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LAWYERS ON LUMBER: WERE THEY WORTH IT?

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Lawyers on Lumber: Were they Worth It?

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Throughout the nearly three-decade *Softwood Lumber* dispute between Canada and the United States, Canadians have complained about lawyers and their fees. The then Liberal Industry Minister, David Emerson, said in September 2005:

> ''Lawyers may be happy with ongoing disputes such as lumber, but I'm not sure that as policy makers and business people we should be happy to squander resources by going around and around on the same issues.''

In early 2006, after a series of Canadian legal victories already achieved when Emerson made his complaint, John Allan of the British Columbia Lumber Trade Council said, on the one hand, ''Yes, I do think it's worth it,'' but on the other hand, ''Legal fees are a dead weight loss. It's a non-productive expenditure.'' Duncan Kerr of Western Forest Products told a National Public Radio audience in May 2008, ''Protracted legal battles really don't benefit anybody other than the lawyers.'' These articulated sentiments echoed comments by government officials and private interests expressed often, sometimes publicly and often privately, all across Canada.

Canadians, certainly more than Americans, have an aversion to lawyers. Canada is inherently a less litigious society, in significant part because it is less adversarial. Americans promote values of competition more than co-operation, of individual more than collective rights. Those American values encourage dependence more on a rule of law than on negotiation, and on a need for lawyers as advocates and champions.

Trade disputes with the United States typically arise in the United States according to American rules and values. Canadians can accept to play by the American rules, or lose access to the US market. The very creation of a Free Trade Agreement with the United States, precursor to NAFTA, was in response to a Royal Commission Report (the Royal Commission on the Economic Union and Development Prospects for Canada—the MacDonald Commission) concluding that access to the US market was a *sine qua non* of Canada's future.

The *Softwood Lumber* dispute has been the greatest of all trade disputes between Canada and the United States, by whatever measure: the scale of the trade by value, volume and number of workers affected; the duration of the dispute, its legal complexity and multiple forums; its political and diplomatic engagements; the number of actors; the number of lawyers; and the legal expense. There has long been speculation about the aggregate costs of legal representation in the *Softwood Lumber* wars. Likely, Canadian federal and provincial governments, and Canadian industry, spent collectively something more than $100 million in legal fees on the episode (known as *Lumber IV)* that began on April 2, 2001, before the Softwood Lumber Agreement was entered in October 2006. A lingering question is whether, as John Allan put it, it was worth it.

The question has at least two meanings. The first is whether the value of what the lawyers accomplished outweighed the costs of legal representation. The second is whether Canada might have negotiated something sooner, and therefore been spared the cost of the protracted legal battle. Considering what Canadians accepted in the end, this question is powerful and disturbing, but it can be examined only in light of what Canadians said they would and would not accept during the previous four years of negotiations. The new Government of Canada, Stephen Harper's Conservatives, abandoned virtually every element of what Canadians had thought essential for a deal during prior negotiations.

The choice

The US Coalition for Fair Lumber Imports Executive Committee (the Coalition) petitioned the US Department of Commerce (Commerce) and the US International Trade Commission (ITC) in April 2001 for the imposition of countervailing and antidumping duties on imports of Canadian softwood lumber. Canadians—government and industry—-could have answered the petitions, or not. Electing to answer would require the appointment of legal counsel because of limitations on the right to

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appear before federal agencies and courts, and access to confidential information essential for responses.

The appointment of multiple counsel would reflect the distinct interests of different parties. Each provincial government, and the federal government, would want their own counsel, and for purposes of answering agency questionnaires about subsidies that each Canadian government allegedly was providing the softwood lumber industry, would need them. The anti-dumping petition led to the naming by Commerce of six Canadian companies as ''mandatory respondents''; each would require counsel were it to decide to defend itself. Some companies seeking their own anti-dumping or countervailing duty rates, believing they could obtain individual rates lower than the average country-wide rates, would also require their own counsel. And industry in each province, wary about the support of provincial and federal governments, would require their own counsel through their trade associations. Government and industry interests often are coincidental, but rarely identical.[1]

The US industry, then, effectively forced Canadians to hire lawyers by filing petitions full of allegations that would have led, necessarily and by law, to onerous import duties. The principal alternative to hiring lawyers, under US law, would have been for the petitioners' allegations to be taken as true, and for duties to have been imposed based entirely on the allegations. A second possibility would have been to negotiate immediately a settlement, but the inevitable basis of negotiation would have been the allegations and the Coalition would have had no incentive to compromise on them.

Consequences of the choice

The investigations

Investigations, administrative reviews and most litigation ended on October 12, 2006. Had Canadians not responded to the allegations of April 2, 2001 by hiring counsel, entering appearances before the two US agencies and responding to voluminous informational demands (including multiple questionnaires, on-site verifications—audits conducted by Commerce officials all across Canada over the course of several months—briefing and participation in public hearings), they would have paid $26.96 billion in duties, based on the allegations in the petitions, from the beginning until the end five years later.[2] This total is derived from the total value of imports for each and every month, beginning in August 2001, when deposits were first collected, and ending in October 2006.

This number, nearly $27 billion, is based on actual shipments during the period in question and application of the anti-dumping rates in Commerce's notice initiating the investigation and the countervailing duty rate alleged in the petition. Over the course of the five years, legal actions brought the rates down. It is possible, therefore, that had the rates remained this high all the time, shipments would have fallen, and with reduced shipments there would have been reduced duties. However, Canadian industry would then have been losing sales. For analytical purposes, holding the rates constant and applying actual sales seems the most reasonable way to extrapolate the consequences of non-response to the petitions.

This scenario might be considered in some way nevertheless unrealistic because one might suppose Canadians would have negotiated a compromise. However, there is no basis for suggesting that Canadians could have negotiated anything better than the allegations had they not defended themselves. In the previous *Softwood Lumber* wars, the Coalition had alleged only subsidies and had gravitated each time toward a 15 per cent *ad valorem* countervailing duty margin. The calculation was based on Canadian benchmarks. This time, for the first time, the Coalition persuaded Commerce to use cross-border benchmarks, comparing Canadian prices directly with US prices. This position eventually

1. US government spokesmen frequently said they acted entirely on behalf of the Coalition. No Canadian government, federal or provincial, ever made a similar remark about Canadian industry.

2. Shipments from the Atlantic Provinces were included in the petitions for both dumping and countervailing duties, but as the cases progressed they were excluded from the countervailing duties. Some 30 companies also gained individual exclusions. Collectively, the excluded companies and the Atlantic Provinces may have represented on average over the course of the litigation about 6% of all Canadian shipments. Precise data on the exclusions, however, are not available, and there are some statistical anomalies that, because of the scale of the numbers here, do not make a material difference but do require treatment of the data as approximate. Harmonized Tariff System numbers, for example, do not match perfectly the scope of the orders, making the customs data less than entirely consistent. Monthly data are imperfect because the anti-dumping and countervailing duty orders commenced in mid-month and ended mid-month. Consequently, the savings from legal assistance for phases following the investigations may be overstated by about 5% (the Atlantic Provinces' shipments, and the shipments of excluded companies, remained subject to dumping duties throughout). At the end of the first administrative review, however, where the reductions in estimated duties were attributable almost entirely to the dumping case, the impact of the exclusions was negligible. The largest change in the Second Review was a reduction in duties owed for alleged subsidies because of the legal victories altering Commerce's benchmarks, which would make the impact of the exclusions from the countervailing duties more notable, but still no more than about 5%.

was struck down in the legal proceedings as contrary to US law and WTO obligations, but the Coalition would not have compromised about it in the beginning, or for several years, and it guaranteed the calculation of a subsidy much greater than had been calculated in the previous cases.

This time, too, dumping allegations were added. Dumping and subsidy allegations combined to produce an *ad valorem* margin of more than 89 per cent, compared with the 15 per cent in the past. There was no reason for the Coalition to settle for anything less than this calculation had the Canadians not put up a legal defence. Hence the first consequence of the choice, to hire lawyers and defend against the allegations, was to complete the investigation phase of the affair, approximately 12 months later. At that point, as a result of the investigative proceedings, the combined dumping and subsidy margins were driven down to 27 per cent. Had those rates remained in place for five years, the Canadians would have owed $8.3 billion. Hence the Canadians saved, by virtue of the legal defence before the Department of Commerce, $18.6 billion.

The Canadians chose to defend themselves against the dumping and subsidies allegations not only before Commerce, but also before the International Trade Commission (ITC). In the American system, Commerce decides whether governments are subsidising industry and whether companies are selling products into the United States at less than fair value, or dumping. Commerce also decides by how much, and therefore what the ''margin'' of difference is between a fair market price and a dumped or subsidised price. Duties are set to make up the difference. Yet, at the investigation phase, Commerce does not decide alone how much in duties must be paid. The ITC also makes decisions that impact the duty rates.

The ITC decides whether the US industry is suffering current material injury or is threatened with material injury. When the ITC determines that the US industry is suffering current material injury, the anti-dumping and countervailing duties are imposed retroactively as of the dates of Commerce's preliminary determinations. By contrast, when the ITC determines that the US industry is only threatened, the duties are imposed going forward from the date of the anti-dumping and CVD orders. Lawyers representing Canadian interests contested the allegations of current injury and prevailed. Had they not, Canadian companies would have paid an additional $1 billion in duties. Hence legal defences provided by lawyers saved Canadian industry, through the investigation phases only, $18.6 billion at Commerce, and an additional $1 billion at the ITC.

First Administrative Review

US trade law is prospective, which means it is designed to persuade exporters of goods to the United States to alter their conduct and not punish them for past misdeeds. When no defence is offered against allegations, the rates alleged are applied, but the rates at the end of the investigation are not definitive because they are based on information dating prior to the allegations. In theory, exporters (and their American importers) were not necessarily aware that they were dumping or benefiting from illegal subsidies. If, while the investigations were going on, they rid themselves of subsidies and adjusted their prices so they would not be dumping, they would not owe duties.

Deposits on estimated duties are collected until the completion of a first ''administrative review'' that covers the year following the imposition of the anti-dumping and CVD orders. Should no subsidies or dumping be found during that period, all deposits are returned. When dumping or subsidies are still found, but at lower rates, the difference between the deposits based on the information gathered during the investigation, which pre-dated the allegations, and the information gathered during the review, which followed the orders, reduces the amount owed and the difference is refunded. The investigation determines whether an order will be imposed to collect duty deposits and to continue through at least three more years of administrative reviews, but no duties are in fact collected until the conclusion of the First Administrative Review, based on rates found during the administrative review, not the rates found in the investigation.

This prospective system means that the First Administrative Review is as important as the investigation. Even though the investigation may have produced an order, it does not necessarily yield duties to be paid and therefore money lost to the exporting or importing parties. The Canadians had a choice, again, following the investigations and the issuance of orders. They could have stopped engaging and paying lawyers and permitted Commerce to conduct its reviews of the dumping and countervailing duty orders without comment or opposition. Or they could challenge the orders and associated rates through counsel.

The Canadian parties in *Softwood Lumber* elected to participate in the First Administrative Review. Although the orders were not overturned in the administrative review, the anti-dumping rate fell from 8.43 per cent to 4.03 per cent, and the countervailing duty rate fell from 18.79 per cent to 17.18 per cent. The net consequence of the legal activity that reduced the rates was a saving to Canadian industry of another $1.6

billion. Meanwhile, appeals of the investigation results were now underway before NAFTA panels, and by the Government of Canada before panels of the WTO.

Second Administrative Review

In the previous *Softwood Lumber* war (1991–94), which was the first subjected to adjudication under the Free Trade Agreement between Canada and the United States (NAFTA's predecessor and the same Chapter 19 dispute resolution system), all proceedings were concluded prior to a Second Administrative Review. The United States had lost before a NAFTA panel and had filed an extraordinary challenge. An Extraordinary Challenge Committee issued a decision in favour of Canada before a Second Administrative Review of the countervailing duty order could have gotten underway. Not this time, however, mostly because the United States successfully stalled proceedings.

Whereas cash deposits from an investigation cannot be converted into duties without the results of a First Administrative Review, the deposits made during a First Administrative Review (and all annual reviews thereafter) will be converted into duties unless the results of the administrative review are appealed, whether to the US Court of International Trade, or to a NAFTA panel. The Canadians had to decide, then, whether to challenge through formal appeal the results of the First Administrative Review in order to suspend the liquidation of entries and avoid the conversion of their cash deposits into irretrievable duties. They also had to decide whether to participate in the Second Administrative Review. Both decisions implied hiring lawyers.

The Canadian parties chose to do both, engaging counsel both for the appeals and for the administrative review. The results of the Second Administrative Review, enhanced significantly by results emerging from the legal appeals, reduced the anti-dumping rate from 4.03 per cent to 2.11 per cent, and the countervailing duty rate from 17.18 per cent to 8.7 per cent. Legal representation through the Second Administrative Review thus saved Canadian parties an additional $2.3 billion. Had the rates not come down as a result of the appeals (which changed the way Commerce measured the subsidies, in particular), and the full participation in the administrative review, Canadian parties would have paid in duties another $2.3 billion.

At this point the appeals had become very important. In the Second Administrative Review, Commerce was no longer able to use a cross-border benchmark—US prices—to determine whether and by how much Canadian governments were subsidising the production of softwood lumber. The anti-dumping calculations were also narrowing and the rates were falling as a consequence. By the end of the Second Administrative Review, the combined duty rate that had begun after the investigation at 27.22 per cent had fallen to 10.81 per cent.

Appeals

The Canadians had to appeal the results of the First Administrative Review in order to prevent cash deposits from conversion into irretrievable duties pending the outcome of legal challenges. They had to appeal the investigation results, however, in order to prevent agency determinations from becoming definitive. Overturning the ITC's Final Affirmative Determination would mean unravelling both anti-dumping and countervailing duty orders; overturning the Department of Commerce Final Affirmative Determinations would mean disabling further administrative reviews and preventing the conversion of any deposits into permanent duties. Decisions not to engage counsel and appeal the final determinations would have been decisions conceding both subsidies and dumping, challenging in the administrative reviews only the degree and consequent amount of duties to be paid.

When the Government of Canada negotiated a 15 per cent export tax as a virtually permanent feature, in down markets, of sales of Canadian softwood lumber into the United States, Canadian industry was paying in duty deposits only 10.81 per cent as a result of the legal accomplishments of the ''non-productive expenditure''. They had saved $23.6 billion by, as Minister Emerson would have had it, ''squander[ing] resources'', compared to what they would have paid in duties without legal representation. Minister Emerson was, after all, a minister in the previous Liberal Government that had not been able to negotiate a settlement.

The new rate negotiated by Canada would be applied with no recourse. Canadians would pay the export tax to the Government of Canada with no prospect of ever getting any of it back. By contrast, deposits they made at the 10.81 per cent rate into the US Treasury, as well as earlier deposits made under higher rates, were accumulating interest and could be returned in total, or at least in significant part, especially as the rates had fallen from more than 27 per cent to less than 11.

The legal appeals, particularly of the final determinations, were not aimed merely at reducing amounts owed. They were designed to prove that nothing was owed.

The appeals proceeded on three tracks. The appeals of the countervailing duty order focused first on the cross-border benchmark, and then

on the application of a fair and legally defensible benchmark for the comparison of Canadian prices. The legal principle, ''adequate remuneration'', required a determination of whether Canadian lumber companies paid ''enough'' for stumpage—the right to cut standing timber on public lands—where ''enough'' meant no less than they would have paid had they purchased the same right on private lands. In March of 2006, a NAFTA binational panel concluded that, once Commerce applied a fair and defensible benchmark, it found adequate remuneration everywhere in Canada. There was no subsidy, and the countervailing duty rate fell to zero.

The second track concerned the anti-dumping rate. It already had fallen to 2.11 per cent, but there remained a key legal dispute over a technique called ''zeroing'' that Commerce used to inflate dumping margins. The WTO Appellate Body had found zeroing contrary to WTO obligations; a NAFTA binational panel had found it contrary to US law. Without zeroing, the anti-dumping rates also would have fallen to nil, but the second track was not complete when Canada negotiated the Softwood Lumber Agreement. The third track concerned the finding that sales of subsidised and dumped Canadian softwood lumber threatened injury to the US lumber industry. A finding of injury or threat of injury is a prerequisite for imposing any trade remedy. A NAFTA binational panel had concluded in August 2004, and an Extraordinary Challenge Committee had confirmed a year later, that the ITC had not found injury or threat of injury in accordance with US law. The United States, however, had resisted these decisions, creating a novel legal interpretation arising from nearly simultaneous actions in NAFTA and at the WTO. It was at this juncture that Minister Emerson had ridiculed the legal process.

The Canadians, recognising the threat the US resistance posed for the future of NAFTA dispute resolution, and for completion of the *Softwood Lumber* war, took their winning decision from NAFTA to the US Court of International Trade for final confirmation and implementation. Even as the dispute resolution system enshrined in NAFTA's Chapter 19 was designed to liberate Canadians from adjudicating trade disputes in US courts, Canadians understood that the United States would respect Chapter 19 decisions, in the end, only with the imprimatur of those very courts. In July 2006 they won a unanimous but incomplete decision of a three-judge panel, which was completed and finalised on October 13, one day after the Softwood Lumber Agreement was proclaimed. The legal results, however, were final and irrefutable: there was no subsidy; there was no injury or threat of injury; there was a minuscule and diminishing dumping margin that could not be applied because of the injury result.

With application of all of the legal decisions, no cash deposits would have been converted into duties and all the cash deposits, with interest, would have been returned. At the end, prior to the final court decisions and prior to entry into force of the Softwood Lumber Agreement, the Canadians had on deposit approximately $5.2 billion in estimated duty deposits and accumulated interest, not the $26.9 billion (plus interest) that would have been collected by the United States had there been no legal defence from the beginning, or any of the other decidedly higher sums that would have been collected at various intervals but for the continuing legal representation. In all, lawyers had saved the Canadians $26.9 billion, or a net gain after approximate legal fees of $100 million, of $26.8 billion. At the point when the Government of Canada wrote off the legal process, one day before it was complete, $23.6 billion (plus interest due) had been saved.

The negotiated alternative

Throughout the legal proceedings the Government of Canada had been seeking a negotiated end to the *Softwood Lumber* war. The Canadians were, from the first, prepared to compromise. They were prepared to accept trade restrictions, however unwarranted or legally unjustified they may have been, provided they were temporary and the criteria and timetable for ending them were unambiguous. They were prepared to leave cash on the table, provided the amount was nominally capped and not calculated as a percentage of anything.

The United States refused to meet these few Canadian requirements. The United States would not relinquish any authority over ''exits'' from restricted trade. Instead, the United States wanted Commerce, and only Commerce, to decide whether the Canadians would have satisfied American demands for reform of Canadian forestry practices, which the Canadians understood to mean that they would never be liberated from managed trade. Those reforms, moreover, were to be governed principally by privatisation of Canada's forests (whether formally through ownership or unofficially through auctions), an intrusion on sovereignty most Canadians rejected. And the United States rejected any specific time horizon for ending the imposition of trade restrictions on Canada.

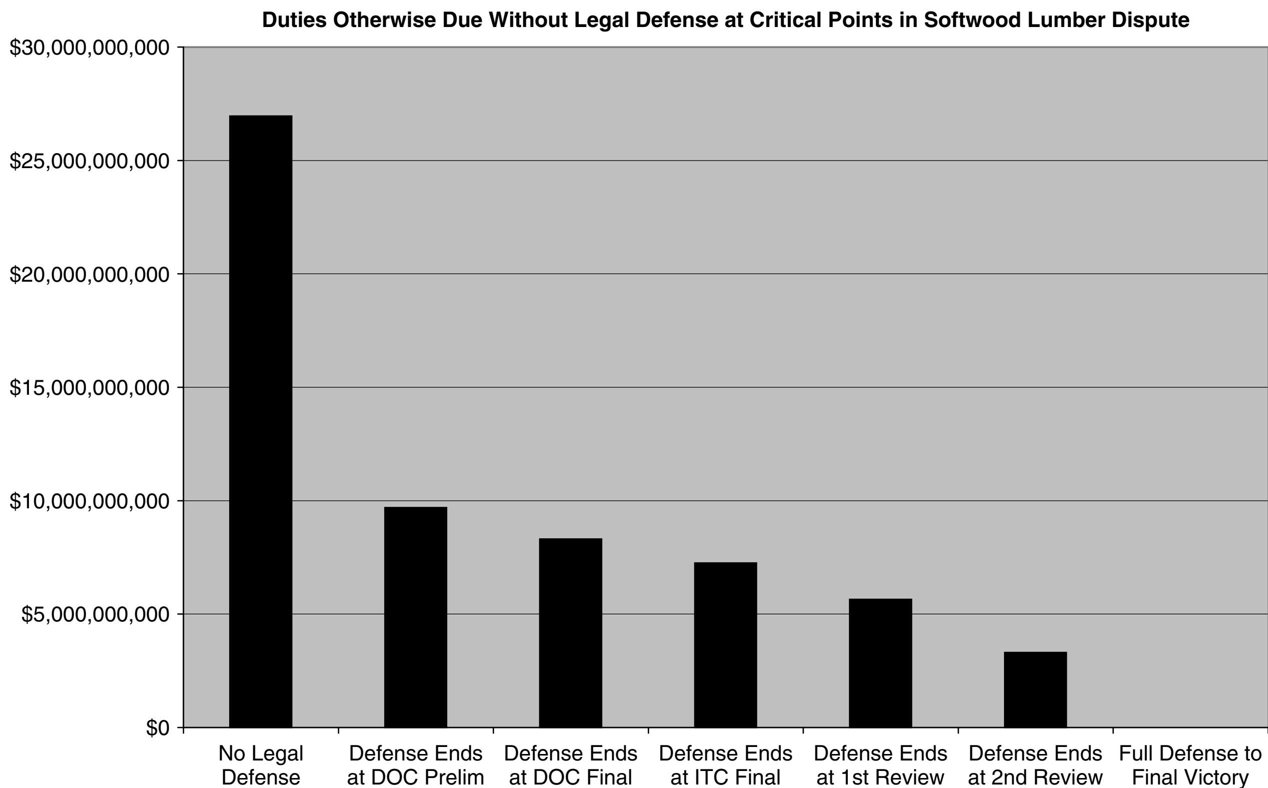
The US Coalition, pursuant to the so-called Byrd Amendment, expected to receive all of the $5.2 billion that had been accumulating in duty deposits, and at no time during any negotiations did the Coalition ever agree to less than 40 per

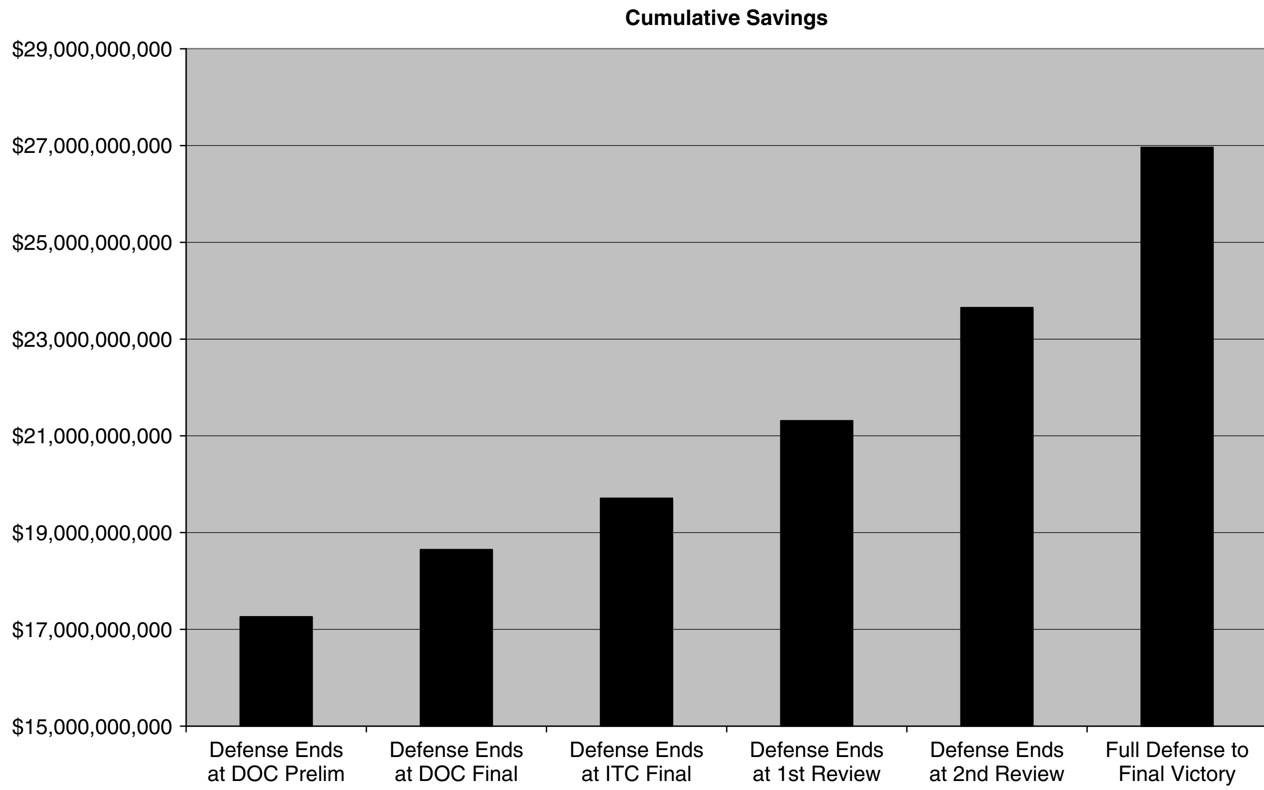
cent. The final settlement, in which Canadian industry gave up 20 per cent but the Coalition received only half that sum, or $500 million, was possible only because the Canadians won a legal victory in US courts establishing that the Byrd Amendment did not apply to Canadian merchandise and the Coalition was not entitled, by law, to any money at all, even if it were to enjoy a complete legal victory. Prior to that decision, in April 2006, there was no negotiated settlement possible as to the distribution of Canadian money held in the US Treasury because the Coalition was not prepared to settle for less than $2 billion.

The Government of Canada settled for effectively permanent trade restrictions (nine years) without exits of any kind. It gave the United States rights to oversee any and all changes in Canadian forest practices throughout Canada. It took a percentage, not a nominal sum, of Canadian industry money and distributed it as it pleased. The Government of Canada neither demanded nor got a single one of the requirements for settlement for which previous governments, and Canadian industry, had held out.

More likely than not, the deal the Government of Canada ''won'' in 2006 could have been had sooner: permanent trade restrictions on US terms, exceeding the restrictions applied by law; no exits; US oversight of Canadian policy and practice; $1 billion in Canadian money otherwise due, by law, back to the Canadians. It would be easy to argue, consequently, that the savings reported here would not have been necessary. But no Canadian government, other than the Harper Government, would have negotiated such a deal while the unfolding legal process was reducing the burden of the trade restrictions and promising the conclusion that, in fact, was achieved, vindicating Canadian exports and Canada's provincial forestry practices.

The United States would have taken the deal it got at most any time, as the Coalition would have. For at least 18 months prior to the deal, back-channel communications revealed a growing anxiety on the part of the Coalition to make a deal, and American officials stated repeatedly that the *Softwood Lumber* war could conclude only through a deal, because the United States, and the Coalition, knew they were losing and would continue to lose the legal fight. The final question, then, was whether the Canadians would capitulate, but the Coalition was convinced, and turned out to be right, that the question was not ''whether'' but ''when''. Nevertheless, when Canada did capitulate, its industry had been saved more than $23.6 billion through the ''unproductive'' efforts of Canada's lawyers in the United States.




Cumulative Savings
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Defense Ends at DOC Prelim
Defense Ends at DOC Final
Defense Ends at ITC Final
Defense Ends at 1st Review
Defense Ends at 2nd Review
Full Defense to Final Victory