PERSPECTIVES ON INTERNATIONAL TRADE AND THE CANADA-UNITED STATES SOFTWOOD LUMBER DISPUTE

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When I was a boy, trade was simple. No nematodes, no countervailing duties! I would give you one Syl Apps card for one Gordie Howe or two Eddie Shack's. In addition to noting how long ago it was that I was a boy, you will also notice there was no mention of where the money to buy the cards came from (if it was an allowance, that clearly would constitute a subsidy) or that my parents permitted more gum chewing than did my trading partner's (which would indicate a benefit that was not universally available and, therefore, an unfair advantage).

But with the passage of time, a lot has changed: I can't pronounce the names of most of the players on the hockey cards, the value of each card has been determined by some anonymous international financier in Zurich and transmitted by overnight computer networks to every nine-year-old in the known world. But most importantly, I now only chew gum that has medicinal properties designed to keep me regular.

And trading is indeed no longer simple and is now governed by a maze of international protocols, agreements and often disagreements.

In the time I have during this symposium, I will try to provide you a short history of how the rules of international trade which govern the Canadian forest industry came to be and discuss the interpretation of those rules in the Canada-United States softwood lumber dispute.

Unfettered market access is critical to the Canadian forest industry. To a large extent, our success depends on market access and our corresponding ability to trade freely around the world. All the productivity and efficiency our companies can muster isn't going to do much good if we don't have access to current and potential markets.

Canada's role as a major player in world markets stems from its presence and participation in the period of reconstruction which followed the Second World War. While some dreamt of a post-war international trade organization, it did not come to pass. In its place, a fundamental set of principles to guide trading nations were drafted. Those principles are embodied in what is known as the General Agreement on Tariffs and Trade, or GATT. GATT is essentially an international trading system for importing and exporting goods. It is based on two key concepts -- multi-lateralism and non-discrimination.

By multi-lateralism, I mean a set of rules to which a large number of countries subscribe.
And by non-discrimination, I mean a set of rules which obliges each signatory to the agreement to

treat every other signatory equally. The GATT marked its 45th anniversary just last month. By and large, GATT has served the interests of international trading nations very well. The volume of world trade has grown tenfold since it's inception.

Not only have the principles of multi-lateralism and non-discrimination been absorbed into the commercial regulations of signatory nations, but the GATT has also become the central institution for the management of international trade issues, a forum for trade negotiations and a mechanism for the settlement of trade disputes. Those are GATT's strengths.

Among its weaknesses are a shortage of resources and powers compared to other international organizations such as the World Bank, the difficulty of its amendment and its susceptibility to challenges of legitimacy when trade issues and disputes turn political.

In addition, several noteworthy developments have changed the nature of international trade and commerce over the last 45 years. The international economy we know today is dominated by three major blocs -- the United States, the European Community and Japan. These developments have caused Canada and others to pursue additional trading options in addition to those afforded under the GATT.

The most significant of these for our country have been the Canada-United States Free Trade Agreement and the North American Free Trade Agreement. Canadian trade experts such as Dr. Sylvia Ostry observe that GATT has found it increasingly difficult to adapt to these changes and that as a result, the multilateral trading system that has emerged since the late 1940's is under stress. The trend towards regional trading blocs and to more frequent unilateral actions by powerful countries is leading to the establishment of a new world trade order. I do not have the same insight into international trade that Dr. Ostry, who served as Canada's former Ambassador for Multilateral Trade Negotiations, does. But I do feel strongly that regardless of the current stress GATT may be under, the values realized from many of the GATT rules can and must endure.

These rules are so deeply embedded in national laws that great webs of commercial relations have been woven around them. The sheer number and the value of the thousands of international transactions that take place daily means that many people in the world of trade and commerce -- knowingly or unknowingly -- have a stake in the GATT system.

The system's rules also form the basis for regional agreements nations are making parallel to GATT. The Canada-United States Free Trade Agreement, for example, is clearly based on GATT rules and concepts. Furthermore, to participate in the process of a GATT dispute settlement is to appreciate the significance which parties attach to their rights and obligations and the seriousness with which they act to protect them.

My current views on international trade have been somewhat shaped by my experiences with a dispute over softwood lumber that has plagued Canada-United States trade relations for more than 10 years. It is Canada's great curse and its great blessing to be situated next to what is still the world's most powerful economy.

My advice to other Canadians who have the fortune -- or misfortune -- of being connected with a trade dispute involving the United States is to keep three guiding principles in mind:

1. "Congress may not be responsible, but it certainly is responsive".
2. "Foreigners don't vote".
3. "Do as we say, not as we do."

I will discuss each of them in turn.

1. "Congress may not be responsible, but it certainly is responsive."

I can't claim credit for this old Washington saying. But I certainly can vouch for its accuracy. The United States is a dynamic and open democracy. It is also a democracy that is uniquely sensitive to special interest groups. As H.L. Mencken once said: "If a politician found he had cannibals among his constituents, he would promise them missionaries for dinner." Today, one of those special interest groups is the U.S. Coalition for Fair Lumber Imports...and they want we Canadian lumber missionaries for dinner.

Back in October of 1982, the coalition filed a petition with the U.S. Department of Commerce alleging that Canada was subsidizing softwood lumber by charging low stumpage fees. Parties to the dispute worked their way through the full U.S. "quasi-judicial" process which entails an investigation, subsidy determinations by the Department of Commerce and injury determinations by the U.S. International Trade Commission. At the end of it all, in May, 1983, the Commerce Department determined that Canadian softwood lumber exports were not subsidized by pricing policies and refused the request for a countervailing duty. The decision was 10 per cent "quasi" and 90 per cent "judicial". Canadians fought the battle believing that reasonable arguments articulated by responsible people would prevail.

They were right in Round One.

The U.S. lumber industry, however, refused to accept Round One as the final resolution of the dispute. They began to work Congress. The U.S. industry's supporters in Congress responded by tabling various bills which, if enacted, would have limited Canadian lumber imports into the U.S. or changed the law the Commerce Department applied in 1983. The period 1984-1986 saw increasing protectionism in U.S. attitudes and enormous growth in Congressional support for the U.S. Coalition even though there had been no substantive changes to Canadian timber pricing programs since the Round One decision.

What had changed was the placement of the goal posts on the political playing field.

Free trade negotiations between Canada and the United States were about to be launched. President Reagan needed the authority of Congress to proceed but the signals he was getting were not very encouraging.

In a straw vote taken in the Senate Finance Committee, 11 out of 20 members indicated that, if they were asked to vote on whether the President should be given authority to commence free trade negotiations with Canada, they would vote no.

One of those committee members was Senator Bob Packwood. What Senator Packwood wanted was a commitment from President Reagan that something would be done about softwood lumber. The President and his then Trade Representative, Clayton Yuetter, made such a commitment. In rather prophetic and chilling words, Clayton Yeutter wrote to Senator Packwood and scrawled on the bottom of his letter, "Bob, we'll 'fix' lumber." And fix it they did. We Canadians believed that since we'd won the case on its merits in 1983, we would win it on its merits in 1986.

In that year, however, the complex trade law process became 90 per cent "quasi" and only 10 per cent "judicial". Let me explain further. As in 1983, the preliminary Round Two determination held that the U.S. lumber industry was being injured by Canadian imports. However, unlike 1983, the Department of Commerce accepted the Coalition argument that stumpage was a specific subsidy being granted to the softwood lumber industry.

Through a highly controversial calculation, the Department of Commerce issued a preliminary determination that provinces were not recovering their "costs" of granting stumpage to the industry. This "cost" was calculated to include an inherent value of trees. The concept of inherent value was never really defined but its effect was to achieve a countervailing duty calculation acceptable to the Coalition for Fair Lumber Imports. At the risk of belabouring the point, I repeat: the only thing that had changed from 1983 to 1986 was the weight of the influence politics had on both the substance and interpretation of the law. Canada was facing a countervailing duty decision that would have sent $500 million a year to U.S. government coffers. Instead of waiting for the final determination and then appealing the result through the U.S. court system, our Canadian government decided, under provincial pressure, that it wanted the money kept in Canada. Accordingly, it entered into the infamous Memorandum of Understanding on Softwood Lumber.

The Memorandum of Understanding or MOU was certainly not the final settlement of the trade dispute as far as the Canadian industry was concerned. Indeed, from the time the MOU was signed, we began to work for its termination. In the short term, however, the MOU did buy peace, keep revenues in Canada and allow B.C. and Quebec to proceed with planned changes to their forest policies. Under the MOU, Canada imposed a 15 per cent export charge on lumber destined for the U.S. in place of a U.S. import tariff. Less than a year after the MOU was signed, the B.C. government replaced the 15 per cent export tax by imposing increased costs on the industry in the area of stumpage and silviculture. Perhaps even more significant than the higher cost structure the MOU inflicted on our industry, was the fact it effectively turned control of our forest policy over to our major competitors. Under the MOU, measures to replace the U.S. countervailing duty had to be approved by U.S. trade officials. Provinces were unable to make any changes to their timber pricing policies without entering extensive and aggravating consultations with the U.S. government. A small bureaucracy grew in the U.S. Commerce Department specifically to monitor the MOU's operation.

By 1991, the MOU had become an increasingly painful thorn in the side of the Canadian industry and provincial and federal governments. Canadian concerns about the MOU were raised many times by John Crosbie and Michael Wilson in bilateral consultations with U.S. Trade Representative Carla Hills. The reply was less than encouraging -- all the U.S. would say is that they were interested in quote, improving" the MOU. In the meantime, the U.S. Coalition for Fair Lumber Imports, knowing that termination of the MOU was a possibility, maintained a strong presence in Congress. The message to the elected representatives who were on-side was that the Coalition would not stand idly by should Canada decide to exercise the legal right to terminate the MOU. Canada did so decide on September 4, 1991.

And Congress responded.

Shortly after Canada gave the required 30-days notice of termination, 66 U.S. Senators signed a letter to the President demanding that a 15 per cent tax on softwood imports from Canada be imposed immediately. The U.S. government bowed to the pressure to take action in order to placate Congress and the U.S. lumber coalition. But rather than require the U.S. Coalition to file another countervailing duty case, it went ahead for the first time in history to file one on its own. What this did was effectively relieve the U.S. Coalition of the burden and cost of putting its case together. The Coalition consulted with the U.S. government in putting together the self-initiation documents. And it's a matter of public record that Coalition representatives had numerous meetings with the U.S. government, specifically the Department of Commerce, during the preparation and conduct of the investigation.

Following a strategy similar to that in the two previous countervailing duty cases, the U.S. Coalition's claim was that provincial stumpage practices constituted unfair subsidies. Unlike the two previous cases, however, the Coalition also argued that federal and provincial export restrictions on raw logs also act as subsidies.

What was Canada's response to all this? Well, the federal government immediately launched a GATT complaint. The GATT conciliation process was followed but to no avail. A GATT panel was then struck to receive submissions on the issue and to hear the parties' points of view.

The decision of the GATT panel is expected shortly. Should GATT rule that the U.S. actions were inconsistent with its obligations, the U.S. would be required to remove the existing countervailing duty.

And now, for the second principle.

2. "Foreigners Don't Vote"

The "Foreigners Don't Vote" principle is related to the first. Since foreigners do not vote, they do not factor into political calculations in the United States. Our problem in lumber is that we are not U.S. employers to any measurable degree. We manage our resource at home and export the products our employees produce.

In Round One, some major U.S. employers and associations identified with our cause. In Round Two, other domestic issues kept them out of the fray for the most part. In Round Three, many supported the Canadian case but regrettably, their excellent efforts were not enough to counter the strong political lobby of the U.S. Coalition.

That brings me to the third principle.

3. "Do As We Say, Don't Do As We Do"

The third principle is somewhat different from the first and second principles.

One of the most interesting and frustrating aspects of the lumber dispute has been the unwillingness of the United States government to recognize the inconsistency between how it has dealt with domestic political issues -- such as below-cost timber sales in its national forests and log export bans both federal and state -- while complaining about Canadian actions in the same areas.

In the 1980's, the U.S. was engaged in a vigorous debate about its national forests. Environmentalists and others attacked the U.S. Forest Service for, in their view, giving away timber. During the latter part of the decade, the U.S. Forest Service worked with the General Accounting Office of the U.S. government to devise a way to evaluate the economic and financial benefits flowing from those forests. The result was the Timber Sales Pricing Information Reporting System or TSPIRS. Using TSPIRS, the U.S. Forest Service sought to prove that when you look not only at actual stumpage payments but as well at income, local and state taxes, the U.S. national forest is actually doing rather well.

Canada decided to play the TSPIRS game too. This was done because the essence of the Department of Commerce negative finding against Canada in Round Two was that our provincial governments were not receiving an adequate return on their investment; in other words, their costs of administering the resource were exceeding their revenues. Not surprisingly, when TSPIRS was applied to Canada, it found that government forest revenues substantially exceed its costs of administering the resource. Yet, when this documentation was put before the United States Commerce Department, the importance of the "cost-to-government" test was dismissed.

The TSPIRS episode aptly illustrates the "do as we say, don't do as we do" principle. It seems to me totally inconsistent that, on the one hand, the United States struggled to deal with valuation of a timber resource owned by the government and then discounted its own "cost-to-government" test in 1992 after relying on it in 1986.

Similarly, why is it that Canadian log export bans are said to be a subsidy when the U.S. government has implemented similar bans on logs from federal lands and has authorized the states to do so as well?

"Do As We Say, Don't Do as We Do".

A strategy of playing fast and loose with trade rules has served the United States well so far in Round Three. Nevertheless, in Canada there is a strong expectation that since we did not win the case in the quasi-judicial process, we surely must win on appeals to dispute panels under the Canada-United States Free Trade Agreement. The panel decisions are due to be released in April and June of next year.

Based on the success experienced in previous cases considered by FTA dispute panels, the federal and provincial governments are optimistic Canada will be successful in having one or both of the subsidy and injury determinations reversed. Under United States trade law, a win on one of those two counts would be enough to have the case thrown out.

If, for some reason, the free trade agreement cannot deliver what Canadians see as justice, the Canadian government will be under tremendous pressure to terminate the agreement.

We do have some allies south of the border. American home builders, lumber wholesalers, building materials dealers and consumer groups are well aware of the cost of this action for them and are letting their Members of Congress and Senators know how they feel about it. They certainly deserve recognition and thanks. So do the American economists and forest industry experts who put on the record strong testimony that Canadian softwood lumber exports were not injuring the American market. It appears our crime is that we have done things differently from the U.S. and have been highly competitive along the way.

To be punished for that through protectionist trade action is not only an affront to our nation but to the spirit of the GATT which launched the era of free trade among nations in the first place. We firmly believe that a fair and apolitical consideration of the facts in this matter will result in a ruling in Canada's favour. I also believe that the global movement to greater trade that has contributed so much to prosperity over the past 45 years must not be allowed to founder on the shoals of political expediency and special interest group pressure.