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FOR ELECTRONIC SUBMISSION

Donald W. Eiss
Chairman, Trade Policy Staff Committee
Office of the U.S. Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508

Re: Canada's Expression of Interest in the Trans-Pacific Partnership Trade Negotiations (Docket No. USTR-2011-0019)

Dear Mr. Eiss:

These comments are submitted on behalf of the U.S. Lumber Coalition[1] (the "Coalition") in response to the "Request for Comments on Canada's Expression of Interest in the Proposed Trans-Pacific Partnership Trade Agreement" published by your office on December 7, 2011.[2] They are submitted within deadline set forth in the notice and contain no business confidential information.

The Coalition welcomes Canada's expression of interest in joining the Trans-Pacific Partnership ("TPP") negotiations. More than two decades of free trade between the United States and Canada, first under the U.S.-Canada Free Trade Agreement and then under the North

[1] The U.S. Lumber Coalition, formerly known as the Coalition for Fair Lumber Imports, is an association of domestic entities interested in promoting fair trade in softwood lumber products. Members of the Coalition were petitioners in the antidumping and countervailing duty proceedings that were settled in the 2006 Softwood Lumber Agreement.

[2] 76 Fed. Reg. 76,480 (USTR Dec. 7, 2011).

American Free Trade Agreement ("NAFTA"), have facilitated an ever-deeper economic integration between the United States and Canada, largely to the benefit of both nations. Canada is the largest trading partner of the United States, and the vast majority of the trade between the United States and Canada takes place without friction or dispute. Unfortunately, the softwood lumber sector remains one of the relatively few areas where significant trade friction remains between our two countries. These disputes are rooted in the way Canada manages its publicly owned forests for the benefit of its domestic processing industries, which are significantly oriented towards exports, especially to the United States. These trade-distorting Canadian policies are mostly unaddressed by, or specifically exempted from, the disciplines of the existing free trade agreements. The Coalition believes that Canada's participation in the negotiation of a "high-standard, 21st century" trade agreement, 76 Fed. Reg. at 76,480, can provide a meaningful opportunity to address these policies and reduce trade friction in this important sector.

In Canada, authority over public forests and other natural resources located on public lands is vested in the provincial governments. In the provinces of Alberta, British Columbia, Manitoba, Ontario, Quebec, and Saskatchewan – which together accounted for more than 88 percent of Canada's softwood lumber exports to the United States in 2011[3] – public land provides more than 80 percent, and in some cases as much as 99 percent, of the softwood timber used in lumber production. In New Brunswick, which accounts for most of Canada's other softwood lumber exports, around 50 percent of the timber used to produce softwood lumber comes from public land. While each province's timber management and pricing system is

[3] Based on export permits issued under the Softwood Lumber Agreement 2006; monthly data provided by Canada's Department of Foreign Affairs and International Trade and available at www.international.gc.ca/controls-controles/softwood-bois_oeuvre/.

unique, none of them sell or price timber on a purely commercial basis. Rather, the provinces use their ownership of the resource to provide competitive advantage to local industry and to advance other governmental objectives. Because the cost of fiber is well over half the cost of producing lumber, the importation of substantial quantities of Canadian softwood lumber into the United States causes significant imbalances in the U.S. lumber market and harms U.S. producers, who must pay market prices for their fiber supply in a fully competitive U.S. timber market. These practices, and the resulting injury to U.S. industry, have been the subject of numerous antidumping and countervailing duty proceedings over the past three decades, as well as three international agreements between the United States and Canada to regulate trade in softwood lumber products. The most recent of these agreements, the Softwood Lumber Agreement 2006 ("SLA"), expires in October 2013, although the two governments may extend the agreement for an additional two years.

Canada's participation in the TPP initiative offers several opportunities to address key aspects of this ongoing dispute in a more permanent fashion. We discuss three of those opportunities below.

1. <u>The TPP Should Not Exempt Canada's Log Export Restrictions from Any Disciplines on Export Restraints</u>

Existing U.S. free trade agreements include significant disciplines on the ability of our free trade partners to impose restrictions on exports. For example, NAFTA (following World Trade Organization ("WTO") norms) forbids "any prohibition or restriction . . . on the exportation or sale for export of any good destined for the territory of any other Party." NAFTA art. 309(1). In addition, with the exception of certain derogations set forth in Annexes 314 and 315, the NAFTA Parties agreed to prohibit all export taxes (unless also imposed on exports of

the same good to other Parties and domestic consumers) and other WTO-consistent export restrictions that distort trade between the Parties. Id. arts. 314, 315. However, NAFTA exempts the application of even the most basic NAFTA disciplines on export measures to "controls by Canada on the exports of logs." Id. Annex 301.3(A)(1).

Indeed, Canada continues to maintain significant restrictions on the exports of unprocessed logs. As explained in more detail in section 3 below, in every province Crown timber is sold only to entities that agree to process timber within Canada (and usually within the province of sale). This policy effectively prevents the export of logs harvested from Crown timber, unless the province grants an exception. In British Columbia ("BC"), where most of the logs that are in fact exported from Canada originate, exceptions are granted only if logs are deemed to be "surplus" to local requirements. In practice, this means that local mills are provided an opportunity to "block" any or all export sales by making an offer (which does not need to be followed through upon) to purchase the logs at the prevailing domestic price, which is usually far lower than the export price. In addition, when Crown logs are exported, a "fee in lieu of domestic manufacture" must be paid to the BC government. Federal export laws, implemented by the BC government, impose a similar surplus-needs test and blocking capability even on timber harvested from private land, and at least some private timber is also subject to the "fee in lieu" requirement where export is permitted. Indeed, it is not uncommon that the "fee in lieu" that harvesters of logs on private land must pay to the BC government upon export is greater than the timber price that BC would charge a harvester of logs on Crown land, if the harvester agrees to process those Crown logs in BC.

The Coalition believes that no similar exemption for Canada's log export restrictions should be maintained in a TPP agreement. These restrictions are not merely incompatible with

the theoretical notion of free trade, but have significant economic effects. Domestic log prices within Canada are significantly lower than world market prices, which has in turn has a substantial market-distorting impact on log-consuming industries, such as softwood lumber. Indeed, it has been Canada's refusal to allow free trade in timber harvesting rights and free trade in unprocessed logs that has made "free trade" in lumber between our two nations so problematic over the last few decades. A "high-standard, 21st century" trade agreement must address this significant continuing derogation from free trade in the forest sector as a whole.

Moreover, the Coalition would expect other TPP partners to have their own interests in disciplining Canada's export restrictions on logs. New Zealand is one of the world's largest exporters of softwood logs and exports a much higher percentage of its softwood timber harvest in log form than does Canada. Japan is a major consumer of both softwood logs and softwood lumber from Canada. Therefore, the United States should not expect to be alone in pressing this issue with Canada during the TPP negotiations.

2. <u>The Trade Laws Should Apply Fully to All TPP Partners, Including Normal Provisions for Judicial Review</u>

Existing U.S. free trade agreements also uniformly provide for the continued application of national antidumping and countervailing duty laws to imports from partner countries. However, the U.S.-Canada Free Trade Agreement, and subsequently NAFTA, provide for international dispute settlement panels to substitute for domestic judicial review of antidumping and countervailing duty determinations by national investigating authorities. NAFTA art. 1904. This "Chapter 19" dispute settlement process is unconstitutional as a matter of law, is based on outdated Canadian concerns that have long since been addressed elsewhere, and has proven unworkable in practice. A TPP agreement that includes Canada should put an end to this highly

problematic provision and provide for normal domestic judicial review of trade law actions with respect to all TPP members.

First, as the U.S. Department of Justice recognized even at the time the U.S.-Canada Free Trade Agreement was being approved, there are significant constiutional problems raised by empowering international dispute settlement panels to direct the actions of U.S. government agencies, by direct operation of U.S. law. These panels are appointed, in part, by foreign governments not subject to constitutional oversight or democratic accountability, and once appointed panel members cannot be removed, even for cause, without the consent of the foreign government. The U.S. Supreme Court recently concluded that a statute limiting Presidential removal authority (in a much less substantive fashion) over persons exercisig Executive Branch authority was unconstitutional, reasoning that "{t}he President cannot 'take Care that the Laws be faithfully executed' if he cannot oversee the faithfulness of the officers who execute them." Free Enterprise Fund v. Public Co. Accounting Oversight Bd., 130 S. Ct. 3138, 3147 (2010) (quoting U.S. Const., Art. II). Although the constitutionality of the Chapter 19 scheme has never been finally decided by the courts, strong constitutional doubts remain.

Further, whatever concerns Canada may have had about the sufficiency of U.S. judicial review of U.S. antidumping and countervailing duty determinations in the 1980s, such concerns are completely misplaced today. The Court of Appeals for the Federal Circuit has issued several major decisions in recent years overturning significant, longstanding U.S. agency practices in cases brought by Chinese respondents. E.g., GPX Int'l Tire Corp. v. United States, No. 2011-1107 (Fed. Cir. Dec. 19, 2011); Dorbest Ltd. v. United States, 604 F.3d 1363 (Fed. Cir. 2010). Canada cannot plausibly claim that it would be unable to protect its interests in a fair and impartial judicial proceeding in the United States in the absence of Chapter 19. Moreover, the

WTO now provides for binding international dispute settlement with respect to compliance with U.S. WTO obligations governing the application of antidumping and countervailing duties, as it did not when the U.S-Canada Free Trade Agreement and NAFTA were entered into. There is no longer any need, if there ever was one, to also provide for international dispute settlement to examine compliance with domestic law in this area.

Finally, the Chapter 19 system has produced many poor decisions that have failed to apply the proper standard of review and that make other severe legal errors, while providing no meaningful check on such improper decisions. The former chief judge of the Court of Appeals for the D.C. Circuit stated that an early Chapter 19 decision "may violate more principles of appellate review of agency action than any opinion by a reviewing body which I have ever read." In re Certain Softwood Lumber Products from Canada, ECC-94-1904-01USA, Aug. 3, 1994, dissenting op. of Wilkey, J., at 41. More recently, at least two Chapter 19 panels have expressly refused to follow binding Federal Circuit precedent in the past few years. In re Stainless Steel Sheet and Strip in Coils from Mexico, No. USA-MEX-2007-1904-01, Apr. 14, 2010, at 20-24; In re Carbon and Certain Alloy Steel Wire Rod from Canada, No. USA-CDA-2006-1904-04, Nov. 28, 2007, at 12-30.

In sum, Chapter 19 is a failed experiment, any possible rationale for which has long since disappeared. The TPP negotiations would be an excellent opportunity to terminate this unfortunate project and bring U.S. unfair trade law as it pertains to Canada (and Mexico) into harmony with that for other TPP members.

3. Canadian Provincial Timber Sale Programs Should Be Covered by Any TPP Disciplines on State-Owned Enterprises

Press reports and the public statements of U.S. trade officials have highlighted the importance of disciplines on state-owned enterprises (SOEs) to the TPP negotiations. Canada's provincial governments, either directly through ministries of natural resources or through intermediary agencies or corporations, intervene directly into timber markets by selling Crown timber to softwood lumber producers and other forest products industries. As noted above, the large majority (between 80 and 99 percent) of the fiber supply used by softwood lumber producers in at least six Canadian provinces is derived from government-owned forests, and these provinces in turn account for a similarly large majority of Canada's softwood lumber production and exports. That these government-owned forests are not managed on a commercial basis, but rather are used to promote domestic industry at the expense of non-Canadian competitors, is at the heart of the ongoing softwood lumber dispute. The Coalition understands that this is exactly the type of trade-distorting practice that has elicited the desire to impose disciplines on SOEs in the TPP negotiations. Thus, Canadian timber-selling entities should be subject to any such disciplines that may be included in a TPP agreement.

As Secretary of State Clinton recently stated in her speech to the Economic Club of New York:

> To make the most of open markets, however, we have to make sure that all companies play by the same rules, whether their owners sit in corporate boardrooms or government ministries. Now, let's just be very clear here, too often, national favorites enjoy preferential access to government resources and special protection from competition in their markets. That gives these companies, whether they are wholly owned or partially owned by a government, an unfair advantage and harms foreign competitors and local entrepreneurs alike. We are working to include a chapter on state-owned enterprises in the Trans-Pacific Partnership and to finalize new OECD guidelines. Our premise is simple; the

> rules must apply equally to all companies. We call this commonsense principle competitive neutrality, and we promote it all over the world.
>
> … Governments are entering markets directly through their cash reserves, natural resources, and businesses they own and control. And they are shaping these markets not just for profit, but to build and exercise power on behalf of the state.
>
> …
>
> The way states deploy their cash, companies, and natural resources, especially in global markets, is of critical concern to us, and I hope it will be also to you. We need, therefore, to develop international rules and norms that set the boundaries, police bad behavior, and require transparency so that state-owned entities are clear about their intentions and their actions.

Speech of Secretary Hillary Rodham Clinton at the Economic Club of New York, Oct. 14, 2011, at 16-18.

It is undeniable that Canada's provinces, when they sell timber, are deploying their natural resources to promote the interests of the government rather than on a purely commercial basis. Timber is sold at prices and in quantities that are generally determined by administrative measures rather than market forces. Once sold, the timber must be processed into lumber or another end product in the province (or, in the case of Ontario, within Canada). Foreign companies, such as U.S. lumber mills operating within commercial distances of the U.S.-Canadian border, cannot purchase provincial timber at any price. The prices charged to domestic producers are demonstrably below market levels, and the widespread availability of cheap, subsidized timber depresses the prices that private Canadian timberland owners, who sell timber in competition with the much larger public sector, can achieve for their timber. As the Canadian lumber industry is highly dependent on the U.S. market, the effect of these government timber sales is to depress U.S. timberland values and to injure competing U.S. producers that does not have access to a subsidized fiber supply. These are exactly the types of policies that Secretary Clinton rightly decried, and to which the TPP SOE chapter is addressed.

Canada's own report to the ongoing OECD project on SOEs indicates that Canada would agree that provincial timber programs fall within the definition of an SOE. According to Canada, three criteria should be used to determine whether an entity belongs to the universe of SOEs: whether the entity is an "institutional unit," whether it is "controlled by the government," and whether it is a "non-market or market producer of goods and services." The Size and Composition of the SOE Sector in OECD Countries (OECD Corporate Governance Working Paper No. 5, Aug. 2011), at 83. Although the details vary from province to province, Crown timber sales are generally handled by an identifiable unit of a government ministry, autonomous government agency, or publicly owned Crown corporation. These are clearly "institutional units" that are "controlled by the government." Further, they provide a good – standing timber – that has commercial value, that is sold in competition with private entities in Canada and globally, and that profoundly affects the commercial viability of processing industries both in Canada and globally. Accordingly, the application of meaningful disciplines on SOEs to Canada's provincial public timber sales programs should be an important goal of the TPP negotiation with respect to Canada.

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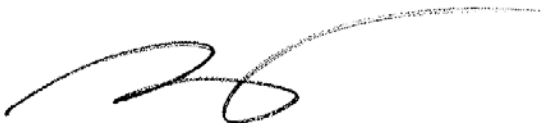
The Coalition would be pleased to provide USTR with additional information about all of these issues if Canada does fully join the TPP negotiations.

Please do not hesitate to contact any of the undersigned if you have any questions about this submission.

Respectfully,



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