard practice was to rely on company-wide data for G&A calculations. In fact, as discussed in response to Question 119, Commerce rejected the data because they were less reliable and could have led to distortions. Moreover, basing G&A on company-wide data is consistent with the definition of general costs (*i.e.*, cost that relate to a company as a whole) while basing G&A on divisional data is not.

C. *Commerce used Tembec's divisional data in the dumping calculation for an extremely limited purpose:*

68. Article 2 of the AD Agreement requires an investigating authority to consider only books and records kept in accordance with GAAP. No evidence was presented that Tembec's divisional data were kept in accordance with GAAP.⁵⁴ Moreover, the United States has provided evidence that Tembec's divisional data were not required to be kept in accordance with GAAP.⁵⁵ Thus, Commerce was under no obligation to consider them.

69. In fact, whenever possible Commerce relied on audited amounts for the dumping calculation. To the extent that Tembec's divisional data were used for an extremely limited purpose (*i.e.*, establishing packaging costs to be removed from the G&A ratio), Commerce relied on this data because audited, GAAP consistent data were not available.

D. *Specialized accounting standards are irrelevant to the Panel's inquiry:*

70. Canada argues that based on the Federal Acquisition Regulation ("FAR"), Commerce's determination that G&A relates to a company as a whole is unreasonable.⁵⁶ However, the FAR standards are specialized accounting rules that relate to government procurement and are not equivalent to generally accepted accounting principles. Commerce's determination that general costs relate to a company as a whole is a reasonable interpretation of the term "general costs" found in

⁵² Canada Second Written Submission, para. 223.

⁵³ *Id.*

⁵⁴ See Tembec's Annual Report, "Auditor's Report," p. 34 (Exhibit US-12) (stating that only the company-wide statements were audited).

⁵⁵ See Exhibit US-80, p. 2.

⁵⁶ See, *e.g.* Canada Second Oral Statement, para. 86.

Article 2 of the AD Agreement.⁵⁷ Moreover, as discussed above, Tembec has failed to provide any credible evidence that its lumber division incurred less G&A than its other divisions.⁵⁸

E. Tembec's divisional statements are not audited and have not been shown to be in accordance with GAAP:

71. Canada argues that the divisional data are audited and reliable. However, the Auditor's Statement clearly indicates that the portion of Tembec's consolidated balance sheet that was audited does not include the divisional information.⁵⁹ Moreover, the United States has shown that under Canadian accounting practices, divisional data are not meant to be an objective measure of costs. Rather, they are meant to enable financial statement users to see the business through the eyes of the management.⁶⁰ Finally, the United States has shown that divisional data in Canada do not have to be kept in accordance with Canadian GAAP.⁶¹

To both parties:

121. Was the "internal accounting methodology" referred to in Comment 33, p. 105, of the Memorandum of 21 March 2002 an allocation methodology "historically utilized by the exporter"? Please refer to the record.

72. Tembec presented no evidence of its historical allocation. In any event, under Article 2.2.1.1 an investigating authority is obligated to consider historical allocations only when such historical allocations are shown to be in accordance with GAAP and to be not distortive. No evidence was presented that Tembec's divisional data were kept in accordance with GAAP.⁶² Moreover, the United States has provided evidence that Tembec's divisional data were not required to be kept in accordance with GAAP nor were they required to be objective measure of costs.⁶³ Thus, even assuming, *arguendo*, that Tembec has historically allocated costs between divisions in the same manner, Commerce was under no obligation to consider Tembec's division-specific G&A data. While historical use may indicate some consistency of compilation or presentation of information over time, historical use alone cannot impart reliability or consistency with GAAP.

I. WEYERHAEUSER:

To the US:

123. It is stated in para. 84 of the US Second Written Submission that:

"[g]eneral expenses are, by definition, expenses incurred for the benefit of a corporate group as a whole. They are not specific to one or another product line. A requirement that general expense be directly related to the good produced would make it impossible to allocate general expense within a company that produces many goods because a direct relationship would never

⁵⁷ See US First Written Submission, para. 200; *see also* Joel G. Siegel, Jae K. Shim, *Dictionary of Accounting Terms* (Barrons Educational Services, Inc. 2nd ed. 1995) (Exhibit US-47).

⁵⁸ See *supra* answer to question 120(A).

⁵⁹ See Tembec's Annual Report, "Auditor's Report," p. 34 (Exhibit US-12) (stating that only the company-wide statements were audited).

⁶⁰ See Exhibit US-80, p. 2.

⁶¹ See *id.*

⁶² See Tembec's Annual Report, "Auditor's Report," p. 34 (Exhibit US-12) (stating that only the company-wide statements were audited).

⁶³ See Exhibit US-80, p. 2.

be identifiable. This would render meaningless the requirement of Article 2.2 that "a reasonable amount for administrative, selling and general costs" be included in a company's cost calculation."

In its practice, how does DOC treat G&A costs which have been demonstrated to it not to "pertain[] to production and sales (...) of the like product" in accordance to the chapeau of Article 2.2.2? Please provide a recent example of that practice.

73. As an initial matter, the United States disagrees with the proposition that G&A costs may pertain more or less to a product. G&A, by definition, relates to a company as whole.⁶⁴ In its Second Written Submission Canada agrees that G&A does not pertain to products.⁶⁵

74. Commerce does have, however, a practice whereby it excludes G&A that does not pertain to a company from that company's G&A calculation. More specifically and as discussed in the United States' Second Oral Statement.⁶⁶ Commerce's administrative practice is to include a portion of a parent company's G&A costs in a producer's G&A.⁶⁷ However, if it is shown that the parent company does not perform any functions on behalf of the subsidiary, Commerce considers that parent company's G&A to not pertain to the subsidiary company and does not allocate any of the parent company's G&A to the subsidiary. An example of this practice is the *Brass Sheet and Strip* determination cited by Canada.⁶⁸ In fact, Canada has not challenged Commerce's practice and agrees that a portion of the parent company's G&A, including G&A listed separately on the parent company's financial statement, should be included in Weyerhaeuser Canada's G&A.⁶⁹

124. It is stated on page 51 of the year 2000 annual report of Weyerhaeuser Company (Exhibit CDA-166) that:

"[t]his is a claims-based settlement, which means that the claims will be paid as submitted over a nine-year period with no maximum or minimum amount."

In determining the amount attributable to the period of investigation [POI], did DOC take into account that the claims would be paid as submitted over a nine-year period with no maximum or minimum amount? Or, did DOC allocate the whole amount booked by the company to the POI? Please explain.

75. Consistent with Weyerhaeuser's treatment of the entire litigation cost as a period expense for fiscal year 2000 in its own books and records, Commerce included the entire litigation cost in its G&A ratio. In other words, Weyerhaeuser recognized the entire litigation cost in the year in which it

⁶⁴ See Joel G. Siegel, Jae K. Shim, *Dictionary of Accounting Terms* (Barrons Educational Services, Inc. 2nd ed. 1995) (Exhibit US-47).

⁶⁵ See Canada Second Written Submission, para. 166. ("Administrative, selling and general costs' . . . are costs that are not directly attributable to the product under investigation or any particular product.")

⁶⁶ United States Second Oral Statement, para. 73.

⁶⁷ See *Final Determination of Sales at Less Than Fair Value; Certain Hot-Rolled Carbon Steel Flat Products from Thailand*, 66 Fed. Reg. 49,622 and accompanying Issue and Decision Memorandum at Comment 7 (28 Sept. 2001) (stating Commerce's practice is to "calculate G&A expenses based on the company-specific unconsolidated financial statements of the producing entity ...we also include in the company's G&A an amount for administrative services performed on the company's behalf by it parent.") (Exhibit US-82).

⁶⁸ See *Brass Sheet and Strip from Canada; Final Results of Antidumping Duty and Administrative Review*, 61 Fed. Reg. 46618, 46619 (4 September 1996). (Exhibit CDA-104.)

⁶⁹ See Canada Second Written Submission, para. 230, where Canada concedes that other separately listed items on the parent company's financial statement constituted general costs and were properly included in Weyerhaeuser Canada's G&A ratio. See also United States Second Written Submission, para. 89 footnote 149.

was incurred (*i.e.*, the POI). Weyerhaeuser never argued before Commerce that this litigation cost should be treated as anything other than a period cost. (*E.g.*, Weyerhaeuser never argued that the settlement cost should be amortized over several years.) Instead, it argued only that the entire cost should be excluded from the allocation of G&A to softwood lumber production.

125. Please comment on the following portion of para. 229 of Canada's Second Written Statement:

"Commerce agreed that it was proper to exclude the expense from parent company G&A in its preliminary determination".

76. Commerce permitted the exclusion of the settlement cost for the *Preliminary Determination* because it was only at verification that Commerce became cognizant of the fact that Weyerhaeuser had excluded the settlement cost from the parent company's reported G&A. In an antidumping investigation verification occurs after the preliminary determination. As discussed in the *Final Determination*, once Commerce considered the settlement cost it determined that the settlement cost was properly considered part of the parent company's G&A and allocated a portion of it to softwood lumber.⁷⁰

126. Please comment on the following portion of para. 93 of Canada's Second Oral Statement:

"the United States never responds in any of its submissions to the fact that Commerce's traditional practice has been to exclude unrelated parent company G&A, finding on numerous occasions that not all G&A is fungible."

77. It is Commerce's standard practice to exclude a parent company's G&A if evidence is presented that the parent company did not perform any functions on behalf of the subsidiary.⁷¹ as was the case in the *Brass Sheet and Strip* determination cited by Canada.⁷² However, this case and Commerce's practice when a parent company performs no functions on behalf of a subsidiary are irrelevant to Weyerhaeuser Canada's G&A calculation, because it is uncontested that the parent company performed functions on behalf of Weyerhaeuser Canada. In any event, Canada has not objected to the inclusion of a portion of the parent company's G&A in Weyerhaeuser Canada's G&A.⁷³ Thus, Canada has not challenged the fungibility of the parent company's G&A in relation to Weyerhaeuser Canada. Instead Canada has challenged only the inclusion of a portion of the litigation cost in Weyerhaeuser Canada's G&A.

127. Please comment on the following extract of para. 90 of Canada's Second Oral Statement:

"Cost Verification Exhibit 26 breaks down the elements of Weyerhaeuser US G&A expense, including a line item for Law of [[]]. This represented the company's general legal

⁷⁰ See *Final Determination*, Comment 48b (Exhibit CDA-2).

⁷¹ See *supra* answer to question 123.

⁷² See *Brass Sheet and Strip from Canada; Final Results of Antidumping Duty and Administrative Review*, 61 Fed. Reg. 46618, 46619 (4 September 1996). (Exhibit CDA-104); see also Canada Second Written Submission, para. 230, where Canada concedes that other separately listed items on the parent company's financial statement constituted general costs and were properly included in Weyerhaeuser Canada's G&A ratio; see also United States Second Written Submission, para. 89 footnote 149.

⁷³ See Canada's Second Written Submission, para. 230 explaining which portion of the parent company's G&A it did not object to Commerce including in Weyerhaeuser Canada's G&A calculation.

expenses. The [[]] hardboard siding expense is not listed."
[footnote excluded]

78. The proper characterization of the hardboard siding litigation expense does not depend on the break-out of that expense by Weyerhaeuser US in its books and records. What is relevant is the inherent nature of the expense. A company usually breaks out particular costs because they are significant and require further explanation⁷⁴, as was the case with the litigation cost on Weyerhaeuser's consolidated financial statement. However, if a cost item is general in nature, listing it separately from the generic G&A line item does not change its general nature. In point of fact, Weyerhaeuser listed another category of general costs, "integration and closure costs," separately on its financial statement. Canada does not challenge the inclusion of these "integration and closure costs" in the G&A ratio for Weyerhaeuser Canada. Similarly, Commerce's inclusion of a portion of the litigation costs in Weyerhaeuser Canada's G&A was reasonable.

J. TEMBEC (BY-PRODUCT REVENUE):

To the US:

128. How was the arm's length test applied? Canada states in para. 235 of its First Written Submission that:

"[w]here the average price charged to affiliated purchasers was higher than the average price charged to unaffiliated purchasers, DOC concluded that a respondent had sold chips to its affiliated purchasers at inflated, non-market prices. In these situations, DOC disregarded the revenues in a respondent's books and records for its sales to affiliated purchasers and re-valued those sales based on the lower price that the respondent charged to unaffiliated purchasers."

Does Canada's assertion accurately reflect DOC's practice as applied in the softwood lumber anti-dumping investigation? In particular, did DOC disregard West Fraser's British Columbia revenues from sales to affiliated parties on the ground that they were made at "inflated, non-market prices"? Please explain.

79. This question appears under the heading "Tembec (By-Product Revenue)." However, Commerce did not apply an arm's length analysis with respect to Tembec's by-product revenues. As explained in the *Final Determination*, with respect to Tembec, the wood chip transactions were between divisions of the same legal entity. Commerce's practice with respect to transactions within the same legal entity is to use the actual cost of the input.⁷⁵ By-products, by their nature, have no directly attributable costs. Thus, Commerce first looked to Tembec's books and records, as required by the AD Agreement, to determine a reasonable value for wood chips. Commerce then compared Tembec's internal values with Tembec's market-based wood chip sales prices. Just as internal costs are generally lower than market prices, in light of the existence of profit, so, too, are by-product offsets to cost calculations generally lower than the market value for a by-product. Commerce observed that Tembec's transfer prices between divisions were lower than its sales prices to unaffiliated parties. It therefore determined that the use of the lower prices was a reasonable estimate of cost for the by-product.

⁷⁴ See Susan Weiss Budak, Patrick R. Delaney, Barry J. Epstein, and Ralph Nach, Wiley GAAP 2002: Interpretation and Application of Generally Accepted Accounting Principles 2000, p. 76 (John Wiley & Sons 2001). (Exhibit US-83).

⁷⁵ *Final Determination*, Comment 11 at 60 (Exhibit CDA-2).

80. It is important to note that, in the case of Tembec, Commerce examined unaffiliated market prices not for purposes of applying an arm's length analysis but as a starting point in determining the cost of the wood chips. Commerce's approach was consistent with the preference that Article 2.2.1.1 of the AD Agreement expresses for reliance on a producer's own books and records.

81. With regard to West Fraser, Canada's statement in paragraph 235 of its First Written Submission accurately reflects Commerce's general application of the arm's length test. However, it is important to note that Commerce does not apply this test blindly, but will review the prices reported in the books and records of a respondent to determine if there are particular factors which justify the use of higher affiliated transaction values. In this case, Commerce disregarded West Fraser's B.C. revenues from sales to affiliated parties where the average price charged to affiliated purchasers was higher than the average price at which wood chips were sold to unaffiliated purchasers. It is important to note that Commerce's arm's length test – which Canada does not challenge *per se*⁷⁶ – is premised on the recognition that affiliated party transactions are inherently unreliable and are, therefore, subject to searching scrutiny. In determining whether transactions between affiliated parties occurred at arm's length prices, Commerce determined that West Fraser's affiliated sales prices were higher than its unaffiliated sales prices.⁷⁷ Consistent with this finding, Commerce disregarded the affiliated prices and revalued West Fraser's chip sales based on the unaffiliated sales prices.

82. The AD Agreement expresses a preference for calculating costs based on a party's books and records, unless those data do not reasonably reflect the costs associated with the production and sale of the product under consideration. In applying its arm's length test to West Fraser's affiliated chip sales, Commerce determined that those sales did not reasonably reflect the costs associated with the production and sale of the product under consideration. Therefore, consistent with Article 2.2.1.1, Commerce revalued those chip sales based on unaffiliated sales prices.

129. Canada draws an analogy between the present case and the finding in para. 148 of the AB in US - Hot-Rolled Steel that "discretion must be exercised in an even-handed way that is fair to all parties affected by an anti-dumping investigation." Please comment.

83. Canada's analogy to the Appellate Body's finding in *United States-Hot-Rolled Steel* is inapposite. At issue in *United States-Hot-Rolled Steel* was Commerce's practice for excluding from its calculation of normal value affiliated party sales determined to be outside the ordinary course of trade. Under that practice, Commerce automatically excluded from the normal value calculation sales to affiliated parties at prices that are less than 99.5 per cent of a weighted average of sale prices to unaffiliated parties. Japan objected to that practice, in part because no similar, automatic exclusion applied to sales to affiliated parties at prices that were greater than 100.5 per cent of a weighted average of sale prices to unaffiliated parties. In other words, Japan objected to the lack of symmetry between the treatment of low-priced sales between affiliates and the treatment of high-priced sales between affiliates.

84. In contrast, the wood chip offset issues in the present dispute do not raise a symmetry question. The proposition that even-handedness requires similar situations to be treated similarly does not mean that Commerce's method for evaluating wood chip sales to affiliated customers must be identical to its method for evaluating wood chip transfers between two divisions of the same company. That is because sales to affiliates and transfers between divisions are not similar transactions. They are fundamentally different types of transactions. Even-handedness does not require that they be evaluated in an identical way.

⁷⁶ See, e.g., Canada's First Written Submission, para. 243.

⁷⁷ This analysis is reflected in DOC Memorandum on West Fraser's Cost of Production and Constructed Value Calculation Adjustments for the *Final Determination*, at 2 and attach. 1 (Exhibit CDA -108).

85. As the United States has explained in prior submissions, sales to affiliates are fundamentally different from transfers between divisions. In the case of sales to affiliated companies, the question is whether those sales reflect a true market price, unaffected by the affiliation between the buyer and seller. In the case of internal transfer prices between divisions, the question is whether the internal transfer price used by the company reasonably reflects the company's cost of producing the by-product being used as an offset. In the softwood lumber investigation, Commerce did calculate wood chip offsets in "an even-handed way that is fair to all parties affected." However, contrary to Canada's suggestion, even-handedness did not require it to apply the same methodology to fundamentally different factual situations.

86. It is also worth noting that, where an arm's length test was applied, as in the case of West Fraser, Canada has not challenged *per se* Commerce's arm's length test, only aspects of its application with respect to the wood chip by-product issues. In its First Written Submission, Canada stated that it:

does not dispute that a determination of non-arm's length pricing could support a determination that books and records containing such prices might not reasonably reflect the costs associated with the production and sale of the product under consideration. In such an instance, the investigating authority might legitimately resort to alternative data and disregard the books and records.⁷⁸

Indeed, Canada has not objected to the use of the arm's length test as it was applied by Commerce to other respondents. Its objection with respect to West Fraser is simply that "an unbiased and objective investigating authority could not have found that West Fraser's recorded chip sales to affiliated purchasers were made at inflated, non-market prices."⁷⁹ Commerce's application of an arm's length analysis in reviewing West Fraser's affiliated wood chip sales was exercised in an even-handed way that was fair to the party affected.

130. Please comment on para. 107 of Canada's Second Oral Statement.

87. The accounting text that Canada cites for the proposition that transactions between affiliated entities should be evaluated in the same manner as transactions between divisions of the same entity does not support its argument. In fact, the text is silent on this issue. Its silence does not amount to a recognition of a prohibition on different methods of evaluating sales to affiliates versus inter-divisional transfers.

88. Moreover, the accounting text cited by Canada at para. 107 of its Second Oral Statement actually supports the US argument that the difference between inter-divisional transfer prices and sales prices to unaffiliated entities is a function of profit, or "gain." The text states that "[a]ny differences between actual selling prices and prices used in by-product costing are treated as a gain or loss."⁸⁰ As the United States has explained, the AD Agreement requires that Commerce determine whether reported costs reasonably reflect costs of production. Sales of merchandise in the market typically include not only actual costs of production, but an additional amount for profit. Thus, while a company may assign a value to a by-product, it generally will sell that by-product for a higher amount to unaffiliated purchasers. The accounting literature cited by Canada confirms the very idea that Canada has rejected: that a company may derive a "gain" from the sale of a by-product in the marketplace, much the same way it would derive "profit" for the sale of factors of production in the marketplace.

⁷⁸ Canada First Written Submission, para. 243.

⁷⁹ *Id.* at para. 244.

⁸⁰ W.J. Morse and H.P. Roth, *Cost Accounting: Processing, Evaluating, and Using Cost Data*, 3rd ed. (Reading, Mass.: Addison-Wesley, 1986), at 157-158. (Exhibit CDA-175.)

K. WEST FRASER:

To the US:

133. With respect to West Fraser's McBride mill, the following statement is contained in p. 23 of DOC's verification report (Exhibit CDA-110):

"[c]ompany officials explained that the McBride mill had a long-term contract in effect for chip sales when the mill was purchased and that all sales occurred during April and May 2000. They explained that the sales value of chips increased in May 2000 and that they were obligated to sell the chips at the lower contracted price."

Did DOC consider the above findings in the context of the investigation? If so, how. Please direct the Panel to the record. The Panel notes that in at least two instances DOC – that is, with respect to Canfor and Tembec – decided not to use certain price data for sales to unaffiliated parties. How did those situations relating to Canfor and Tembec differ, if at all, from that of the McBride mill?

89. Regarding whether Commerce considered the findings of its verification report, three points are worth noting: (1) West Fraser never argued that its unaffiliated McBride mill sales were made under circumstances that caused them not to reasonably reflect the market values for West Fraser's chips, and in fact, Commerce found at verification that the McBride mills sales reasonably reflected a market value for wood chips;⁸¹ (2) even if West Fraser had made this claim in the investigation, there is nothing about the nature of the long-term contract that would cause the transactions to be "noncommercial," given that long-term contracts are common commercial instruments;⁸² and (3) Commerce did not rely solely on the McBride mill sales in its analysis; it also considered the Pacific Island Mill transactions, which were market-based transactions.⁸³

90. The Panel refers to the treatment of sales to unaffiliated parties by Tembec and Canfor. With respect to Tembec, all related-party sales were between divisions of the same legal entity.⁸⁴ Comparing Tembec's internal transfer prices for chips in British Columbia with Tembec's B.C. sales of chips to unaffiliated parties, Commerce determined that the internal transfer prices were reasonable surrogates for wood chip costs.⁸⁵ For Tembec's Quebec and Ontario internal chip sales, there was no usable market price data to evaluate whether internal transfer prices were preferential. Thus, Commerce applied the company-specific finding for Tembec's B.C. chip sales, *i.e.*, that the internal transfer prices for chips were not preferential, to the company's Quebec and Ontario chip sales and determined that Tembec's internal transfer prices for chips were not preferential and could be relied upon for the final determination. In other words, the results of the analysis on Tembec's B.C. chip sales were sufficiently reliable that they could be applied to the company's chip sales in other provinces. There was no claim that any contractual arrangements influenced the price of Tembec's

⁸¹ See US First Written Submission, para. 224, and record citations therein. Notably, Canada stresses the importance of the alleged noncommercial nature of West Fraser's McBride Mill contracts in front of the Panel, but during the investigation, West Fraser never even placed the contract on the record. The commercial/noncommercial status of the contract was never called into question by West Fraser, so it was not an issue specifically addressed by Commerce.

⁸² US Opening Statement at Second Substantive Meeting, para. 79.

⁸³ See, *e.g.*, West Fraser Cost Verification Exhibit C5, WF-Cost 007503 (Exhibit CDA-106); US First Written Submission, para. 219; US Answers to Panel's 19 June 2003 Questions, para. 71;

⁸⁴ See DOC Verification Report on the Cost of Production and Constructed Value Data Submitted by Tembec Inc. (29 January 2002) (Exhibit CDA-112 - Contains Business Confidential Information).

⁸⁵ *Final Determination*, Comment 11 at 61 (Exhibit CDA-2).

chip sales to either affiliated or unaffiliated parties. For these reasons, the facts regarding Tembec are different from those involving West Fraser.

91. With respect to Canfor, Commerce determined that its sales of wood chips from Alberta sawmills to unaffiliated purchasers were distorted due to so-called "contractual arrangements" that did not reflect any market price during the relevant period. The exact nature of Canfor's "contractual arrangements" in Alberta is business confidential information that cannot be disclosed in this proceeding, but it is a completely different factual situation from West Fraser's contract between the McBride mill and certain unaffiliated purchasers.⁸⁶ Thus, there was no reliable basis upon which to perform the arm's-length test for Canfor's chip sales in Alberta. In British Columbia, Canfor's sawmills made no sales of chips to unaffiliated parties.⁸⁷ With no unaffiliated chip sales in British Columbia, and no reliable results from Alberta that could be applied to British Columbia (different from Tembec's situation), Commerce was left with one option – comparing Canfor's chip sales to affiliates in British Columbia with the weighted-average market price of other respondents' unaffiliated chip sales in British Columbia. The result was that Canfor's affiliated chip sales were found to be at arm's-length prices.

92. These wood chips sales situations of Tembec and Canfor were different from the situation of West Fraser. First, West Fraser was the only one of these three respondents that had chip sales to both affiliated parties and unaffiliated parties in all provinces in which it had chip sales. Second, neither Canfor nor Tembec had contractual issues similar to West Fraser's. There were no contractual issues associated with Tembec's chip sales, and the contractual issues raised in connection with Canfor's chip sales were completely different factually from West Fraser's issues. Third, although Canada attempts to characterize West Fraser's unaffiliated B.C. chip sales as *de minimis*, those sales were actually sizable.⁸⁸ Accordingly, West Fraser was differently situated than Canfor and Tembec. In light of the differences, it was appropriate for Commerce to apply a different evaluation to West Fraser's wood chip offset than it applied to Canfor or Tembec's offset.

L. SLOCAN:

To the US:

137. It is stated in para. 319 of Canada's Second Written Submission that:

"Commerce did not include Slocan's futures trading profits anywhere in its preliminary determination."

With respect to the Final Determination, it is stated in para. 327 of Canada's Second Written Submission that:

"Commerce's Final Determination left Slocan's futures revenue unaccounted-for and excluded from the margin calculation."

Does the US agree with the above statements and other statements to that effect, contained in Canada's Second Written Submission?

93. While the quoted statements from paragraphs 319 and 327 of Canada's Second Written Submission are factually correct, they are incomplete and misleading.

⁸⁶ See US First Written Submission, para. 255, note 268.

⁸⁷ *Id.* at 60.

⁸⁸ See US First Written Submission, para. 219.

94. Contrary to Canada's suggestion, throughout the course of the investigation, Commerce gave full and fair consideration to the adjustments that Slocan sought for its futures contract revenues. Moreover, contrary to Canada's suggestion, there was no requirement that these amounts be included in the margin calculation absent a demonstration of effect on price comparability, as provided in Article 2.4 of the AD Agreement.

95. As the panel in *Egypt-Rebar* stated, the burden of substantiating a claim for an adjustment rests with the party seeking the adjustment — here, Slocan — not with the investigating authority.⁸⁹ The respondent has an affirmative obligation both to assert and to justify the information and arguments required to prove its claims. Not only is this what Article 2.4 provides, it also makes sense, inasmuch as the relevant information will be in the respondent's hands. The investigating authority has no duty to explore or grant adjustments that have neither been requested nor demonstrated by the respondent.

96. Slocan sought two alternative adjustments for its futures contract revenues. First, it asked to have the revenues treated as an offset to direct selling expenses. Alternatively, it asked to have them treated as an offset to financing expenses. Slocan did not request nor did it demonstrate any further alternative basis for an adjustment.

97. Once Commerce evaluated and properly rejected the two bases for adjustment that Slocan requested, Commerce had satisfied its obligation to consider an adjustment. Any other conclusion suggests that respondent companies are free to make general claims of entitlement to adjustment with minimal explanation of the data and that it is the obligation of an investigating authority to find the appropriate basis for adjustment, even though the explanation may be incomplete, unclear, or contradictory. The AD Agreement does not require such an illogical result. The only requirement under Article 2.4 is that due allowance be made, "in each case on its merits," where the difference is "demonstrated" to affect price comparability.⁹⁰

138. Please comment on the following statement contained in Exhibit CDA-123, page III.55:

"[f]utures hedging contracts are not direct selling expenses/income, as they are not directly related to sales. They are indirect selling expense/income, not a financing expense/income, and as such also are not proper as a set-off for interest expenses included in production costs."

98. Exhibit CDA-123 is an excerpt from the Response Brief of the Investigating Authority to the NAFTA panel considering Commerce's lumber antidumping investigation. The quoted statement was Commerce's response to Slocan's submission to the NAFTA Panel, in which Slocan stated *for the first time* that the futures profits might be an indirect selling expense/income. Slocan had made a *post hoc* argument to which Commerce responded, as quoted above. Commerce's statement correctly summarizes its post-proceeding understanding of how Slocan could have presented (but did not in fact present) its request for adjustment. However, that observation — made in litigation subsequent to the investigation — has no bearing on the question before this Panel. The sole question before this Panel is whether Commerce's rejection of Slocan's two alternative bases for its requested adjustment was based on a proper establishment of the facts and an unbiased and objective evaluation of those facts. The United States notes, moreover, that Slocan's only submission during the investigation regarding

⁸⁹ *Egypt-Rebar*, paras. 7.381, 7.387 (claim for adjustment for credit cost not properly raised at agency level).

⁹⁰ See US First Answers to Panel Questions, para 137.

any possible indirect selling expenses was, in fact, its unambiguous assertion in its 23 July 2001, Questionnaire Response that it had incurred *no* indirect selling expenses in the United States.⁹¹

139. Please comment on para. 192 of Canada's replies to Question 77 of the Panel:

"[t]he prices that it offers on other sales are thus different than they would have been absent the safety net that hedging contracts provide, [sic] Thus, hedging activity, by definition, affects prices for all sales in the market, not only those made through the CME."

99. Canada's argument is *post hoc* rationalizations. Slocan made no such argument during the investigation to support its requested adjustment.

100. As the United States stated in response to oral questions at the Second Panel Meeting, the total evidence on this issue consisted of two general sentences in Slocan's Section C Questionnaire Response, plus a brochure on hedging that was provided at verification. This evidence failed to demonstrate an effect on price comparability necessary to support an adjustment. There is no *per se* rule — such as Canada advocates — that futures trading by definition affects all sales in the market.

101. In its 23 July 2001 Questionnaire Response, Slocan unambiguously stated that the hedging profits should be treated as an offset to direct selling expenses in the US market, as an adjustment for differences in the conditions and terms of sale.⁹² It stated:

Sometimes Slocan will sell its short positions and take the loss or profit between the sale and strike prices. These expenses or revenues are linked to Slocan's sales in the United States and so are being reported as direct selling expenses.⁹³

Slocan failed to explain the link between these expenses or revenues and any particular US sales of lumber. It also said nothing about how its contracts might affect prices to US customers. The facts failed to demonstrate that these profits should be considered an offset to direct selling expenses. They were not directly related to particular softwood lumber sales.⁹⁴

102. Canada has engaged in a *post hoc*, theoretical exercise by now asserting: "Once Slocan demonstrated that it engaged in futures trading activity, which necessarily affects price comparability, Article 2.4 required Commerce to make an adjustment."⁹⁵ This is a new assertion made by Canada, which has no basis in Article 2.4 or in the investigation record. Slocan introduced no evidence to demonstrate — as Canada now claims — that "hedging through futures trading activity affects all sales in a particular market."⁹⁶

103. The record evidence submitted by Slocan states that: "The purpose of hedging is *to reduce the risk of holding lumber inventory*."⁹⁷ The *Random Lengths* brochure on hedging (supplied by Slocan at verification) also states that when a company hedges, it can "*reduce the risk of holding or acquiring*

⁹¹ Response of Slocan Forest Products Ltd To Sections B, C, & D of the Department of Commerce Antidumping Questionnaire, 23 July 2001, pages C35-37 (Exhibit US-71).

⁹² Response of Slocan Forest Products Ltd To Sections B, C, & D of the Department of Commerce Antidumping Questionnaire, 23 July 2001, page C35-37 (Exhibit US-71). In the same submission, Slocan unambiguously asserted that it did not incur indirect selling expenses.

⁹³ *Id.*, p. C-35-36 (Exhibit US-71).

⁹⁴ See Slocan Cost Verification Report at 26 (Exhibit CDA-118); see also *Final Determination*, Comment 21 (Exhibit CDA-2).

⁹⁵ Canada Second Written Submission, para. 336; see also notes 356 and 363.

⁹⁶ Canada Second Written Submission, note 356.

⁹⁷ Sales Verification Report of 28 January 2002, Exhibit 21 at VE 02361, Exhibit CDA-119.

inventory through taking an equal and opposite position in the Random Length Lumber futures market."⁹⁸

104. A demonstration that hedging is used to reduce the risk of holding inventory is *not* a demonstration of an effect on all prices in the market. Slocan's evidence does not demonstrate the *per se* effect on price comparability asserted by Canada. Nor does it demonstrate that Slocan's futures contracts (which did not result in delivery) affected any lumber prices included in our analysis. Contracts that resulted in actual delivery to Slocan's customers (in fact, the only sales for which prices were affected) were included as sales in the calculation of Slocan's dumping margin. But the profits earned on contracts that were sold and did not result in lumber delivery are not a proper basis for adjustments for terms and conditions of sale. Accordingly, Commerce appropriately rejected Slocan's requested adjustment.

To both parties:

140. Please provide in diagram format the company structure of Weyerhaeuser International Inc., showing the relationship between Weyerhaeuser Canada, Weyerhaeuser US and Weyerhaeuser International Inc. In addition, could Canada provide the structure of the financial records of the different entities, that is, at which level are they audited/consolidated.

105. In the *Softwood Lumber* anti-dumping investigation, the Department of Commerce ("Commerce") received information from Weyerhaeuser Company, located in the United States, and its wholly-owned Canadian subsidiary, Weyerhaeuser Company Ltd. (collectively, "Weyerhaeuser"). The structure of these companies, in diagram format, was submitted in the administrative record of the underlying investigation as part of Weyerhaeuser's response to the Department of Commerce's Section A Questionnaire. (Weyerhaeuser's 22 June 2001, Section A Questionnaire Response at A-7 and Exhibits A-3 and A-5.) Because these diagrams have been designated as containing proprietary information by Weyerhaeuser, the Canadian respondent, it is more appropriate for the Government of Canada to submit them in response to the Panel's request. Explanations of this structure were also provided in Weyerhaeuser's 23 July 2001, Section D Response, at D-24-25, where it was noted that Weyerhaeuser Company prepares consolidated financial statements in accordance with US GAAP and that Weyerhaeuser Company Ltd. prepares a set of financial statements for tax purposes.

⁹⁸ Sales Verification Report of 28 January 2002, Exhibit 21, Random Lengths - An Introductory Hedge Guide, at VE 02364, Exhibit CDA- 119.