

THE CANADA-U.S. SOFTWOOD LUMBER DISPUTE: AN INTERDEPENDENCE  
APPROACH

by

**Sharn Tyakoff**

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APPROVAL

Name: SHARN TYAKOFF

Degree: MASTERS OF ARTS

Title of thesis: THE CANADA-U.S. SOFTWOOD LUMBER DISPUTE: AN  
INTERDEPENDENCE APPROACH

Examining Committee:

Chairman: M. COVELL

\_\_\_\_\_  
Senior Supervisor  
T. Cohn

\_\_\_\_\_  
Second Supervisor  
L. Dobuzinskis

\_\_\_\_\_  
External Examiner  
D. Munton  
Department of Political Science  
University of British Columbia

Date Approved: March 17, 1988

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Author:

(signature)

Sharn Tyakoff

(name)

March 17, 1988

(date)

## ABSTRACT

This thesis is a study of the Canada-U.S. softwood lumber dispute and attempts to determine what factors influenced its outcome. The lumber issue is a significant problem in the bilateral relationship and is of particular importance to Canada given the increasing ability of American interest groups to obtain protection for their industries. Moreover, the subsidy allegations made in the lumber case could also be applied to other natural resources. In 1982-83 Canadian softwood lumber was the subject of an American countervailing duty investigation, which determined that subsidies to Canadian lumber producers were *de minimus*. This study uses the interdependence framework to determine what factors contributed to Canada's success in 1983, through an examination of the documents and reports of the lumber dispute. Although the primary focus of the study is the 1981-83 period, subsequent events are reviewed and related to the analysis of the earlier stage.

Robert O. Keohane and Joseph S. Nye have applied an interdependence framework ("complex interdependence") to the study of Canadian-American relations. It postulates that the outcome of conflict in the relationship is related to several factors, including the multiplicity of socio-economic and political connections between the states; a lack of hierarchy among issues; and the absence of force as a tool in settling disputes. This study reveals the importance of asymmetry of

attention and the role of heterogeneity versus homogeneity of interests in the dispute. The limitations of the interdependence approach as applied to the lumber case include a lack of attention to the validity of each side's case; the costs that the smaller power must incur to win; and the ongoing nature of conflict in the relationship. The lumber dispute shows that Canada does have resources which it can utilize in a trade dispute, but that Canada's chances of success are greatly diminished when the U.S. decides to devote more attention to a contentious issue.

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## TABLE OF CONTENTS

Approval .....	ii
Abstract .....	iii
Acknowledgements .....	v
List of Organizations .....	viii
I. Introduction .....	1
An Overview of the Softwood Lumber Dispute .....	7
Interdependence in Canada-U.S. Relations .....	11
II. Canadian-American Lumber Trade .....	18
The Structure of the Canadian Industry .....	21
The Structure of the United States Industry .....	24
The North American Softwood Lumber Market .....	29
The U.S. Countervail System .....	34
Interdependence in the North American Softwood Lumber Market .....	41
III. The Origins of Canadian Softwood Lumber Exports as a Trade Issue .....	44
The Timber Strategy Panel's Report .....	53
Senate Hearing .....	54
The Canadian Producers' Response .....	65
The ITC Section 332 Study .....	69
Organizing for the Countervail Action .....	72
Summary of the 1981-82 Period .....	79
IV. The Countervail Proceedings .....	83
The Petition .....	83
Canadian Response .....	92
ITC Preliminary Ruling .....	103

International Trade Administration's Investigation . . . .	104
An Evaluation of the Countervail Proceedings . . . . .	118
V. Conclusion . . . . .	127
The Relevance of this Study to the 1984-87 Period . . . . .	134
Canadian Response . . . . .	137
Sources Consulted . . . . .	147



## LIST OF ORGANIZATIONS

Canadian Forest Industries Council --- CFIC  
Canadian Softwood Lumber Committee --- CSLC  
Council of Forest Industries of B.C. --- COFI  
International Woodworkers of America --- IWA  
National Forest Products Association --- NFPA  
North American Wholesale Lumber Association --- NAWLA  
Northwest Independent Forest Manufacturers Association --- NIFM  
U.S. Coalition for Fair Lumber Imports --- CFLI  
U.S. Federal Trade Commission --- FTC  
U. S. International Trade Administration --- ITA  
U. S. International Trade Commission. --- ITC

# CHAPTER I

## INTRODUCTION

This thesis is a case study of a dispute over Canadian softwood lumber exports to the United States. In the early 1980s, softwood lumber producers in the U.S. and Canada experienced substantial declines in sales and revenue. In 1981, a small group of American producers filed a complaint against Canada with the U.S. Department of Commerce, requesting that countervailing duties be assessed on Canadian softwood lumber imports. These producers claimed that government subsidies were enabling Canadian firms to increase their market-share at the expense of the U.S. industry. After investigations of the petitioners' claims by the U.S. International Trade Commission (ITC) and the International Trade Administration (ITA), the U.S. Commerce Department decided against imposing countervailing duties. However, this decision did not mark the end of the dispute as another petition requesting countervailing duties was filed in 1986, and in 1987 Canada agreed to impose a fifteen percent export tax on softwood products destined for the American market.

Due to the ongoing nature of the softwood lumber dispute and because of restrictions in time and length, this thesis focuses primarily on the first stage of the dispute: the 1981-83 period. Nineteen eighty-three was selected as the cut-off date since the ITA's ruling on Canadian subsidies to the lumber industry was

issued in May of that year. Although detailed analysis of the second phase of the dispute is left for future studies, events during the 1984-1987 period will be briefly outlined and referred to on occasion, and the final chapter will include a discussion of the relevance of this analysis to the later period. It should be noted that much of this thesis was written prior to the imposition of the fifteen percent export tax on Canadian softwood products in January 1987. Because the tax is so recent, its present and future effects on Canada and the U.S. have not yet been fully determined. Therefore, this thesis makes reference to various studies which have attempted to estimate the impact of duties on the U.S. and Canada.

This case study was selected for several reasons. In a general sense it is a significant issue in Canadian-U.S. relations, and will add to our scholarly knowledge of the bilateral relationship. The ability of U.S. interest groups to obtain protection for their industries has been increasing because of political developments,<sup>1</sup> and the lumber dispute is of particular importance to Canada because the U.S. might also question Canadian pricing mechanisms for other natural resources. Furthermore, some researchers have estimated that restrictions will have a major impact on certain Canadian regions and on the overall economy. The softwood lumber petition was the largest countervailing duty claim in terms of dollar

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<sup>1</sup>Susan Strange and Roger Tooze, "Conclusion: the Management of Surplus Capacity and International Political Economy," in *International Politics of Surplus Capacity*, (eds.) Susan Strange and Roger Tooze (London: George Allen & Unwin Ltd, 1981) p. 214.

value ever filed in the United States.<sup>2</sup> In 1983, Canada had 34 per cent of the U.S. softwood market, but supplied about 50 percent of the low value construction lumber,<sup>3</sup> and total lumber exports were worth about \$2 billion annually.<sup>4</sup> One economic simulation suggested that "in the short run a fifteen percent duty would lead to a fall in real wages and real income of 2.87 and 2.05 percent respectively," while "the long run impact of a duty would be a massive contraction in the British Columbia economy."<sup>5</sup> An export tax was eventually imposed on Canadian softwood lumber despite a 1983 U.S. Commerce Department ruling in favour of Canada, and the issue continues as a source of tension in the bilateral relationship.

It has been postulated that Canada-U.S. relations are marked by the multiplicity of socio-economic and political connections between the two states. Some Interdependence theorists feel that these connections, a lack of hierarchy among issues, and the absence of force as a tool in determining the outcome of conflicts are related to Canadian success in disputes with the

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<sup>2</sup>Fred Harrison, "Where Canada-U.S. Frictions May Boil Up Again," *Financial Post*, November 6, 1982, p. 3.

<sup>3</sup>Eli Sopow, *Seeing the Forest: A Survey of Recent Research on Forestry Management in British Columbia*, (A limited edition working paper prepared for the Western Resources Program of the Institute for Research on Public Policy, October, 1985) p. 27.

<sup>4</sup>"Softwood Lumber Exports," *International Canada*, February and March 1985, p. 3 (supplement in *International Perspectives*, May/June 1985).

<sup>5</sup>M.B. Percy, *Forest Management and Economic Growth in British Columbia*, (Minister of Supply and Services Canada, 1986) p. 51.

U.S.<sup>6</sup> This thesis will show that the interdependence approach is useful in analyzing the 1981-83 events and the final ITA ruling in favour of Canada. The two aspects of the interdependence approach that will be demonstrated as important in this case are: heterogeneity of interests (larger country) vs homogeneity of interests (smaller country); and asymmetry of attention. In addition, this study will also address some of the limitations in an interdependence approach to Canadian-American relations. These limitations include a lack of attention to the validity of each sides' case; the costs that the smaller power must incur to win; and the ongoing nature of conflicts in the relationship, which means that a state may win at one stage and lose at another stage of the same dispute. In this case interdependence appears to be most accurate in predicting outcomes in the short-term. By using an interdependence approach, the focus of the analysis is not on the state as a unitary actor in the dispute but includes other actors such as interest groups.

There have been several important studies of the softwood lumber dispute.<sup>7</sup> Gordon Jansen, a business analyst, covered the dispute up to the ITA ruling and concluded that the Canadian

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<sup>6</sup>Robert Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, (Boston: Little, Brown and Co., 1977) p. 203.

<sup>7</sup>Gordon W.V. Jansen, "Canada-United States Trade Relations: The Lessons of the Softwood Lumber Countervail Case", *Executive Bulletin*, No. 27, August 1984; and David Leyton-Brown, *Weathering the Storm: Canadian-American Relations 1980-83*, (Toronto: Canadian-American Committee and C.D. Howe Institute, 1985).

victory was due to several factors. These included the validity of Canada's case and the unified stand of lumber producers, the federal and provincial governments, and related parties such as labour. In addition, the Canadian defence was rapidly organized primarily because of the existence of an 'early warning system'; and expert legal representation was acquired to handle the case in Washington. The softwood lumber dispute was also examined by David Leyton-Brown as part of a larger analysis of Canada-U.S. relations between 1981 and 1983. Leyton-Brown describes the bilateral relationship as one of "complex interdependence,"<sup>8</sup> but his study emphasizes the role of multilateral commitments as an underlying factor affecting the process of dispute settlement, and as an effective method of preventing or resolving bilateral disputes.<sup>9</sup>

This thesis differs from previous studies of the lumber dispute in several respects: it focuses more closely on the conditions in the U.S. that gave rise to the issue, it examines the validity of the subsidy argument, and it evaluates the efficacy of interdependence as an explanation of the initial Canadian success. Particular attention will be paid to the importance of two elements of interdependence in the outcome of the dispute: the homogeneity of the smaller state vs the heterogeneity of the larger state, and asymmetry of attention.

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<sup>8</sup>Leyton-Brown, p. 21.

<sup>9</sup>Ibid., p. 56.

The remainder of this chapter provides a brief overview of the softwood lumber dispute, examines interdependence in Canada-U.S. relations, and discusses the applicability of the interdependence framework to the softwood lumber dispute. Chapter 2 contains basic information on Canada-U.S. lumber trade, on the structure of the lumber industry in both countries, and on the American countervail process and the multilateral agreements which contributed to its design. Chapter 3 covers the period from October 1981 to October 1982. It examines the regional and economic factors that led to Canadian softwood lumber imports becoming a trade issue, chronicles the responses of U.S. elected officials to the pressure from American producers for restrictions on Canadian imports, and reviews Canada's reaction to these events. Chapter 4 covers the period from the actual filing of a countervailing petition in October 1982 to the May 1983 announcement by the U.S. Commerce Department that countervailing duties would not be imposed on Canadian softwood lumber. It focusses on the factors that led to a favourable decision for Canada, reviews the proceedings and rulings of the ITA and ITC, and examines the arguments of the petitioners and Canada. Chapter 5 presents some conclusions about the 1981-83 softwood lumber dispute and the value of an interdependence approach to understanding the outcome, and in addition it comments on the relevance of this study to the post-1983 period.

## An Overview of the Softwood Lumber Dispute

The bilateral relationship with the United States is important from a Canadian perspective because of the impact the U.S. has on many aspects of Canada's economy, politics, and society.

The greatest foreign policy challenge is the relationship with the United States. It always has been. The United States is the only country where the importance of the relationship is imposed on us.<sup>10</sup>

The differences between Canada and the United States in terms of the size of their economies and populations is reflected in their different interests and roles in the international system, and affects the priority that the bilateral relationship has in each state.<sup>11</sup> While the connection is important for strategic and economic reasons, relations with Canada are seldom a primary consideration in determining the foreign or domestic policy of the United States. There are many sources of conflict in the Canadian-American relationship. Some disputes are the result of the physical proximity of the two countries, while others arise in response to events in the global environment. No matter what the immediate source of a problem--environmental, socio-economic, technical or

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<sup>10</sup>Allan Gotlieb and Jeremy Kinsman, "Reviving the Third Option", *International Perspectives*, (January/February 1981) p. 2.

<sup>11</sup>Naomi Black, "Absorptive Systems are Impossible: The Canadian-American Relationship as a Disparate Dyad", *Continental Community? Independence and Integration in North America*, (eds.) Andrew Axline, James E. Hyndman, Peyton V. Lyon, and Maureen A. Molot, (Toronto: McClelland and Stewart, 1974) p. 98.



legal--problems become issues in the relationship when they have a perceived negative impact on one or both states and are a subject of disagreement. "An issue becomes an issue when an action or inaction by one government is a matter of dispute and requires intergovernmental negotiation".<sup>12</sup>

There are always a range of issues between Canada and the United States which are matters of dispute and negotiation. Because disputes between the two states range from regional conflicts between adjacent localities to broader national concerns, not all issues are accorded the same significance in negotiations.

The issue agenda establishes priorities among issues. It also records the way each government estimates the costs, risks, utilities of resolution, and the available means of resolving each issue.<sup>13</sup>

In economic relations between the two states, the central concerns continue to be the cross-border transmission of business cycles, investment, and trade.<sup>14</sup> Investment became an issue in the 1980's when the United States reacted negatively to particular elements of Canada's National Energy Policy and increased activity of the Foreign Investment Review Agency,<sup>15</sup>

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<sup>12</sup>Charles Doran, *Forgotten Partnership: U.S.-Canada Relations Today* (Baltimore: The Johns Hopkins University Press, 1984) p. 43.

<sup>13</sup>Ibid.

<sup>14</sup>Diebold, "Canada and the United States: Twenty-five Years of Economic Relations", *International Journal*, vol. 39, no. 2, (Winter 1983/84) p. 393.

<sup>15</sup>Marie-Josée Drovin and Harald B. Malmgren, "Canada, the United States and the World Economy", *Foreign Affairs*, vol. 60, no.2,

and that negative reaction was effectively transmitted to Ottawa.<sup>16</sup> Due to the large volume of trade and investment between Canada and the U.S. it is almost inevitable that some domestic economic policies and practices designed to alleviate particular industrial or regional concerns, will have unintended and unforeseen international ramifications.<sup>17</sup>

Currently, trade is a major focus in the Canada-U.S. relationship as negotiations over a free-trade agreement are taking place between the two states. Canada's motivation for seeking a trade agreement is in part a fear of increasing U.S. protectionism.<sup>18</sup> American protectionism has been aimed primarily at the European Community and Japan, but Canadian goods also have been affected and in some cases are the target of U.S. trade restrictions.<sup>19</sup> On the other hand, Canada has also taken actions which the U.S. has regarded as being protectionist. Recent trade issues between Canada and the U.S. involve a range of products including steel, raspberries, potatoes, hogs, corn, and shakes and shingles.

The softwood lumber dispute began when, in response to declining profits, southern and western U.S. producers initiated

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<sup>15</sup>(cont'd) (Winter 1981/82) p. 393.

<sup>16</sup>A. Bromke and K. R. Nossal, "Tensions in Canada's Foreign Policy," *Foreign Affairs*, (Winter 1983/84) p. 348.

<sup>17</sup>Diebold, p. 403.

<sup>18</sup>Jock A. Finlayson, "Canadian Business and Free Trade," *International Perspectives*, March/April 1985, p. 30.

<sup>19</sup>Ibid., p. 31.

proceedings to have countervailing duties imposed on Canadian lumber. American producers felt that Canadian governments were subsidizing softwood lumber exports to the United States mainly through low stumpage costs. Traditionally, Canadian and American attitudes towards the role of government in the economy have differed, as Canadians have accepted and supported a broader range of government intervention.<sup>20</sup> The issue of whether or not Provinces provided a subsidy when setting their stumpage rates arose in part because of differing perceptions over the role of government as an owner of natural resources.

An investigation by the ITC found that Canadian lumber was causing injury to the domestic industry, but the ITA ruled that the subsidies provided were minimal, which ended the formal 1983 enquiry and the first stage of the dispute. In the immediate period after the May 1983 ruling, American producers lobbied the U.S. Congress. Producers wanted legislative action that would either directly restrict Canada's market-share or broaden the statutory definition of subsidy to ensure that a subsequent countervail investigation would be positive. An overall improvement of the American economy in combination with an increasing Canadian market-share served to unite the previously divided American industry behind the call for import restrictions on Canadian lumber. A second countervail petition was eventually filed and it resulted in a preliminary subsidy

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<sup>20</sup>Carl E. Beigie and James K. Stewart, "New Pressures, Old Constraints: Canada-United States Relations in the 1980s", *Behind the Headlines*, August 1983, p. 7.

ruling. The second round in the lumber dispute ended with a negotiated settlement between Canada and the U.S. which imposed an export tax of fifteen percent on Canadian softwood lumber.

### Interdependence in Canada-U.S. Relations

Interdependence is one of the theoretical frameworks in international relations that has been applied to the Canada-U.S. relationship. A strength of the model is its attention to the roles of non-governmental actors and transnational relations in international politics, and this approach is effective in examining how the political, economic, and social ties between the U.S. and Canada affect the outcomes of bilateral conflicts. This thesis focuses on transnational relations at times referring to "interactions across the border in which at least one actor is nongovernmental," while "transgovernmental refers to direct interactions between agencies (governmental subunits) of different governments where those agencies act relatively autonomously from central governmental control."<sup>21</sup> The interdependence approach is useful in understanding many aspects of the softwood lumber case, since the traditionally close ties between lumber producers and wholesalers in the two states presented Canada with opportunities and means to influence the

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<sup>21</sup>Robert O. Keohane and Joseph S. Nye, Jr., "Introduction: The Complex Politics of Canadian-American Interdependence," *Canada and the United States: Transnational and Transgovernmental Relations*, (eds.) Annette Baker Fox, Alfred O. Hero, Jr., and Joseph S. Nye, Jr., (New York and London: Columbia University Press, 1976) p. 4.

outcome of the dispute. The interdependence framework used in this thesis was developed by Keohane and Nye in *Power and Interdependence* and applied by them to outcomes of conflict in the Canadian-American relationship.

According to Keohane and Nye, there are three specific conditions necessary for the realization of complex interdependence. First, the existence of multiple channels connecting societies encompassing governmental, and non-governmental ties among elites and transnational organizations. Second, the agenda of interstate relations consists of multiple issues that are not arranged in a clear or consistent hierarchy, which means that military security does not dominate the agenda and the distinction between foreign and domestic issues is blurred. Third, military force is not used as a tool by governments within a region or in issue areas.<sup>22</sup> In a reappraisal of their approach, Keohane and Nye point out that "multiple channels of contact means that states are not unitary actors."<sup>23</sup>

A general theoretical problem with interdependence is the lack of consensus over how the concept should be defined.<sup>24</sup>

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<sup>22</sup>Keohane and Nye, *Power and Interdependence*, p. 25.

<sup>23</sup>Robert O. Keohane and Joseph S. Nye, Jr., "Power and Interdependence Revisited," *International Organization*, vol. 41, no. 4 (Autumn 1987) p. 740.

<sup>24</sup>R.J. Barry Jones, "The Definition and Identification of Interdependence," *Interdependence on Trial: Studies in the Theory and Reality of Contemporary Interdependence*, (eds.) R.J. Barry Jones and Peter Willetts, (London: Frances Pinter Publishers, 1984) pp. 17-21.

Interdependence has been used in a variety of ways to describe different relationships, and while some definitions require a high degree of symmetry others allow for more asymmetry.

One of the more intractable issues within recent literature has been the controversy between those who define interdependence as 'mutual dependence' and those who view it more in terms of close 'interconnectedness', or 'interlinkage', between societies. If mutual dependence is the concept to be adopted, then there is also the question of symmetry or asymmetry, balance or imbalance.<sup>25</sup>

Kenneth Waltz's definition of interdependence limits the concept to those relationships exhibiting a high degree of symmetry. According to his view the Canada-U.S. relationship would not appear to be one of interdependence.

Interdependence suggests reciprocity among parties. Two or more parties are interdependent if they depend on one another about equally for the supply of goods and services. They are interdependent if the costs of breaking their exchanges are about equal for each of them. Interdependence means that the parties are mutually dependent.<sup>26</sup>

In contrast, Keohane and Nye view interdependence as not limited to those situations of mutual benefit and they extend the concept to include relationships "where there are reciprocal (although not necessarily symmetrical) costly effects of transactions."<sup>27</sup> It has been suggested that "many of the contrasting perspectives upon interdependence rest, fundamentally, upon basic judgements about the benign or malign

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<sup>25</sup>Jones, p. 20.

<sup>26</sup>Kenneth Waltz, *Theory of International Politics*, (New York: Addison-Wesley Publishing Co, 1979) p. 143.

<sup>27</sup>Keohane and Nye, *Power and Interdependence*, p. 9.

character of the relationships under consideration."<sup>28</sup>

Keohane and Nye clearly feel that the Canadian-American relationship is more of a benign character and can be viewed as falling into a category they term asymmetrical interdependence. They emphasize that it is the asymmetries present in interdependence that become a source of power for the actors in a relationship.<sup>29</sup> Canadian success in disputes with the U.S. is attributed in part to the elements of symmetrical and asymmetrical interdependence in the relationship, and to the effects of complex interdependence on the bargaining process.<sup>30</sup> Keohane and Nye suggest that in some instances Canadian trade is important enough to the U.S. to give Canada a retaliatory capacity, which strengthens its position even under conditions of asymmetrical interdependence. However, the deterrence value of any Canadian action is based on Canada's willingness to endure economic hardship, and Keohane and Nye feel that Canada has shown such a willingness because of asymmetrical salience; that is, "the relationship is more important to Canada than to the United States."<sup>31</sup>

Keohane and Nye also attribute Canadian success in disputes with the United States to its greater coherence in bargaining positions.

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<sup>28</sup>R.J. Barry Jones, p. 20.

<sup>29</sup>Keohane and Nye, *Power and Interdependence*, p. 11.

<sup>30</sup>Ibid., p. 203.

<sup>31</sup>Ibid., pp. 203-205.

In particular, the smaller state may have greater internal political unity than the larger one. Even though the more powerful state may be less dependent in aggregate terms, it may be more fragmented internally and its coherence reduced by conflicts of interest and difficulties of coordination within its own government.<sup>32</sup>

The differences in cohesion between the two states are due to relative size, the different governmental systems (parliamentary versus presidential), and the effects of asymmetry of attention. All these factors have an impact on the politicization of issues and on the pressures from democratic processes in both states.<sup>33</sup> The outcomes of disputes in Keohane and Nye's study were influenced by transnational and transgovernmental actors, and they found that Canada had benefitted in some cases from the participation of these actors.

In several cases, transnational organizations proved to have interests of their own that did not always coincide with the United States government's. This differentiation meant that the transnational organization sometimes improved rather than weakened the Canadian government's position in bargaining with the United States.<sup>34</sup>

This thesis uses the approach developed by Keohane and Nye and their conception asymmetrical interdependence, because of the presence in the lumber case of many of the factors they attribute to Canada's success in disputes with the United States. A significant element in Canada's initial success was the lack of cohesion among American producers compared to the

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<sup>32</sup>Keohane and Nye, *Power and Interdependence*, p. 19.

<sup>33</sup>Ibid., pp. 206 & 209.

<sup>34</sup>Ibid., p. 207.



unified position of Canadian producers. Canadian producers also had the support of forestry workers as well as the federal and provincial governments. Provincial governments and the Canadian producer's association, the Canadian Softwood Lumber Committee, were also major actors in the dispute. The lack of support for the countervail petition on the part of transnational organizations, primarily large lumber companies with mills in both countries, worked to Canada's advantage. In addition, alliances formed with the U.S. housing industry and consumer groups were also important elements in Canada's success. These alliances stemmed from the belief that any trade restricting action would result in higher prices to U.S. consumers, potentially restricting sales and therefore harming the American economy.

Although the interdependence approach is useful in examining the softwood lumber dispute, there are other factors that must also be examined: first, Keohane and Nye devote little attention to the validity of each country's position, which may have been an important element in Canada's success in the 1983 ITA investigation. Secondly, Keohane and Nye ignore the financial and manpower costs associated with a dispute, which may not be equal for each side and which are present even when Canada is successful. Finally, they examine cases over a specific time period, but many Canadian-U.S. issues continue for years making it difficult for the smaller power to prevail over the long-term. As the smaller power Canada has fewer resources in a

prolonged dispute, and as an issue persists asymmetry of attention declines and the U.S. may focus more of its resources on achieving its goals. The persistent nature of some conflicts means that the determination of when an issue has ended may have a substantial effect on which state is viewed as being successful. These problems suggest that in the long run interdependence may be less useful in understanding the outcomes of disputes between Canada and the United States. However, despite these limitations Keohane and Nye's interdependence approach is a useful framework for examining the Canada-US lumber dispute.

The following chapter examines Canada-U.S. lumber trade, the structures of the industries in both states, and the softwood products market. The primary focus is on those factors inherent in the industries which contributed to the heterogeneity and homogeneity present during the lumber dispute. Finally, the chapter concludes with a discussion of U.S. trade policies and the forces which have shaped the countervail process.

## CHAPTER II

### CANADIAN-AMERICAN LUMBER TRADE

This chapter discusses Canada-U.S. lumber trade and the softwood industries in both countries, and in particular the contribution of regional differences to the heterogeneity in the U.S. during the lumber dispute. The divisions within the American industry are contrasted with the more uniform and cohesive Canadian industry. Finally, the American countervail process and the factors that have influenced its design are examined.

Seventy percent of Canada's exports in 1980 were to the U.S. and eighteen percent of American exports were to Canada, which made the two countries each other's largest trading partners. American-Canadian forest products trade is often described as being complementary, as U.S. exports to Canada are oriented towards more highly processed or manufactured products, while Canadian exports are in general less processed.<sup>1</sup> Although the trade is complementary, the volume of forest products overwhelmingly flows from Canada to the United States. Softwood lumber is a less processed good and a major component of the forest products exported from Canada and destined for the American market. In terms of economic usage, softwood lumber can be described as an intermediate good, and more specifically, the

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<sup>1</sup>Peter Pearse, "Forest Products," *Natural Resources in US-Canadian Relations: Vol II Patterns and Trends in Resource Supplies and Policies* (eds.) Carl E. Beigie and Alfred O. Hero, Jr., (Boulder: Westview Press, 1980) p. 426.

relates to a wide variety of products--such as boards, planks, timbers, framing materials, moldings, flooring, or siding--produced from coniferous species of trees.<sup>2</sup>

Table 1. 1981 Softwood Lumber Trade Patterns of the U.S. and Canada  
(in billions of boardfeet)

	U.S.	Canada
Production	22.7	16.4
Imports	9.0	.4
Exports	1.9	11.6
Consumption	29.8	5.3

Adapted from: U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 15.

In 1981, seventy-eight percent of Canadian softwood lumber exports were sent to the U.S., while nineteen percent of American lumber exports were directed to Canada.<sup>3</sup> Canada exports a greater share of its total lumber production than the U.S., and lumber imports account for a larger share of American consumption. The U.S. clearly recognizes that it needs to import lumber to meet consumption requirements, as evidenced in in the guarantees sought from Canadian producers by the President's

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<sup>2</sup>United States International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States: Report to the Senate Committee on Finance on Investigation No. 332-134 Under Section 332 of the Tariff Act of 1930*, USITC Publication 1241, (Washington, D.C.: April 8, 1982) p. 1.

<sup>3</sup>Ibid., pp. 12 & 13.

Panel on Housing and Environment in 1972 and in statements by American proponents of restrictions on Canadian lumber in the 1980s. "Quite frankly, our nation needs Canadian lumber at times when home building is booming, as in the 1970s."<sup>4</sup>

Despite the close connections between producers in both the U.S. and Canada, significant differences exist in the style and organization of industries in each state. As in other areas, Canadian governments are more directly or visibly involved than U.S. governments in the softwood industry and the manner in which Provincial governments as resource owners establish the price of timber is central to the dispute. Another important difference between the Canadian and American forest industries is in their contribution to the national economy.

The value of production in forestry and forest-based manufacturing in the United States is more than five times that in Canada but these industries figure much larger in the Canadian economy, where they account for twice the proportion of GNP, employment, and private capital spending and comprise the leading industrial sector in terms of value added, employment, and salaries and wages.<sup>5</sup>

The differences in the structures and economic importance of the Canadian and American lumber industries contributed to the relative degrees of homogeneity and heterogeneity present during the softwood dispute.

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<sup>4</sup>William R. Ganser, Jr., "U.S. Needs Trade Policy to Compete with 'Giveaway' Canadian Timber," *Forest Farmer*, (July/August, 1985) p. 20.

<sup>5</sup>Pearse, p. 402.

## The Structure of the Canadian Industry

This examination of the Canadian softwood lumber industry focuses primarily on conditions in British Columbia. Over half of all softwood products exported to the United States market in 1984 came from B.C., and the province was used as the principal point of comparison with the U.S. by American producers.<sup>6</sup> However, while B.C. is still the major source of softwood lumber in Canada, the trend has been away from the formerly lucrative coastal region and for more production in the B.C. interior and eastern Canada.<sup>7</sup>

There is a significant degree of American involvement in the Canadian softwood lumber industry, with U.S.-owned mills accounting for ten percent of all production in 1980.<sup>8</sup> In British Columbia, the American presence is substantially larger; ten U.S.-owned firms accounted for nearly twenty per cent of the province's production in 1980. Total production by firms in which U.S. companies held some ownership was 5.7 billion board feet in 1980 out of a total production of 10.4 billion board feet.<sup>9</sup>

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<sup>6</sup>Patrick Durraut, "Interior lumber wins," *Province*, June 30, 1985, p. 38.

<sup>7</sup>Ibid.

<sup>8</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 21.

<sup>9</sup>Ibid.

A key element in softwood lumber production is access to a supply of timber. With some regional variations (most often in the Maritimes), timber-land in Canada is generally Crown land. Ninety-five per cent of the productive forest land in British Columbia is owned by the province, and is harvested under various types of licenses granted to individual private firms. Other provinces use similar methods of allocating timber cutting rights. In general, the various licenses are designed to assure firms of an adequate supply of timber over a specified period of time. The system of licenses or tenure is quite complex and reflects the provincial government's interests as landowner and the impact of forest policy on various other socio-economic, industrial, and political goals.

Because public forests cover most of the usable land throughout the province, forest policy is a critical influence in the pattern of economic and social development. . . . Thus, the policies affecting forest development determine in large degree the pattern of development of access, infrastructure, other extractive industries, and economic development generally.<sup>10</sup>

In return for harvesting rights, firms are required to undertake various obligations and improvements to the land as specified in the particular type of license they hold; and to pay the province stumpage fees, a form of royalty, for the timber harvested. Essentially, stumpage fees represent the economic rent owed to the landowner (provincial government). The calculation of stumpage by the provincial forest service is an

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<sup>10</sup>Hartley Lewis, "Objectives of Public Forest Policy," *Timber Policy Issues in British Columbia* (eds.) William McKillop and Walter J. Mead, (Vancouver: University of British Columbia Press, 1976) p. 5.

extremely complicated process.

Stumpage (rents returned to the crown) is, as previously, to be determined on the basis of calculations by the forest service. Simply stated, these are calculated for the interior regions as: the selling price of lumber and chips in four zones minus the mill operating costs for an operator of average efficiency plus an allowance for profit and various risks: for the coastal region, the calculation is: the average selling price of logs on the Vancouver log market, minus the costs of production.<sup>11</sup>

Historically, the amount of stumpage fees paid by the forest industry has been a contentious issue among different provincial political parties, interest groups, and professionals. It has been argued that the fees collected have not adequately reflected the value of the resource.

They [governments] have established a resource rent which, . . . is very low compared to that in neighboring American states of Washington and Oregon.<sup>12</sup>

Provincial stumpage practices have been the focus of a number of government and private studies over the years.<sup>13</sup> Stumpage rates

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<sup>11</sup>Patricia Marchak, *Green Gold: The Forest Industry in British Columbia*, (Vancouver: University of British Columbia Press, 1983) p. 57.

<sup>12</sup>Ibid., p. 30.

<sup>13</sup>For an overview of various Canadian views see: British Columbia, *Policies and Procedures for Evaluating Crown Timber in British Columbia, Report of the Task Force on Crown Timber Disposal*, (Victoria: 1974); British Columbia, *Timber Rights and Forest Policy in British Columbia, Report of the Royal Commission on Forest Resources*, (Victoria: 1976); Canada, Department of Industry Trade and Commerce, "Analysis of Wood costs in North American Forest Products Industries," (Ottawa: 1977); David Haley, "A Regional Comparison of Stumpage Values in British Columbia and the United States Pacific Northwest," *Forestry Chronicle*, 1980 (vol. 56, no.5) pp. 226-230; British Columbia Ministry of Forests, "The Sale of Crown Timber in British Columbia and the Determination of Its Price," (Victoria: 1980); H. Smith, "How Much Competition for Stumpage is Desirable?" *Forestry Chronicle*, 1981 (vol. 57, no.2) pp. 54-55; Ian McAskill, "Public Charges and Private Values' A Study of



charged in B.C. and the other provinces were also the central issue raised by American producers and their supporters in seeking restrictions on Canadian exports of softwood lumber. "The issue of subsidy, therefore, is central to the Canadian lumber debate. Many analysts trace Canada's competitive edge to subsidized timber or 'stumpage costs'."<sup>14</sup>

### The Structure of the United States Industry

In contrast to Canada the majority of forest land in the United States is privately owned. Farmers and other non-forest industry groups control fifty-eight percent of the total available forest land with an additional fourteen percent belonging to the forest industry.<sup>15</sup> Of the remainder of the forest lands, eighteen percent is held by the federal government and ten percent by individual states. Because of the variations in species and location of timber resources across the U.S. and the concentration of national forest lands primarily in the western states, the relative importance of federally-owned timber land to the softwood lumber industry is increased. The

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<sup>13</sup>(cont'd) British Columbia Timber Pricing," MNRM Thesis, Simon Fraser University, (Burnaby: 1982); P. B. Drysdale, "Monitoring British Columbia's Timber Pricing Performance: An Examination of Inter-regional Stumpage Comparisons," M.A. Project, Simon Fraser University, (Burnaby: 1984).

<sup>14</sup>Don Bonker, "Knots In Our Wood View From the U.S.," *Vancouver Sun*, August 2, 1985, p. A5.

<sup>15</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 25.

differences between producers in terms of ownership and access to timber resources in the U.S. contributes to the heterogeneity of interests within the industry. The industry is divided into groups based on regions and according to size of operation.

In the pacific northwestern states, forty-seven percent of the timber harvested is from public lands, and traditionally this region was the largest source of softwood lumber products manufactured in the United States, accounting for sixty-eight percent of production in 1981.<sup>16</sup> There are two types of producers in the west: "those dependent on the Government and others for timber, and those with sufficient or nearly sufficient supplies to meet their own needs."<sup>17</sup> Larger producers usually fall into the latter category, and the top forty producers in the U.S. own sixty percent of industry controlled timber lands.<sup>18</sup> This division between two different groups of western producers contributed to the lack of unity within the industry over the issue of Canadian imports and to the difficulties that small to medium size producers faced in obtaining assistance from state and federal governments. The impact of these divisions on support for the effort to restrict Canadian lumber imports were evident in the testimony of a small northwestern producer.

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<sup>16</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, pp. 50 & 7.

<sup>17</sup>Ibid., p. 57.

<sup>18</sup>Ibid.

First, we're a small segment of a very large industry. Many of the major producers in the industry are very large corporations which own land in the United States and also buy timber in Canada. They have mills that process Canadian or British Columbian provincial timber. Now it's certainly to their advantage to get high prices for their standing timber in the United States, which they own in fee, and to buy Canadian timber to use in processing in their mills in Canada at a low price. So we are not a united industry in this effort.<sup>19</sup>

Softwood lumber production in the southern states has been increasing over the last ten years, while production in the Pacific Northwest has been declining. In 1981, the southern region ranked second in softwood lumber production (twenty-eight percent of the total manufactured), but by 1984 the south had overtaken the Pacific Northwest.<sup>20</sup> Timber land ownership in the south follows a very different pattern than it does in the west. Although large forestry corporations do own some acreage in the south, farmers and small family trusts control the majority of forest land, and timber is frequently grown on plantations using modern silviculture techniques. The remaining four percent of softwood lumber produced in 1981 came from the northeastern United States, primarily Maine, where private, non-industry owners control the bulk of timber land.

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<sup>19</sup>M.J. Kuehene testimony in U.S. Congress, Senate, *United States-Canadian Trade Policies: Impact on Border State Industries*, Hearing before the Subcommittee on Oversight of Government Management of the Committee on Governmental Affairs, Ninety-Seventh Congress, First Session, (Washington, D. C., November 17, 1981) p. 39

<sup>20</sup>U.S. International Trade Commission, *Conditions Relation to the Importation of Softwood Lumber into the United States*, p. 7; and Durraut, p. 38.

The diversity of ownership of timber resources in the United States has an impact on the competitive position of firms in the country's softwood lumber industry. Large, integrated lumber producers located throughout the U.S. who own extensive tracts of forest land are better situated to survive the cyclical nature of the lumber industry. In the south, the plantation system is more responsive to changes in the market and producers are not locked into long-term contracts. In contrast, small producers in the pacific northwest who depend on public timber are the most vulnerable to market downturns.<sup>21</sup>

Determining the actual costs of timber to producers is complicated because of the diversity in ownership of forest resources. Income tax considerations influenced the accounting cost of timber cut on industry land since, before the implementation of the 1986 U.S. federal tax reform legislation, timber was treated as a capital gain item. This policy encouraged large firms to price their own stumpage at as high a cost as permissible regardless of original or book value.<sup>22</sup>

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<sup>21</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. viii.

<sup>22</sup>Ibid., pp. 16, 36 & 40.

Under U.S. capital gains provisions revenue from the sale or exchange of timber is partially excluded from taxation. "In the United States it is possible for firms that cut their own timber to treat the cutting as a sale of the timber cut if it has been held for more than one year prior to cutting. The gain determined for this hypothetical transaction is reported as a long-term capital gain. If the alternative tax applies, this gain is taxed at the long-term capital gain rate of 28 percent. Otherwise it is taxed the same as other income of the operation. The basic federal rate on other income is 46 percent for large

Private, non-industrial owners of timber land negotiate directly with softwood products firms and the price determined is more the product of a market transaction than is the case with stumpage charges for timber from either industrial or public lands.

In the case of U.S. federal timber land, the forest service uses a residual pricing system to determine an appraised stumpage value.<sup>23</sup> The advertised price at which the forest service places timber contracts out for public bidding is based on the appraised value of a lot plus road construction costs. Contracts for timber vary in length between one and eight years with an average sales period of three and a half years.<sup>24</sup> Federal timber contracts vary slightly from one region to another; the most significant difference is the inclusion of a "rate adjustment clause" in sales in Idaho, Montana, and east of the Cascade Mountains in Oregon and Washington. In these areas the rate adjustment clause allows the forest service to alter stumpage costs in accordance with fluctuations in the market

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<sup>22</sup>(cont'd) profitable operations." This system created an incentive for large corporations to transfer earnings to their timber divisions and since capital gains provisions also applied to federal timber contracts, high income taxpayers could form limited partnerships which would enable them to lower their overall tax rate. It has also been suggested that this system created an incentive for large companies to bid up federal timber contracts for land adjacent to their holdings since the U.S. Internal Revenue Service uses Forest Service stumpage prices in their capital gains calculations.

<sup>23</sup>U.S. International Trade Commission, Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, pp. 41-43.

<sup>24</sup>Ibid.

value of timber.<sup>25</sup> Differences such as this contributed to the divisions within the industry by creating different regional conditions which in a competitive market become part of an area's comparative advantage.

Comparisons of raw material prices charged softwood lumber producers in Canada and the U.S. by both Canadian and American researchers have been based on studies of two western regions, because of the apparent similarity in timber resources in these areas. Most studies examined the differences in the price bid on U. S. Pacific Northwestern national forest timber which accounts for forty-seven percent of the total harvest for that region and the stumpage rate charged in B.C. where ninety percent of the harvest is from Crown land.

#### The North American Softwood Lumber Market

Softwood lumber products are primarily used in construction industries, and demand for these products has been directly linked with the American housing market. New housing construction accounts for forty-five percent of American softwood lumber consumption, with another fifteen percent going to residential upkeep and ten percent to new non-residential construction.<sup>26</sup> Since the majority of Canadian softwood lumber

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<sup>25</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 44.

<sup>26</sup>Ibid., p. 19.

produced is destined for the U.S, the economic health of the Canadian industry depends largely upon the growth of the American housing market, and therefore on U.S. government decisions that affect the demand for new housing. The relationship between U.S. home construction and Canadian lumber sales was evident in the early 1980s when housing starts declined in response to rising interest rates and B.C. lumber sales were substantially reduced. <sup>27</sup> Another aspect to this relationship is that the U.S. housing industry regards Canada as an important source of lumber and it became an important Canadian ally during the dispute.

Generally, the industries of both countries compete in the same markets, without substantial barriers to trade between them; and softwood lumber products are basically tariff free items of trade between Canada and the United States.<sup>28</sup> Although there are differences in the species of timber located in the two states, softwood lumber products from any region are basically similar.

For a given end use, softwood lumber of a different species or from different regions is generally interchangeable. However, for some uses a specific species is frequently preferred because of its particular characteristics--e.g. Douglas-Fir for house framing, redwood for home exteriors, and white pine for molding.<sup>29</sup>

Since Canadian and American lumber industries use almost the

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<sup>27</sup>Marchak, p. 6.

<sup>28</sup>Pearse, p. 399.

<sup>29</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 5.

same marketing practices, the major determinant of sales of similar lumber sizes and grades is price and not origin. When the demand for lumber declines then price competition between firms becomes intense.<sup>30</sup>

In 1976, the primary destinations of B.C. softwood lumber products were the northeast, northcentral, and southern United States. In an expanding market, these areas were also supplied by producers located in the U.S. pacific northwest. Fifty-eight per cent of pacific northwest production was shipped to other areas of the western U.S., while only eight percent of B.C. lumber was shipped to western states.<sup>31</sup> Over the last ten years, market distribution patterns have changed substantially for producers in the Pacific Northwest and western Canada. As a result, these producers have been competing more directly to supply the housing market in the American west. In 1981, producers in Oregon and Washington were shipping sixty-seven percent of their products to other areas in the west, while B.C. producers with declining sales in the northeast and north central regions increased sales to the south and west.<sup>32</sup> In the 1980s, in a declining market this increased competition in what pacific northwestern firms regarded as their own 'backyard' has contributed to their anger over Canadian market-share. Since a

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<sup>30</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. xi.

<sup>31</sup>Ibid., p. 68.

<sup>32</sup>Ibid., p. 69.



common feature of industries seeking protection from imports is a mature and competitive market where locational advantages have shifted rapidly to favour the most efficient plants it is not surprising that these producers looked to state and federal governments for assistance.<sup>33</sup>

Despite their differences, it is evident that American and Canadian producers share many common concerns. Increasingly, U.S. and Canadian firms are affected by world demand for lumber, and the value of timber products and their cost of manufacture change constantly in long term secular patterns with changes in technology, relative prices, and societal conditions.<sup>34</sup>

Sophisticated techno-industrial methods which have made North American mills more cost-efficient and labour efficient have contributed to world-wide surplus capacity in the industry. Increased timber self-sufficiency in Japan, Europe, and Australia has added to overcapacity in North America, and current forecasts point to increasing production of softwood timber in the southern hemisphere, including New Zealand, Chile, and Brazil.<sup>35</sup> The addition of these countries to the world lumber supply means that Canadian and American producers face increased competition in both traditional and developing export

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<sup>33</sup>Charles Lipson, "The Transformation of Trade: The Sources and Effects of Regime Change," *International Organization*, vol. 36, no. 2. (Spring 1982) p. 429.

<sup>34</sup>Pearse, p. 405

<sup>35</sup>David A. Pease "Canada Industry Hurt by Decline in Exports," *Forest Industries*, March 1985, p. 46; and Ronald Anderson, "Overcapacity hits forest industries," *Globe and Mail* December 20, 1985, B2.

markets in the coming decades. Canadian and American producers have also been affected by the presence of tariff barriers especially with Japan, increased competition with Scandinavian producers, and the maturation of the European market.<sup>36</sup> Competition in the North American market is also increased by changing consumer preferences towards smaller and multi-family dwellings and new construction techniques which require less consumption of softwood lumber products.<sup>37</sup>

American and Canadian producers are cognizant of the problems posed by environmental groups, labour, and governments for firms on either side of the border.

Paradoxically or not, U.S. and Canadian lumbermen get along quite well. . . . This fraternity owes a great deal to mutual respect: Americans respect Canadians' ability to somehow prosper with a notoriously strike-prone labour force; Canadians respect Americans ability to survive an indifferent government and a powerful environmental movement.<sup>38</sup>

The extent to which producers from the two countries have similar interests is evident in the existence of several transnational trade associations including a regionally based group, the Pacific Logging Congress, as well as, The North American Forest Products Association, which is the only

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<sup>36</sup>Paul MacDonald, "Competition Still Keen Overseas," *B.C. Lumberman*, April 1985 p. 10; "Japan May Give In, Cut Wood Products Tariffs," *Forest Industries* May 1985, p. 15; and Luke Popovich, "Common Factors Outweigh U.S.-Canadian Differences," *Forest Industries*, June 1984, p. 24.

<sup>37</sup>"Pacific Loggers Mull Baking 'Bigger Pie'," *Forest Industries*, January 1985. p. 38.

<sup>38</sup>Popovich, "Common Factors Outweigh U.S.-Canadian Differences," p. 24

interregional producer organization in the United States.

### The U.S. Countervail System

The decision by U.S. producers to ask for countervailing duties moved the lumber dispute into the complex system of American trade policy. Some Americans feel that their system is unique due to the dominant role accorded to the rule of law, and because the U.S. government is viewed as acting as a neutral referee.<sup>39</sup> Although the lumber dispute is bilateral, the American countervail process is in part shaped by the existence of multilateral agreements to which both countries are parties. In general, countervailing duty provisions are designed to offset the export subsidies for a particular product that give a foreign country an unfair advantage and cause injury to domestic producers. Initially, U.S. countervail only applied to items which were already subject to a tariff, but in 1974 duty-free goods were also made countervailable.<sup>40</sup> These countervail provisions were amended again in 1979 to bring them into conformity with the Tokyo round of the General Agreement on Tariffs and Trade (GATT). The major changes to the countervailing duty provisions included "a clearer and broader

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<sup>39</sup>Alan Wm. Wolff, "International Competiveness of American Industry: The Role of U.S. Trade Policy," in *U.S. Competitiveness in the World Economy*, (eds.) Bruce R. Scott and George C. Lodge, (Boston: Harvard Business School Press, 1985), p. 303.

<sup>40</sup>Rodney de C. Grey, *United States Trade Policy Legislation: A Canadian View*, (Montreal: The Institute for Research on Public Policy, 1982) p. 37.

definition of the term 'subsidy'; a new injury test for dutiable imports; a way of remedying problems early in investigations; and a new method of adjudicating proceedings with the right to appeal preliminary and final decisions in systems court."<sup>41</sup>

The U.S. countervailing duty law adopts an adjudicatory approach,<sup>42</sup> and the submission of a countervail petition to the Department of Commerce triggers a process of investigations that must accord with a strict timetable.<sup>43</sup> Initially, the International Trade Commission (ITC) conducts a preliminary investigation to determine if there is a reasonable indication that the domestic industry is materially injured or threatened with injury as a result of the imports.<sup>44</sup> At this juncture, if the ITC finds no indication of injury the process is terminated. If it is determined that a reasonable indication of injury exists then the International Trade Administration (ITA) is charged by the Department of Commerce with conducting an investigation into whether the alleged subsidies exist and whether they are significant enough to merit a countervailing

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<sup>41</sup>Fred Lazar, *The New Protectionism: Non Tariff Barriers and Their Effects on Canada*, (Ottawa: Canadian Institute for Economic Policy, 1981) p. 30.

<sup>42</sup>John J. Barcelo III, "The Two-Track Subsidies Code--Countervailing Duties and Trade Retaliation," in *Non-Tariff Barriers after the Tokyo Round*, (eds.) John Quinn and Philip Slayton, (Montreal: The Institute for Research on Public Policy, 1982) p. 126.

<sup>43</sup>U.S. International Trade Commission, *1984 Annual Report*, USITC Publication 1718, (Washington, D.C.: Public and Consumer Affairs Office, 1985) p. 9.

<sup>44</sup>*Ibid.*, p. 6.

duty.<sup>45</sup> The ITA issues a preliminary determination prior to its final determination, which if negative terminates the investigation. A positive determination results in the case being returned to the ITC to decide whether the domestic industry is materially injured or threatened with injury by reason of the imports.<sup>46</sup>

This process for determining if countervailing duties should be assessed is a product of the legal environment which shapes American trade policy. The four main features of this legal setting are "the importance of the separation of powers and the dominant role of Congress; the prescription of detail and procedure; the importance of 'legislative history' of congressional intent in the interpretation of trade relations law; and the pervasive concern for the protection of private rights."<sup>47</sup> Some of the complexity of the countervail system can be attributed to Congress's desire to limit the amount of discretion available to executive branch officials.<sup>48</sup> Conflict between Congress and the Executive branch, and within Congress has always been a central characteristic of American trade policy; and in 1980, because of pressure from Congressional members who felt that the Treasury Department was too lax in

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<sup>45</sup>Grey, pp. 56-59.

<sup>46</sup>Ibid.

<sup>47</sup>Ibid., p. 18

<sup>48</sup>John H. Jackson, "United States Law and the Implementation of the Tokyo Round Negotiation," in *Implementing the Tokyo Round: National Constitutions and International Economic Rules* (Ann Arbor: The University of Michigan Press, 1984) p. 177.

administering anti-dumping and countervailing duty legislation, the authority to determine subsidization was transferred to the Commerce Department.<sup>49</sup>

From an American viewpoint the benefits of this system, which include "its openness; comparative objectivity; comparative insulation from undue political influence; and comparative reliance on relatively detailed published criteria," ensure foreign parties a degree of predictable access.<sup>50</sup> However, the complex legalistic nature of the system has been viewed as a trade barrier itself.

Against this system of hearings and judicial review of trade relations legislation, however, it can be argued that 'justice delayed is justice denied'. The cost of pursuing a case before the administration, before the ITC, and in the courts is very substantial, and a long period of time may elapse before a complicated case can be concluded.<sup>51</sup>

A central question in regard to the countervailing duty provisions of U.S. trade law is what constitutes a subsidy. Establishing what constitutes a subsidy is also one of the most difficult and contentious issues in international trade policy. In a broad sense a subsidy can be any of a wide range of government policies pursued primarily for legitimate domestic

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<sup>49</sup>Joan Edelman Spero, *The Politics of International Economic Relations*, 2d ed. (New York: St. Martin's Press, 1981) p. 14; and Robert E. Baldwin, "The Changing Nature of U.S. Trade Policy Since World War II," in *The Structure and Evolution of Recent U.S. Trade Policy*, (eds.) Robert E. Baldwin and Anne O. Krueger (Chicago & London: University of Chicago Press, 1984) p. 7.

<sup>50</sup>Jackson, p. 177.

<sup>51</sup>Grey, p. 18.

policy goals which may also have some effect on international trade flows.<sup>52</sup> Some agreement on countervailable subsidies was reached as part of the GATT Tokyo Round, but American law includes a broader range of practices defining a subsidy as "any bounty or grant upon the manufacture or production or export of any article or merchandise" by any level of government or private entity.<sup>53</sup>

Trade policy-making in the U.S. has become considerably more involved as the traditional line between foreign and domestic issues has been blurred.<sup>54</sup> There is evidence of this in the Tokyo round negotiations when due to the perception that "the administration always tends to try to negotiate around Congressional views and to use international agreements to contain the interests . . . [of] the constituents of Congressmen," the Congress required close consultation with the U.S. negotiators and specified American objectives in some detail.<sup>55</sup> Reports of the Tokyo round negotiations have noted the existence of two opposing views on the role of countervailing duties. The American and especially the Congressional perception was that the U.S. did not subsidize production and exports to any great extent and that the use of subsidies was declining. In

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<sup>52</sup>Jackson, p. 155.

<sup>53</sup>Lazar, p. 31 & 45; and U.S. Code, Vol. 26, Title 19, section 1301(a).

<sup>54</sup>M.J. Abrams, "Trade Policy-Making in the U.S.," *International Perspectives*, March/April, 1984, p. 9.

<sup>55</sup>Grey, p. 15.

contrast, other countries, particularly the EEC and developing countries, and of course, Canada, were felt to be subsidizing more and more.<sup>56</sup> This view is still evident in legislation being considered by the United States Congress, which attempts to redress a perceived unfairness in the way other countries conduct their trade.<sup>57</sup> Canada has also expressed similar views about the behaviour of other countries including the extent of U.S. and EEC agricultural subsidies.

Another view evident in the Tokyo negotiations, which the majority of countries supported, was more critical of the use of countervailing duties.

The view competing with this U.S. perception was that many, if not all governments were subsidizing agricultural and fisheries production and exports. Moreover, the countervail system dealt, in a rather punitive fashion, with only one sort of injurious effect of subsidization. . . Further, subsidies designed to encourage industrial development in regions of low employment or underdevelopment were important aspects of national economic and social policy in certain countries, the EEC and Canada included, where it appeared that there were greater disparities in incomes between various regions than there were in the United States.<sup>58</sup>

What emerged from these negotiations was a compromise. The United States came to accept a more restricted view of the role of countervailing duties and agreed to an injury test, and a list of prohibited subsidies was approved. The legislation which

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<sup>56</sup>Grey, p. 38.

<sup>57</sup>For example see: "House Passes Comprehensive Trade Measure," *Congressional Quarterly: Weekly Report*, vol. 45, no. 18 (May 2, 1987) pp. 811-816.

<sup>58</sup>Grey, p. 39.



brought U.S. trade law into accordance with the Tokyo Round included an injury test which was less stringent than the one set out by the Tokyo agreement, and it has been argued that the 1979 amendments in fact establish the countervailing duty provisions as a protectionist tool.

Indeed, the Trade Agreements Act went well beyond the GATT subsidies code in offering U.S. companies greater opportunities for complaint against a wider range of foreign subsidies. In effect, the subsidies code and the subsequent amendments to the Tariff Act should make it easier--or at least no more difficult--for U.S. firms to lodge complaints and for the ITC to find in favour of these complaints in countervailing duty cases. . . As a result, the amended countervailing duties section of the Tariff Act (Section 701) will be no less protectionist than its predecessor, Section 303, and may prove in time to be a more potent and effective protectionist tool.<sup>59</sup>

The number of firms utilizing U.S. fair trade legislation has been increasing as companies have become aware of the system and the changes in procedure have facilitated its use.<sup>60</sup> While Canada also has countervail procedures that may be applied to American producers, before 1984 it was virtually impossible for Canadian producers to win a countervail case and prior to 1985 Canada relied on anti-dumping regulations rather than countervail provisions. The increasing use of countervail action is seen as having a larger impact on Canada due to the asymmetry between the two systems.

United States countervail can have a decisive impact on the willingness of firms to accept subsidies in Canada,. . . [but] Canadian countervail proceedings against

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<sup>59</sup>Lazar, p. 31.

<sup>60</sup>Baldwin, p. 20.

similar U.S. subsidies will be merely an irritant.<sup>61</sup>

### Interdependence in the North American Softwood Lumber Market

The Canadian-American softwood lumber industry is characterised by the existence of close ties between producers in the two states. Canadian producers are as affected as their American counterparts by changes in the U.S. housing market. U.S. producers are affected by the competitiveness of Canadian producers in the American market and their rapid adjustment to changes in the demand for softwood products. In the North American lumber industry, independent U.S. producers have the most difficulty adjusting to changes in the supply of timber and the demand for softwood products. These pacific northwest producers are the most vulnerable segment of the continental industry to the responsiveness of the softwood lumber market to price differentials. Therefore, they are extremely sensitive to any increase in Canadian market-share, and in the 1980s their desire for some type of market protection is not unusual.

During the 1980s, as in recent years, a sharp increase in imports, whether induced by a tariff reduction or simply occurring autonomously, will invoke requests by domestic producers of import competing products, and workers in these industries, for some form of market safe guard to limit imports.<sup>62</sup>

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<sup>61</sup>Grey, p. 98.

<sup>62</sup>G. M. Meier, "U.S. Foreign Economic Policies," in *The United States in the 1980s*, (eds.) Peter Duigan and Alvin Rabushka, (Hoover Institute Publication, No. 228, 1980) p. 591.

The vulnerability dimension of interdependence, "rests on the relative availability and costliness of the alternatives that various actors face."<sup>63</sup> From this perspective, Canada appears to be very vulnerable to changes in its lumber trade with the U.S, since the number of alternative markets is limited and because of the importance of lumber exports to national and regional economies. The ability of Canadian producers to develop alternative markets appears limited, enhancing their vulnerability to U.S. restrictions.

Canadian companies have depended on the United States market for so long that in the process they have not only neglected other potential markets but also relegated offshore buyers to 'second class' status; as a result they are not leading competitors for these new markets.<sup>64</sup>

On the other hand, American producers, particularly in the northwest, are very sensitive to Canada's ability to adjust its lumber costs rapidly and remain competitive in a changing market. Also evident are the close ties between Canadian and American producers, who jointly participate in trade associations and share common concerns.

The following chapter traces the origins of the softwood lumber issue to the particular problems in U.S. federal timber contracts in the U.S. Pacific northwest and the impact of the 1981-82 recession on softwood lumber producers in that region. The Canadian response to charges that its lumber products were

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<sup>63</sup>Robert Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, (Boston: Little, Brown and Co., 1977) p. 13.

<sup>64</sup>Marchak, p. 14.

subsidized and to the various U.S. investigations which took place are also examined.

## CHAPTER III

### THE ORIGINS OF CANADIAN SOFTWOOD LUMBER EXPORTS AS A TRADE ISSUE

This chapter examines the emergence of Canadian softwood lumber exports to the United States as a trade dispute from 1981 to October 1982. In particular, the factors behind the regional nature of the issue in the United States and the reaction of U.S. elected officials to the growing pressure from the northwest for government action to assist financially troubled independent producers are reviewed. Finally, the Canadian lumber industry's response to the pressure for restrictions is analyzed.

The softwood lumber dispute was one of a number of contentious issues that arose during the early 1980s, a period in which Canadian-American relations were viewed as being in a state of crisis.<sup>1</sup> During 1980, elections took place in both states which were to result in conflicting policy objectives.<sup>2</sup> President Reagan's election marked a shift in the U.S. towards conservatism, and a desire to re-assert an American presence in the world, while Prime Minister Trudeau's return to power ushered in a period of greater Canadian nationalism. A rift between Canada and the U.S. was created by two Canadian actions,

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<sup>1</sup>Stephen Clarkson, *Canada and the Reagan Challenge: Crisis and Adjustment, 1981-1985*, (Updated Edition) (Toronto: James Lorimer & Company, 1985) p. 4.

<sup>2</sup>C. E. Beigie and James K. Stewart, "New Pressures, Old Constraints: Canada- United States Relations in the 1980s," *Behind the Headlines*, August 1983, p. 12.

the establishment of the National Energy Program (NEP) and increased activism of the Foreign Investment Review Agency (FIRA), but the crisis in the relationship was sparked by "Canadian takeovers of American companies in the spring of 1981."<sup>3</sup> Canadian concerns focussed on the withdrawal of the previously negotiated east coast fisheries treaty from the Senate, and on the problem of acid rain. Due to American pressure, Canada backed away from its economic program and managed to salvage only parts of the NEP, and by mid-1982 many of the tensions in the bilateral relationship had eased.<sup>4</sup> Although the lumber issue was not directly linked with FIRA and the NEP, in British Columbia where these policies were not popular there was certainly some fear that such a linkage might take place.<sup>5</sup> The possibility of linkage was raised by a U.S. Congressional report which advocated American retaliation against Canadian energy and investment policies by means of trade sanctions and higher tariffs.<sup>6</sup> The U.S. Congress has traditionally been more prone to link issues in Canadian-American relations, and in this case Canadian lumber was associated with other regional trade irritants including potatoes, maple syrup, and ground fish.

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<sup>3</sup>Clarkson, p. 48.

<sup>4</sup>Beigie and and Stewart, p. 18.

<sup>5</sup>Marjorie Nichols, "Socreds Belatedly Awaken to Threat to Forest Industry," *Vancouver Sun*, January 21, 1983, p. A4; and "Ease Up You Guys," (editorial) *Vancouver Sun*, February 26, 1983, p. A4.

<sup>6</sup>Bogdan Kipling, "Reagan Hit for 'Soft Stand on Canada'," *Vancouver Sun*, October 30, 1982, p. E3.

The initial impetus for restrictions on Canadian softwood lumber came from the pacific northwest region, and was directly related to the impact of the 1980-82 recession on particular segments of the softwood lumber industry. The home building industry was particularly hurt by the 1980-82 recession and by changing economic policies. Initially, the decline in softwood lumber sales appeared to be a normal cyclical downturn. However, by mid-1981 it had become apparent to the industry that an increase in new housing construction was not imminent and that a recovery was largely dependent on federal fiscal policy.<sup>7</sup> By this point, (according to the industry) production had declined to the lowest level since World War Two and unemployment in the lumber industry had risen substantially with an estimated fifty-four percent of the western work force either laid-off or working reduced hours.<sup>8</sup>

Compared to the financial positions of large integrated firms and producers in other regions, the independent softwood lumber producers in the Pacific northwest were more liable to become insolvent.<sup>9</sup> Independent producers in the pacific northwestern U.S. were financially vulnerable for several

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<sup>7</sup>"Industry Leaders Fear Collapse Unless Interest Rates Fall," *Forest Industries*, October 1981, pp. 11 & 13.

<sup>8</sup>"Housing Starts Fall Again; So What Else Is New?", *Forest Industries*, November 1981, p. 11.

<sup>9</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, Report to the Senate Committee on Finance on Investigation No. 332-134 Under Section 332 of the Tariff Act of 1930, USITC Publication 1241, (April 1982) p. viii.

reasons. As a group, independent sawmills had always been the marginal producers in the lumber industry and the first to feel the effects of a downturn in the U.S. housing market. In 1981, the impact of the declining market on these producers was more severe than in the past, due to recent financial commitments to purchase federal timber. During the late 1970s, independent producers entered into seven to eight year contracts for U.S. forest service timber. These long-term contracts had made financial sense in the economic environment of the 1970s, when government and industry forecasts pointed towards future timber shortages and a strong environmental movement was decreasing the amount of timber available for harvesting. The primary concern of all producers in the softwood lumber industry during the 1970s, and particularly from 1977-79, had been to secure an adequate supply of future timber resources. For those Pacific northwestern producers who did not own timber land the goal of securing a future timber supply was achieved through contracts for federal and state timber. As the amount of timber available for harvesting in the pacific northwest decreased, contract prices arrived at through a competitive bidding system rose. Moreover, independent producers factored into their bids the high rate of inflation of the 1970s, which further increased contract prices. Also contributing to the rise of contract prices was the involvement of speculators in the bidding process due to provisions of the U.S. tax system which enabled timber contracts to be used as tax shelters. By the end of 1980, the stumpage price for federal timber had risen to a point where the



cost of producing lumber exceeded its value.

In the pacific northwest, the average price of timber sold has had little relationship to appraised values in recent years. Because of intense competition for Forest Service timber, bid prices regularly have exceeded appraised values. Two of the primary reasons for this 'over bidding' are (1) past rates of inflation have fueled speculation of much higher timber values in the future and (2) industries' concerns over raw materials shortages in the future which results in a willingness to bid high prices to secure future supplies. Speculation in anticipation of high prices is further fueled by sales contracts of up to 7 or 8 years in length, the lack of stumpage rate adjustment mechanisms to reflect changing lumber prices (in western Washington and western Oregon), and small bid deposit requirements on sales.<sup>10</sup>

In the Pacific northwest there was no mechanism for adjusting previously negotiated federal timber contracts when the contracted price exceeded the actual value of the timber. Firms which defaulted on their federal timber contracts faced substantial financial penalties, would not be allowed to bid on re-auctioned timber, and would face close scrutiny when bidding on future sales.<sup>11</sup> The inability to adjust stumpage rates to reflect changes in value is a major difference between the stumpage systems in the pacific northwest and Canada. In Canada, where stumpage rates were determined based on the value of the lumber produced, timber costs were easily adjusted to the altered circumstances of the 1980 market.

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<sup>10</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 44.

<sup>11</sup>Luke Popovich, "Timber Contract Extensions Bring Loggers Temporary Relief", *Forest Industries*, November 1981, pp. 28-29.

The U.S. Forest Service realized by the fall of 1980, that the expectations of rising stumpage prices of many timber buyers had not translated into increased lumber prices, and as a result many federal timber harvest contracts had become economically unviable.<sup>12</sup> The U.S. Forest Service responded to this situation by granting a one year extension on contracts expiring by April 1981.<sup>13</sup> The Forest Service had previously granted extensions under similar market conditions, and based on its past experience this extension "was granted with the expectation that the normally reliable housing market would quickly rebound and absorb the swelling volumes of sold but uncut timber under contract."<sup>14</sup>

When the housing market failed to recover, the U.S. Forest Service was again faced with the possibility of a large number of contract defaults in the pacific northwest. Therefore, on October 15, 1981, the Forest Service announced an additional two year extension on timber contracts due to expire before April 1982.<sup>15</sup> Along with the extension, the Forest Service attempted to prevent speculative bidding by outlining new conditions for

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<sup>12</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 24.

<sup>13</sup>Luke Popovich, "Timber Contract Extensions Bring Loggers Temporary Relief"

<sup>14</sup>Ibid.

<sup>15</sup>"Timber Buyers Saved From Default on Contracts", *Forest Industries*, November 1981, p. W7.

future timber sale contracts.<sup>16</sup> Forest Service extensions on contracts were a welcome relief to those producers in the northwest who benefitted from them. However, other local producers viewed the extensions as at best, a short-term solution and as further encouragement to speculators in federal timber. In other regions, particularly the south, producers were opposed to contract extensions which they viewed as assistance to their competition.<sup>17</sup> The need for national policy changes to alleviate the problems in the housing market prompted the lobbying efforts of the National Forest Products Association who joined with other U.S. housing industry groups in calling for lower interest rates.<sup>18</sup>

At the same time as the Forest Service was deciding to continue its policy of contract extensions, independent producers began to organize to explore the alternatives available for long-term assistance to the northwest lumber industry. The Northwest Independent Forest Manufacturers Association (NIFM), based in Tacoma, Washington, conducted a study of the market-share of Canadian softwood lumber products. According to the figures released by M.J. Kuehne, head of the

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<sup>16</sup>In December 1983, the Forest Service implemented a policy of granting further extensions of up to five years on contracts previously extended. See: United States Department of Agriculture Forest Service, *Report of the Forest Service: Fiscal Year 1983*, February 1984, p. 22.

<sup>17</sup>Popovich, "Timber Contract Extensions Bring Loggers Temporary Relief," p. 29.

<sup>18</sup>"Industry Leaders Fear Collapse Unless Interest Rates Fall," *Forest Industries*, October 1981, pp. 11 & 13.

Association, Canadian lumber imports reached 32.2 percent of U.S. consumption during the first five months of 1981.<sup>19</sup> Kuehne viewed Canadian imports as the second factor after the U.S. housing depression responsible for high unemployment in the western forest industry. The NIFM alleged that Canadians benefitted from subsidized timber, rail, and energy costs which enabled them to undersell U.S. producers.<sup>20</sup>

Some NIFM members visited Washington, D.C. in early fall, calling on Congressional representatives, the Office of the U.S. Trade Representative, and the Commerce Department.<sup>21</sup> In discussions with the U.S. Trade Representative's office, the producers attributed their difficulties to a number of factors including federal stumpage costs, the low level of lumber exports, and imports of Canadian softwood lumber.<sup>22</sup> In regard to the latter issue the U.S. Trade Representative's office provided information on the alternative approaches available to the producers.

We have explored the various avenues of Import Relief which are available to aid U.S. industries impacted by import competition, whether from fair or unfair reasons. We have reviewed frankly with them the merits and demerits of each approach, and have expressed our

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<sup>19</sup> "Canada Takes One-Third of U.S. Lumber Market," *Forest Industries*, October 1981, p. W5.

<sup>20</sup> Ibid.

<sup>21</sup> U.S. Congress, Senate, *Forest Products Industry Issues, Hearing Before the Taxation and Debt Management Subcommittee and the International Trade Subcommittee*, Ninety-Seventh Congress, First Session (Washington, November 24, 1981) pp. 84 & 21.

<sup>22</sup> David R. MacDonald, testimony in *Forest Products Industry Issues Hearing*, p. 87.

willingness to continue to advise them further.<sup>23</sup>

Problems in the pacific northwestern lumber industry created pressure on elected officials for government action to reduce the gap between stumpage prices and market value. Oregon's Governor Vic Atiyeh responded to the growing crisis in the lumber industry on October 18, 1981, by appointing a Timber Strategy Panel to investigate the problems and to recommend actions to alleviate the situation.<sup>24</sup> In addition, a Senate hearing into forestry issues was held by Robert Packwood, an Oregon Republican.

It was no coincidence that the Oregon officials were the first to react to the problems in the lumber industry, since Oregon is the largest lumber producer in the U.S. and is substantially more dependent on timber from federal lands than any other state including Washington. In 1982, for example, 44.7 percent of the timber used to produce lumber in Oregon came from federal land compared to a figure of 23 percent in Washington.<sup>25</sup> In Oregon, the effects of the recession in the forest products industry were widespread. Not only was the lumber industry the major source of employment in the state, but forest sales also provided a significant source of direct

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<sup>23</sup>MacDonald, p. 92.

<sup>24</sup>Kenneth W. Self, Chairman, Timber Strategy Panel, in a letter to Governor Vic Atiyeh submitted as part of Oregon, Governor's Timber Strategy Panel, *Report*, November 25, 1981, p. 1.

<sup>25</sup>1983 *Statistical Yearbook of the Western Lumber Industry*, (Portland: Western Wood Products Association Economic Services Department, August 1984) pp. 7 & 10.

revenue and generated tax dollars for schools and local governments.<sup>26</sup>

### The Timber Strategy Panel's Report

The Oregon Timber Strategy Panel held six public hearings and received testimony from one hundred individuals including a presentation from a Canadian contingent.<sup>27</sup> These hearings and the final report served to focus media attention on the problems of the industry and made the general public more aware of the issue of Canadian imports. While commending the Governor's desire to re-invigorate the forest products industry, the Panel concluded that "there is no quick fix, no easy solution, no immediate and total cure."<sup>28</sup> The Panel attributed the malaise in the industry to Oregon firms being "significantly less competitive in the market place," "to a drastic reduction in our customary markets," and to Oregon's forest industries being "primary producers of raw materials and very subject to market fluctuations."<sup>29</sup>

The short and long-term recommendations of the Timber Strategy Panel can be categorized into five different areas. The major themes were: contract conditions to discourage

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<sup>26</sup>Oregon, Governor's Timber Strategy Panel, *Report*, November 25, 1981, p. 2.

<sup>27</sup>Ibid.

<sup>28</sup>Ibid., p. 2.

<sup>29</sup>Ibid., pp. 1-2.

speculation, adjusted sales schedules to allow harvesting during contract extension periods, mechanisms to allow stumpage rates to be adjusted downwards, provisions to ensure a stable timber supply, and changes in transportation rates to make Oregon lumber more competitive in the east. Furthermore, the importance of a federal policy that reduced the national budget deficit, lowered interest rates, and restored housing as a national priority was stressed.<sup>30</sup>

Within the report, there was evidence of dissension over the role of Canadian imports as a factor in the problems experienced by softwood lumber producers. The Panel's findings cited subsidies to Canadian lumber producers in combination with "the favorable exchange rate as a major cause of Oregon's loss of market share."<sup>31</sup> However, the Panel made no explicit mention of Canadian imports in its recommendations, and referred the issue along with the problem of U.S. log exports to the Joint Legislative Interim Committee on Trade and Economic Development and the Oregon Congressional delegation.<sup>32</sup>

### Senate Hearing

Congress is an important target of different groups concerned about trade issues, and the "various interests

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<sup>30</sup>Oregon, Governor's Timber Strategy Panel, pp. 4-9.

<sup>31</sup>Ibid., p. 3.

<sup>32</sup>Self, *Letter*, p. 1.

affected by specific legislation and policy decisions present their concerns to individual legislators, who represent each region according to how that region stands to gain or lose as a result of the policy adopted."<sup>33</sup> Congressional attention is also an "effective instrument of politicization in the U.S.," and was utilized by northwestern producers who addressed the issue of Canadian lumber imports at several Congressional hearings.<sup>34</sup> The most significant was the one day joint hearing of the Subcommittee on International Trade and the Subcommittee on Taxation and Debt Management to examine problems in the forest products industry. The hearing record illustrates the regional divisions within the American lumber industry. southerners were interested in tax questions involving capital gains and reforestation credit, as well as the provisions for limited partnerships and family trusts. Only pacific northwest producers addressed the problems of high stumpage rates and speculation in federal timber contracts. Except for one individual from Maine, the testimony relating to the impact of Canadian imports came from producers from western Oregon and to a lesser extent from western Washington. Several of the northwestern producers also testified that they had lost sales to firms in the southern U.S.

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<sup>33</sup>David H. Blake and Robert S. Walters, *The Politics of Global Economic Relations* (2ed) (Englewood Cliffs, New Jersey: Prentice-Hall, Inc., 1983) p. 220.

<sup>34</sup>Keohane and Nye, p. 33. The Hearings included: *United States-Canadian Trade Policies: Impact on Border States Industries*, Subcommittee on Oversight of Government Management of the Committee on Governmental Affairs, November 19, 1981; *Forest Products Industry Issues, Hearing Before The Taxation and Debt Management Subcommittee and the International Trade Subcommittee*, November 24, 1981.



as well as to Canadian suppliers, but they did not ask for any barrier against southern U.S. competition.<sup>35</sup>

A second significant cleavage within the American industry, apparent in the hearing was between small producers dependent on federal timber and large producers with private timber supplies. This division in interests was most evident within the pacific northwest delegation. Large pacific northwest producers with private timber supplies were not interested in contract relief or Canadian imports, instead they came to the hearing in search of tax breaks. These large producers had common interests with southern producers in reforestation credits, limited partnerships, and trusts.<sup>36</sup>

The small, independent northwest producers felt that the most important outcome of the hearing was a request for an investigation by the U.S. International Trade Commission on the importation of Canadian softwood lumber under Section 332 of the 1930 Tariff Act. It has been suggested that the requested investigation was a politically expedient response of elected officials to constituency pressure without obligating them to support any new legislation.<sup>37</sup> The investigation was to focus in particular on the pacific northwest region of the U.S., and

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<sup>35</sup>*Forest Products Industry Issues Hearing*, p. 205.

<sup>36</sup>*Ibid.*, pp. 253-254.

<sup>37</sup>David Leyton-Brown, *Weathering the Storm: Canadian-U.S. Relations, 1980-83*, (Toronto: C.D. Howe Institute and Washington, D.C.: National Planning Association, 1985) p. 46.

regardless, of the motivations for the request, the study was of paramount significance to independent producers as a source of information on which to base their case for restrictions on Canadian softwood lumber imports. The producers viewed the investigation as "the most direct assistance that could be provided by the Senate, because it would reduce the expense of filing a countervailing petition and would also "enhance the appreciation and understanding" of the issue by the government agencies involved.<sup>38</sup>

The one area of agreement among small and large producers from all regions, Senators, labor representatives, and Governor Atiyeh was the impact of high interest rates and the lack of a national housing policy on the lumber industry. Governor Atiyeh blamed a change in federal fiscal policies for home mortgage interest rates of 17 to 19 percent which had hurt the home building industry.<sup>39</sup> Thomas Westbrook, representing Cascade West Forest Products and the Northwest Independent Forest Manufacturers Association (NIFM), supported both contract extensions and action against Canadian imports, but described the recession in the forest products industry as a result of a severely depressed housing market caused by "a restrictive monetary policy and basic changes in the structure of the

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<sup>38</sup>Thomas J. Westbrook, testimony in *Forest Products Industry Issues Hearing*, p. 157.

<sup>39</sup>Governor Vic Atiyeh, testimony in *Forest Product Industry Issues Hearing*, p. 54.

monetary delivery system."<sup>40</sup> Westbrook made one of the most forceful statements at the hearing on the issue of Canadian imports in the American market and the extent of government subsidies to the Canadian industry. The presence of a NIFM representative at the hearing was a continuation of the Association's prominent role in the drive to restrict Canadian softwood lumber imports. In his testimony, Westbrook referred to a University of British Columbia study by David Haley. This study, which NIFM had updated, calculated that there was a twelve-to-one differential in stumpage prices between British Columbia and the U.S Pacific northwest. According to the study the differences in stumpage rates between B.C and the northwestern States had increased during 1979 and 1980; and, for example, in 1980 the average price in B.C. was \$24 per thousand board feet as compared to \$286 per thousand board feet in the National forest lands of Washington and Oregon.<sup>41</sup>

NIFM maintained that such a large difference in stumpage rates charged for similar timber was clear evidence that Canadian provinces were artificially lowering the cost of stumpage to provide a subsidy to Canadian producers. Furthermore, NIFM stressed that the ultimate aim of the subsidy was to enable Canadian producers to gain a greater share of the American market. The twelve-to-one price differential in stumpage rates was accepted with almost no dissent at the

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<sup>40</sup>Westbrook, p. 149.

<sup>41</sup>Ibid., p. 154.

hearing and repeated often by witnesses and Senators. Throughout the countervail dispute the Haley study was used by American producers to support their argument that Canadian stumpage was subsidized. NIFM's study was cited by Senator Cohen who felt that when a case arose in which there was a policy of pricing at a twelve to one differential there should be some sort of presumptive evidence that would be taken into account in proving that American producers were entitled to have a countervailing duty imposed on imports.<sup>42</sup> The almost unanimous acceptance of a price differential of twelve-to-one between U.S. Forest Service and Canadian timber costs ignored the major differences in the two stumpage systems that made any comparison extremely difficult. The previous testimony on the problem of speculation in federal timber contracts in the northwest was also ignored. This testimony could be interpreted as supporting the argument, that rather than Canadian rates being too low, western Forest Service stumpage costs were artificially high. The problems in comparing Canadian and American stumpage costs were discussed in great detail by the U.S. International Trade Commission in its Section 332 report to the U.S. Congress.<sup>43</sup>

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<sup>42</sup>Senator Cohen, testimony in *Forest Products Industry Issues Hearing*, p. 51.

<sup>43</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, pp. 51-53.

The ITC's discussion of the problems in comparing stumpage costs is reviewed on pages 68-70 of this chapter.

Further evidence of the heterogeneity of positions among U.S. producers was apparent at the hearing when, two northwestern producer representatives, who accepted the figures on the price differential as correct, suggested that the discrepancy illustrated the degree of speculation in the competitive bidding system. Both Aaron Jones and Lester Anderson called for specific changes in the procedures of contracting for Forest Service timber. Jones felt that any attempt to address the issue of Canadian imports through international law would take "significant time to pursue with no guarantee of success."<sup>44</sup> Anderson, a member of the Oregon Governor's Timber Strategy Panel, saw the problems resulting from Canadian lumber as not necessarily the cause "but to a large extent . . . the effect of many of our own actions and policies, or in some cases inaction."<sup>45</sup>

Also testifying at the hearing were Lawrence J. Brady, Assistant Secretary of Commerce for Trade, and David R. MacDonald, Deputy U.S. Trade Representative. Both men discussed previous contacts with northwest lumber producers and expressed concern over the condition of the industry in that region, as well as a willingness to work with the industry on the issue of Canadian softwood lumber imports. These men were in favour of the proposed Section 332 study, and Brady linked the issue of

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<sup>44</sup>Aaron Jones, testimony in *Forest Products Industry Issues Hearing*, p. 168.

<sup>45</sup>Lester Anderson, testimony in *Forest Products Industry Issues Hearing*, p. 66.

Canadian imports with the Reagan administration's concern over increasing Canadian intervention in its economy, particularly in the areas of energy and investment.<sup>46</sup> MacDonald, however, qualified his remarks by stating that British Columbia producers disputed the subsidy figures given by the NIFM and that he was waiting for further clarification on some apparent discrepancies.<sup>47</sup> It was evident during the hearing that a number of Congressmen felt that the administration was not as supportive of American producers as it could be and was also not responsive to the wishes of Congress. In October 1982, a Congressional report was released which accused President Reagan of being soft on Canada and urged American retaliation against Canadian energy and investment policies.<sup>48</sup>

The importance of the forest industry in the Pacific northwest and the need of Congressional representatives to be seen as responding to local concerns was underscored by the strong statements entered into the hearing record by Congressmen Bonker, from Washington, and Smith of Oregon. Bonker reiterated the NIFM position that the Canadian government unfairly subsidized its lumber industry and Smith stated that he had discussed the issue of Canadian imports with the President and

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<sup>46</sup>Lawrence Brady, testimony in *Forest Products Industry Issues Hearing*, p. 20-21.

<sup>47</sup>David MacDonald, testimony in *Forest Products Industry Issues Hearing*, p. 92.

<sup>48</sup>Kipling, "Reagan Hit for 'Soft Stand on Canada'."

called for a boycott of Canadian lumber.<sup>49</sup>

One unique aspect of the hearing was the agreement between pacific northwestern producers and the National Resources Defense Council on the desirability of an ITC investigation. This alliance was unusual because of the antagonism generated by their differing views over how National Forest resources should be managed. Some U.S. producers blamed the rise in stumpage in the northwest on the environmental movement having persuaded the government to prohibit logging of certain wilderness areas in the west. Tom Barlow, of the National Resources Defense Council called for a prohibition of the dumping of wood products at less than the costs of sustained yield management by any country, and he also urged that the pricing structure in the national forest system in the U.S. be examined to determine if indeed it met the costs of sustained yield management.<sup>50</sup>

Opposition to the proposed ITC investigation came in a written statement by the North American Wholesale Lumber Association (NAWLA), which represents distributors of lumber products. This association actively supported the Canadian position throughout the lumber dispute, and was encouraged by Canadian lumber producers to present its view to Congress. At the time of the hearing, eighteen percent of NAWLA's total

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<sup>49</sup>Representative Dan Bonker, statement in *Forest Products Industry Issues Hearing*, pp. 289-290 and Smith, pp. 291-294.

<sup>50</sup>Tom Barlow, testimony in *Forest Products Industry Issues Hearing*, pp. 281-282 & 287-288.

membership was Canadian. The wholesale lumber distributors cited four reasons for opposing the ITC investigation. First, NAWLA felt that the government and industry could ill-afford the expense of an investigation unless there was substance to the charges, and it claimed that there was no indication the charges of subsidy were valid.<sup>51</sup> Second, the association felt that Canadian imports had been increasing historically and that Canadian producers were not doing anything differently.<sup>52</sup> Third, NAWLA maintained that restrictions were not an answer to the main problem of high-priced government timber in the northwest. Finally, the association expressed concern over the accuracy and completeness of material introduced in the hearing; by implication it appeared to be referring to the figures on Canadian market-share and the twelve-to-one differential in stumpage rates.<sup>53</sup>

Soon after the hearing, Governor Aityeh declared that Oregon's forest industries were in a state of disaster. The Governor hoped that Oregon firms would then qualify for assistance from federal small business programs, but the Commerce Department stated that those programs had no available funds.<sup>54</sup> Significantly, Aityeh blamed the crisis on federal

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<sup>51</sup>North American Wholesale Lumber Association, statement in *Forest Products Industry Issues Hearing*, p. 297.

<sup>52</sup>North American Wholesale Lumber Association, p. 297.

<sup>53</sup>Ibid., p. 298.

<sup>54</sup>"Disaster State Declared in Oregon Timber Industry," *Forest Industries*, January 1982, p. W2.



fiscal policy, speculation in federal timber, and contract extensions, and despite the claims of producers he reiterated that the problems in the industry were not the result of international and inter-regional competition.<sup>55</sup> His position was very close to the views of one segment of the western industry and indicated that independent producers would have a difficult time convincing federal officials to take action against Canada. In his study of state influence in American international economic affairs, Kline discusses the utility of the endorsement of special interests by state government officials.

The political utility for special-interest groups of such an endorsement device creates an additional congressional influence mechanism that can help broaden their appeal. Similarly, state actions that serve to pose aggregate geographic interests in opposition to special-interest positions would provide potentially important off setting influences of congressmen in a debate on international economic policy.<sup>56</sup>

In a statement following a meeting with B.C.'s Premier, Bill Bennett, the Governor of Washington State rejected tariffs as a means of dealing with the issue of lumber imports, and cited the importance to Washington of foreign trade.<sup>57</sup> However, the pro-restriction forces had their first victory on December 2, 1981, when Bob Dole, chairman of the Senate Finance Committee, and Robert Packwood formally asked the International Trade

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<sup>55</sup>Aityeh, p. 54.

<sup>56</sup>John M. Kline, *State Government Influence in U.S. International Economic Policy*, (Toronto: D. C. Heath & Company, 1983) p. 226.

<sup>57</sup>Brian Kieran, "Lumber Tariffs Rejected," *Vancouver Sun*, January 22, 1982, p. A13.

Commission to conduct an investigation on the effects of softwood lumber imports into the United States. Three days earlier, Congressman Sam Gibbons of Florida had asked the ITC to initiate a similar investigation.

### The Canadian Producers' Response

The request for the ITC investigation proved to be the stimulus for Canadian producers to organize on a national basis to prevent U.S. restrictions from being imposed. Previously, individual Canadian firms were aware of the discussion in the northwest on the impact of Canadian softwood products, and some firms had been represented at the Oregon Governor's Timber Strategy Panel hearings. Representatives of individual Canadian producers had also presented material to the Department of Commerce contesting some of the claims of northwest producers prior to the Senate hearing.

On December 14, 1981 the framework for a Canadian response was rapidly developed at the inaugural meeting of the Canadian Softwood Lumber Committee (CSLC) in Ottawa. The formation of the CSLC was instigated by the President of the Council of Forest Industries in British Columbia, Donald Lanskill, who became the head of the committee.<sup>58</sup>

. . . the CSLC was to be an *ad hoc* body composed of representatives of the regional forest industry

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<sup>58</sup>Gordon W.V. Jansen, "Canada-United States Trade Relations: The Lessons of the Softwood Lumber Countervail Case," *Executive Bulletin*, No. 27, August 1984, pp. 10 & 11.

associations across Canada and a number of the major forest companies. Contacts were made with the eastern Canadian associations . . . as well as a number of key forest industry executives and federal government officials.<sup>59</sup>

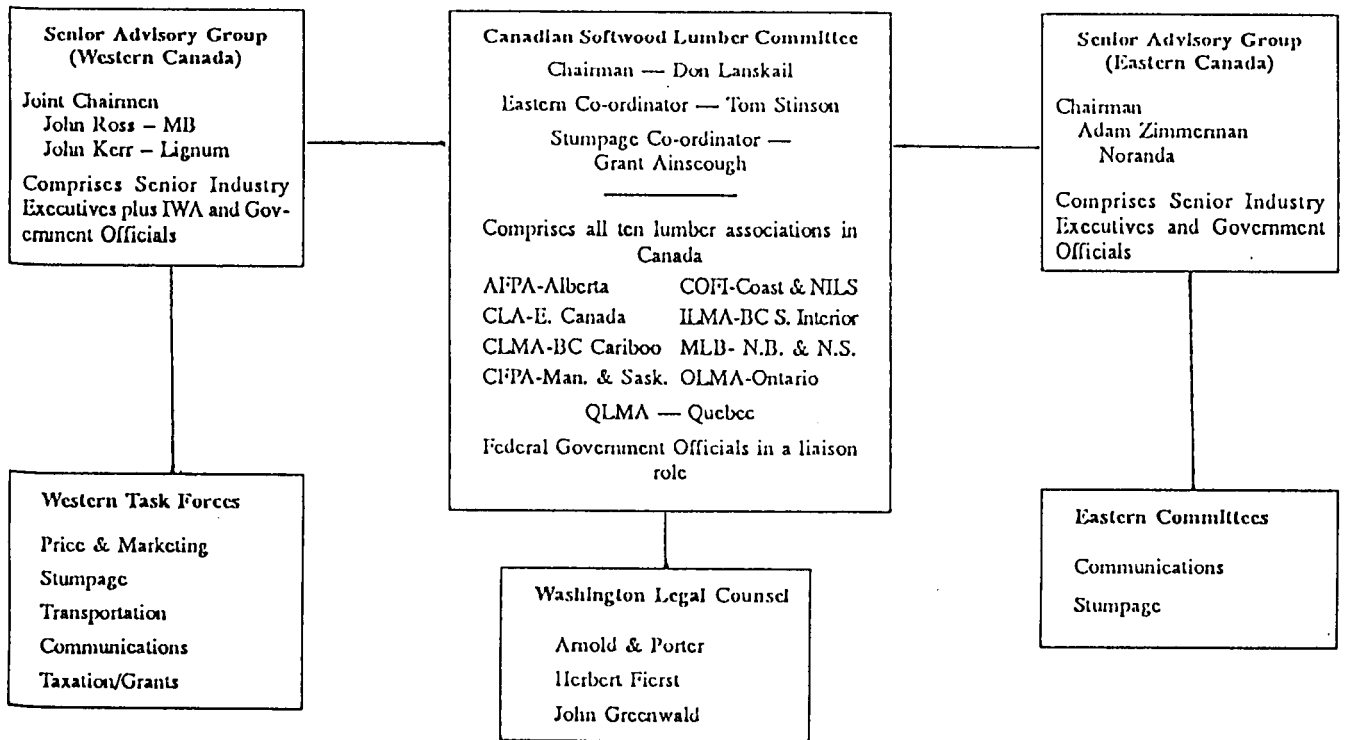
The initial meeting reviewed the issue, recognized the need for a unified Canadian response, and attempted to "ensure the full participation and co-operation of the federal government, and to lay the groundwork for organizing a Canadian industry submission to the ITC investigation."<sup>60</sup>

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<sup>59</sup>Jansen, p. 11.

<sup>60</sup>Ibid.

*Organizational Chart of the Canadian Softwood Lumber Committee*



Adapted from: Canadian Softwood Lumber Committee, *Collective Proceedings of the Investigation into the Imposition of Countervailing Duties on Canadian Softwood Lumber Products*, Vol 1 (1984) p. 2.

The leading role of Don Lanskaill and the Council of Forest Industries of B.C. (COFI) in the organization of the Canadian response is not surprising. COFI had an "early warning system" of legal representation in Washington D.C. and transnational contacts in place prior to the request for the ITC

investigation. COFI's early involvement in discussions on the issue of Canadian softwood lumber exports to the U.S. was clearly in line with its goals as an association.<sup>61</sup>

[COFI] a non-profit organization which represents, and acts on behalf of, member companies in all areas of common interests except industrial relations and direct selling.<sup>62</sup>

The Council had been successful as a lobbyist for the forest industry and "in persuading governments at every level to facilitate the needs of their member companies."<sup>63</sup> Most importantly, COFI had previous experience in defending provincial stumpage practices as it functioned as a "frontline defense" by responding "to criticism by ecologists, foresters, professors, communities, and critics of either the lack of reforestation or the low stumpage rates."<sup>64</sup>

While the CSLC represented the interests of all Canadian producers in regard to the dispute, the U.S. Coalition for Fair Canadian Lumber Imports was not formed until September 1982. This Coalition attempted to organize and represent a broad spectrum of American producers, but it never gained the support of a majority of American producers. In October 1982, the Coalition represented approximately 350 producers out of an

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<sup>61</sup>Jansen, p. 19.

<sup>62</sup>B.C. Lumber Greenbook, 1978-79, p. 215 in Patricia Marchak, *Green Gold: The Forest Industry in British Columbia*, (Vancouver: University of British Columbia Press, 1983) p. 107.

<sup>63</sup>Marchak, p.107.

<sup>64</sup>Ibid.

industry of 2000.<sup>65</sup> While the larger number of producers in the U.S. as compared to Canada may have contributed to the problem of organizing American producers, there was also greater homogeneity of interests among producers in Canada.

### The ITC Section 332 Study

The ITC report on the importation of softwood lumber products into the U.S., submitted to the Senate Finance Committee in April 1982, was a comprehensive review of the softwood lumber industry in both the U.S. and Canada. The report contained a wealth of information on the structure of the continental industry and the market for softwood lumber products as well as statistics on Canada-U.S. lumber trade. During the course of its investigation the ITC interviewed producers, elected and non-elected government officials, trade associations, academics, and union officials on both sides of the border.<sup>66</sup> Furthermore, the Commission heard testimony from northwest producers and the North American Wholesale Lumber Association in a public hearing on March 3-4 in Portland, Oregon. Canadian producers at this hearing were represented by

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<sup>65</sup>U.S. Coalition for Fair Canadian Lumber Imports, *Certain Forest Product from Canada: Softwood Lumber, Shakes and Shingles, and Fence*, Countervailing Duty Petition before the United States Department of Commerce and the International Trade Commission (Washington, D.C.: October 7, 1982) pp. 2 & 7.

<sup>66</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, pp. 80-85.

COFI'S Washington D.C. legal counsel, Herbert A. Fierst.<sup>67</sup>

The principal findings of the ITC report were subject to varying interpretations. According to the CSLC the report was "a vindication of the Canadian position."<sup>68</sup> However, Senator Robert Packwood viewed the study as supporting a U.S. import duty on Canadian softwood lumber products.<sup>69</sup> The report supported the U.S. producers' claim that the Canadian market-share was increasing, even though production in both countries was declining.<sup>70</sup> Canadian producers had lower transportation costs and benefited from a favourable exchange rate,<sup>71</sup> but according to the ITC "the primary reason for Canada's increasing market-share is the lower cost of raw materials for Canadian lumber producers."<sup>72</sup> The ITC concluded that B.C. stumpage costs varied from one-half to one-sixth of the comparable U.S. Forest Service cost. This figure is lower than the twelve-to-one differential which the Northwest Independent Forest Manufacturers cited in the Senate hearing on Forestry Issues.

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<sup>67</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 82.

<sup>68</sup>Jansen, p. 11.

<sup>69</sup>"U.S. May Impose Duty on Canadian Lumber", *Forest Industries*, June 1982, p. 13.

<sup>70</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. viii.

<sup>71</sup>Ibid., p. viii.

<sup>72</sup>Ibid., p. vii.

After appropriate adjustment the 1981 average price for coastal B.C. stumpage was about one-sixth the comparable U.S. Forest Service price per 1,000 board feet for western Oregon and Washington stumpage: US \$18 versus US \$118. In better market years, such as 1979, British Columbia prices were roughly half of comparable U.S. prices: US \$60 versus US \$127.<sup>73</sup>

The commission did not directly attribute the difference in stumpage costs to government subsidies. However, the report did discuss differences between the Canadian system of allocating timber and the various U.S. Forest Service methods, and the section examining variations in timber costs mentioned several problems in directly comparing stumpage prices in the U.S. and Canada. The ITC also commented that the Canadian observation that logging costs were higher in coastal British Columbia than in western Oregon and Washington appeared to be confirmed when stumpage prices were compared with the price of logs in log markets.<sup>74</sup> After comparing log prices the ITC found that Canadian costs were still lower, but maintained other differences in measurement systems, and in the quality and species of timber harvested made it difficult to make direct comparisons between U.S. and Canadian timber costs.<sup>75</sup>

Canadian producers were pleased with the ITC's acknowledgement that in the U.S., privately controlled fee

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<sup>73</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. x.

<sup>74</sup>Ibid.

<sup>75</sup>Ibid., p. 51.



timber is available at a lower cost than public timber.<sup>76</sup> The ITC's comments on the limited supply of federal timber in the U.S. were also favourable to Canada.

The supply of timber available now in most regions of Canada is more than sufficient to meet the productive capacity of the license holders. However, in the United States the supply from Government lands has been held at fairly constant levels in recent years, resulting in intensive competitive bidding for sales of government timber.<sup>77</sup>

The Commission compared the transportation costs to various markets of U.S and Canadian producers, and concluded that B.C. producers benefitted from lower transportation costs.<sup>78</sup> In contrast with the complex issue of raw material costs, the question of transportation subsidies was answered in an unambiguous manner. High U.S. transportation costs were determined to be the result of American regulations.<sup>79</sup>

#### Organizing for the Countervail Action

In the five months between the ITC study and the filing of the petition for a countervailing duty in October, both the independent pacific northwestern producers and the Canadian

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<sup>76</sup>U.S. International Trade Commission, *Conditions Relating to the Importation of Softwood Lumber into the United States*, p. 51.

<sup>77</sup>Ibid., p. ix. Similar statements also appear on pp. viii and xii.

<sup>78</sup>Ibid., p. ix.

<sup>79</sup>Ibid.

Softwood Lumber Committee were actively organizing, planning strategy, and preparing their cases. In March, M.J. Kuehne announced at the Portland hearing that NIFM intended to file a petition seeking a tariff on Canadian lumber, and the independent producers attempted throughout the summer of 1982 to broaden their base of support.<sup>80</sup> The Western Wood Products Association, which represents larger lumber producers in the northwest, decided not to support the NIFM, because they felt that there was no chance of success and that joining the effort would only be throwing money away.<sup>81</sup> In addition, Oregon Senator Mark Hatfield stated that he was unconvinced that a duty was a desired remedy to the problems in the industry.<sup>82</sup> An alliance was formed between the independent producers and two of the southern producer associations, the South East Lumber Manufacturers Association and Southern Forest Producers Association. Joining this alliance were two of the larger forest companies in the United States, International Paper Ltd. and Louisiana-Pacific.<sup>83</sup>

The involvement of southern producers may be attributed to the increasing Canadian market-share in the southern region.<sup>84</sup> Indeed, it was reported that in 1980 Canadian lumber accounted

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<sup>80</sup>"Canadian Exports Draw Fire at Trade Hearing," *Forest Industries*, April 1982, p. 64.

<sup>81</sup>*Vancouver Sun*, September 8, 1982, p. D1.

<sup>82</sup>*Forest Industries*, November 1982, p. 40.

<sup>83</sup>Jansen, p. 11.

<sup>84</sup>*Ibid.*

for one-half of all consumption in the south, and it was suggested that "although Pacific northwest Lumbermen have made the most noise lately about the threat from competition from Canada, southerners might do well to consider the question."<sup>85</sup> It is also clear that southern producers were strongly opposed to any Congressional action which would provide for the termination of federal timber contracts in the U.S. pacific northwest. Southerners felt that "it was not in their interest to support the efforts of the independents in the pacific northwest to win relief on their timber contracts," because they felt that contract termination could only hurt their "competitive position by assisting their domestic competition."<sup>86</sup> Thus, southerners would directly benefit from a successful countervailing action and, even if the petition was not successful, by focusing attention on Canadian lumber it would draw energy from the attempt to get federal timber contracts cancelled.

Within the National Forest Products Association, (NFPA) southern support for Congressional action to terminate high cost pacific northwest federal timber contracts was sought at the June 1982 annual meeting where it was one of the central topics discussed along with promotion of new wood products markets.<sup>87</sup>

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<sup>85</sup>"Canadian Lumber Invades the South," *Forest Industries*, May 1982, p. S2.

<sup>86</sup>Jansen, p. 11.

<sup>87</sup>Luke Popovich, "NFPA Leaders Keep Faith Despite Signs of Hardship," *Forest Industries*, July 1982, p. 39.

Any discussion of restrictions on Canadian softwood lumber products at this national meeting was not reported, but southern producers' concerns over the prospect of contract termination were expressed.

What sort of 'equity' southerners will demand wasn't plain, but observers said an essential ingredient to any consensus position would be that terminated volumes wouldn't be dumped on the already ailing market.<sup>88</sup>

Some progress towards industry unity on contract termination came in the June meeting of the Southern Forest Products Association directors when they rescinded their standing resolution opposing timber contract relief.<sup>89</sup> These producers were not indicating their support for contract termination, but by changing their position southerners hoped to be able to have some impact on the conditions which would be applied if Congress did agree to provide contract relief. During the June meeting, southern producers were pressured to change their position by some large companies, who felt that contract defaults were inevitable. These firms were concerned because it was likely that defaulted timber would be added to previously approved sales volumes contributing to a further decline in stumpage prices. Despite the move towards greater industry unanimity on the issue of contract relief, opposition from the administration and environmentalists seemed to block any quick action.

Moreover, the veto of the Housing Stimulus Bill by President

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<sup>88</sup>Popovich, "NFPA Leaders Keep Faith Despite Signs of Hardship," p. 39.

<sup>89</sup>Dave Pease, "Southern Producers Okay Timber Contract Relief," *Forest Industries*, July 1982, p. 9.

Reagan made the possibility of an immediate improvement in the financial position of any sector of the lumber industry appear unlikely.<sup>90</sup> This lack of Congressional action increased the likelihood that the industry would go the ITC route. The use of countervail legislation, contingency protection and similar measures by U.S. companies is usually a function of the general health of the industry, of the stress to which they are subject by foreign imports and their lobbying successes with Congress.<sup>91</sup>

By supporting restrictions on Canadian lumber southern producers might prevent further erosion of their market-share and possibly provide themselves with some protection in the event that any form of contract termination took place. The motivations behind the support of Louisiana-Pacific and International Paper, both large integrated forest products companies, for the countervail action has been the source of speculation. These two firms were the only ones out of the top ten producers in the industry to support the countervail action. It has been suggested that the firms were upset over previous experiences they had had in Canada.

The interests of International Paper Ltd. and Louisiana-Pacific Corporation are more complex. There is no doubt that the executives in these firms believed that there was explicit and implicit subsidization in Canada. In addition, both firms had previously had

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<sup>90</sup>Luke Popovich, "Timber Companies Fight a Battle They Can't Win," *Forest Industries*, August 1982, p. 8.

<sup>91</sup>Abraham Rotstein, "Hidden Costs of Free Trade," *International Perspectives*, July/August 1985, p. 4.

unfavourable experiences in Canada.<sup>92</sup>

The U.S. Coalition for Fair Canadian Lumber Imports grew out of the alliance of independent northwest Producers, southern producers, International Paper, and Louisiana-Pacific. However, this coalition did not encompass many of the major U.S. lumber producers or industry associations, including the NFPA. This major industry organization, which includes Canadian members, was to remain neutral on the issue of Canadian imports until 1985-86. The U.S. Coalition was loosely organized and support for its efforts varied greatly between different firms, and, in contrast to Canada, there was very limited involvement by chief executives of the larger firms.<sup>93</sup> With the formation of the Coalition, preparation of a petition requesting countervailing duties began. The task of drawing up the petition was made easier and less expensive, because "much of the work of gathering information about Canadian stumpage practices and market conditions" had already been done at public expense by the ITC in its report.<sup>94</sup>

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<sup>92</sup>Jansen, p. 12.

<sup>93</sup>For U.S. Industry involvement see: Griff Griffin, "Coalition Gains Clout on Lumber Import Issue," *Forest Industries*, July 1986, p. 29.

<sup>94</sup>Leyton-Brown, p. 46.

*The Canadian Softwood Lumber Committee*

During the summer of 1982 the newly formed Canadian Softwood Lumber Committee was developing its strategy premised on the belief that some action against Canadian lumber could be anticipated and that "because of the complexity of the issue and the timetables involved under U.S. legislation preliminary preparation would be fundamental to success."<sup>95</sup> The evolving strategy of the CSLC stressed the need for a unified Canadian position and ensuring that various governments, industry, and labour were aware of the importance of the issue and the consequences of a U.S. producers' victory. The view in Canada that the ITC study was a vindication of the Canadian position was a cause of concern to the CSLC because of its impact on Canadian preparedness for further action by U.S. producers.

Several senior Canadian forest executives believed that this interpretation caused some industry participants to become complacent. The duty free trade in lumber products between Canada and the United States reinforced the perception that, since the issue was mainly due to poor economic conditions, pressures in the United States to restrict Canadian imports would disappear when the economy improved. Moreover, many Canadians took heart in the fact that the Reagan Administration was opposed, in principle, to trade restrictions and that legislation in Congress focused mainly on seeking relief from stumpage contracts with the U.S. Forest Service.<sup>96</sup>

In preparation for a countervail action, the CSLC in August retained the Washington D.C. based firm of Arnold & Porter.<sup>97</sup>

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<sup>95</sup>Leyton-Brown, p. 13.

<sup>96</sup>Jansen, p. 14.

<sup>97</sup>Ibid., p. 15.

The firm had experience in trade law and was reputed to be one of Washington's top legal firms with extensive political knowledge and connections.<sup>98</sup> The legal team was able to use the period from August to October to familiarize itself with the forest industry and to attend briefing sessions arranged by federal officials.<sup>99</sup>

### Summary of the 1981-82 Period

This period saw the emergence of Canadian softwood lumber imports as a regional trade issue among independent producers in the U.S. pacific northwest. The heterogeneity of interests in the U.S. that Keohane and Nye found in their examination of Canadian-American relations is evident in this period of the lumber dispute. Alliances between the independents, southern producer associations, and two large firms (Louisiana-Pacific and International Paper) led to the formation of the umbrella organization the U.S. Coalition for Fair Canadian Lumber Imports. However, despite its name, the U.S. Coalition only represented a small portion of American lumber producers. The various hearings and investigations during this period revealed the diverse positions within the industry on the issue of Canadian softwood lumber. Also apparent during this period were the sometimes conflicting views of government officials. State

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<sup>98</sup>Bogdan Kipling, "Lumber Industry Hires Top U.S. Lawyers: Tariff Counter Attack Sure to be Expensive," *Vancouver Sun*, November 6, 1982, p. E1.

<sup>99</sup>Jansen, p. 16.



officials disagreed with the actions of the U.S. Forest Service, and with Congressional officials over the impact of Canadian imports on lumber producers. Conflicting views on trade were also clearly evident between federal officials and some Congressmen. The lumber industry as a whole, through the efforts of the National Forest Products Association (NFPA), was attempting to pressure the federal government to take action to revive the U.S. housing industry. Regional and sectoral concerns predominated and the forest products industry was divided over the issues of contract relief and Canadian imports. Indeed, throughout this period the regional producer associations were concentrating on protecting their particular market-share and were not interested in any policy that might assist firms in another area. Producers clearly felt that any assistance to one sector of the industry would be at the expense of others.

In this case the heterogeneity of interests in the U.S. contrasts, as Keohane and Nye suggested, with the homogeneity evident in the smaller state. Canadian producers reacted to the threat of restrictions by organizing on an industry wide basis to provide the resources necessary to fight any U.S. producer action, and to resist the allegations of unfair subsidization. The CSLC strategy of advance preparations also included rallying labour and governmental support. In part, the divisions in the U.S. industry were the result of the regional differences in the ownership of forest land and the allocations of timber rights. In Canada, an external threat to its main market combined with

fewer regional differences in the structure of the forest industry made it easier to obtain the support of all producers, forestry workers, and governments.

The differences in homogeneity and heterogeneity between Canada and the U.S. were also related to the degree of attention that each paid to the dispute. Throughout the 1981-82 period the primary focus of attention in the U.S. industry and government was the problem of high federal timber stumpage costs, and outside of the pacific northwestern region the concerns of independent producers about the presence of Canadian lumber received little attention. The NFPA was primarily concerned with the economy and the possibility of legislated contract relief, and it did not support a countervail action as a solution to the problems of the industry. Aside from the lumber industry, Canadian imports were not a significant issue. (Only those Congressmen who came from lumber producing areas showed up for the Senate hearing.) Most American producers did not appear to be concerned. In Canada, the allegations of subsidy were taken very seriously, especially in B.C. where the issue was reported on regularly in the local media.

Despite the greater heterogeneity of U.S. interests, American producers achieved a significant objective during this period when they persuaded the Senate to request an ITC investigation. The material gathered in the course of this enquiry provided much of the information necessary for the Coalition to file a petition for countervailing duties, and

reduced the cost of the proceedings to the petitioners. Although Keohane and Nye did not examine the costs to either party in the cases they analyzed, in some instances such as the softwood lumber dispute the expenses involved are quite high.

The next chapter continues to examine the impact of heterogeneity versus homogeneity and asymmetry of attention on the softwood lumber dispute, and the relative success of Canada and the U.S. producers in the countervail process.

CHAPTER IV  
THE COUNTERVAIL PROCEEDINGS

The purpose of this chapter is to further examine the issue of Canadian softwood lumber exports to the U.S. within the context of conflict resolution in Canadian-American relations. The focus will be on the countervail proceedings launched by the U.S. Coalition for Fair Canadian Lumber Imports in October 1982, which involved a series of investigations and quasi-judicial proceedings conducted by the U.S. Department of Commerce's International Trade Administration and the U.S. International Trade Commission. The factors that led to the decision by the Commerce Department in Canada's favour and the continuing central roles in the dispute of two non-governmental actors, the Canadian Softwood Lumber Committee (CSLC) and the U.S. Coalition for Fair Canadian Lumber Imports, will also be analyzed.

The Petition

The petition requesting the imposition of countervailing duties on Canadian softwood lumber products was filed by the U.S. Coalition for Fair Canadian Lumber Imports on October 7, 1982. Although the coalition at that time included only about 350 U.S. producers out of an industry of 2000, it claimed to represent a broad, national base of support for restrictions on Canadian softwood lumber.<sup>1</sup>

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<sup>1</sup>U.S. Coalition for Fair Canadian Lumber Imports, *Certain Forest*

The coalition is composed of eight trade associations and more than 350 companies. Six of those trade associations and nearly 200 of those companies represent producers of softwood lumber. The trade associations and companies are from every major lumber producing area of the country. The petitioning companies include all sizes of operations. They include five of the top seven U.S. producers who do not produce in Canada.<sup>2</sup>

The countervail petition filed with the U.S. Department of Commerce triggered separate but parallel investigations by the U.S. International Trade Administration (ITA) and the U.S. International Trade Commission (ITC). When a countervailing duty petition is filed, the ITA has twenty days in which to decide if the request will be accepted. Due to time constraints the ITC will begin its investigation into injury prior to the ITA announcing if the petition is accepted.<sup>3</sup> If a petition is accepted and the ITC finds that a domestic industry has been injured or is threatened with injury due to imports, then the ITA begins an investigation into the allegations of subsidies.<sup>4</sup>

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<sup>1</sup>(cont'd) *Products from Canada: Softwood Lumber, Shakes and Shingles, and Fence*, Countervailing Duty Petition before the United States Department of Commerce and the International Trade Commission (Washington, D.C.: October 7, 1982) pp. 2 & 7.

<sup>2</sup>U.S. Coalition for Fair Canadian Lumber Imports, *Post-Conference Brief and Responses to Questions Raised by Commission Staff and Comments on Certain Statements by Speakers Opposing Petitioner at Preliminary Conference*, Brief before the U.S. International Trade Commission (Washington, D.C.: November 9, 1982) p. 1.

<sup>3</sup>Rodney de C. Grey, *U.S. Trade Policy Legislation: A Canadian View*, (Montreal: The Institute for Research on Public Policy, 1982) p. 58.

<sup>4</sup>Ibid.

The petition filed by the U.S. Coalition for Fair Canadian Lumber Imports alleged that Canadian softwood lumber producers benefitted from a wide variety of federal and provincial subsidies. The primary benefit to Canadian producers according to the petition was the "stumpage subsidy."<sup>5</sup>

Canada completely controls the process through which mills acquire stumpage by administratively determining how much stumpage will be sold, to which mills and at what price. Canada specifically subsidizes its forest products industry by directly providing government-owned standing timber to Canadian mills for a fraction of its true market value. This is the stumpage subsidy.<sup>6</sup>

The allegation of a Canadian stumpage subsidy in the petition reiterated the main argument that Pacific Northwestern U.S. producers had been making at Congressional hearings during the previous twelve months. The American producers argued in the petition that since there was no "free market for stumpage" or "arms length transactions" in Canada, the value of the stumpage subsidy to Canadian producers should be determined by a comparison with U.S. stumpage rates.

Petitioner has used the average stumpage price set in the competitive U.S. segment of the North American domestic lumber market as the commercial benchmark against which to measure the administratively controlled average stumpage price set by Canadian provincial governments. Supporting comparisons were made for: virtually identical forests just north and south of the border; a small quasi-competitive sales system in Canada and a small Canadian-like sales system in the U.S.<sup>7</sup>

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<sup>5</sup>Countervailing Duty Petition, p. 2.

<sup>6</sup>Ibid., p. 4.

<sup>7</sup>Ibid., p. 31.

After some adjustments the value of the "stumpage subsidy" was set at 113.78 U.S. dollars per metric board feet in the petition.<sup>8</sup> In addition to the stumpage differential, the petitioners argued that Canadian producers received direct and indirect assistance from a variety of federal and provincial programs. A relatively small number of the programs cited in the petition were explicitly directed at the forest industries. Federal-provincial forest subsidiary agreements provided for federal assistance with reforestation, silvaculture, construction of access roads and timber salvage; the Canadian forestry service participated in "a number of major research activities to help the provinces and industry effectively manage and use forest resources"; and mills received assistance with the costs of converting from fossil fuels to mill and forest residues under the forest industry renewable energy program.<sup>9</sup> Of the remaining programs listed in the petition, some were directed at regional and small business development and had benefitted identifiable mills or regions. However, a large proportion of the programs cited were taxation and employment measures or directed towards general export market development.

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<sup>8</sup>Countervailing Duty Petition, p. 97.

<sup>9</sup>Ibid., pp. 42, 71, & 53.

*Federal Programs Cited in Petition as Conferring Subsidies*

1. Forest Industry Programs
  - a. Federal-Provincial Forest Industry Subsidiary Agreements
  - b. Forest Industry Renewable Energy Program
  - c. Canadian Forestry Service\*
2. Regional and Small Business Development
  - a. Regional Development Incentives Program
  - b. Small Business Industrial Development Agreements
  - c. Enterprise Development Program
  - d. Small Business Loans\*
  - e. Assistance to Remote Rural Areas
3. Export Development
  - a. Federal Business Development Bank\*
  - b. Export Development Corporation
  - c. Program for Export Market Development
4. Taxation Measures
  - a. Research and Development Measures\*
  - b. Manufacturing and Processing Profit Reduction\*
  - c. Small Business Tax Reduction\*
  - d. Employment Tax Credit
  - e. Investment Tax Credit
  - f. Accelerated Capital Cost Allowances
  - g. Inventory Allowance
5. Employment Programs
  - a. Worksharing Program
  - b. Manpower Industrial Training Program\*
  - c. Manpower Mobility
  - d. Manpower Training
  - e. Community Based Industrial Adjustment Program
  - f. Community Development Program\*
  - g. Local Employment Assistance Program
6. Transportation
  - a. Rail
    - 1) Rail Rate Agreements
    - 2) Currency Exchange Rate Tariff
    - 3) Re-load Centres
  - b. Truck
    - 1) Fuel Tax Refund
    - 2) Federal program subsidizing transportation within Quebec and from Quebec to western Canada.

Source: Countervailing Duty Petition, pp. 32-82 & p. 97.<sup>10</sup>

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<sup>10</sup>The petitioners eventually dropped the programs marked with an asterisk from the petition.



Programs in British Columbia, Quebec, Ontario, and Alberta were also listed in the petition as providing subsidies to their respective softwood lumber producers.

*Provincial Programs Cited as Providing Subsidies*

1. British Columbia
  - a. Forest Subsidiary Program
  - b. Stumpage Payment Moratoria
  - c. Forest Subsidiary Agreements
  - d. Special Assistance to Remote Rural Areas
  - e. Low-Interest Loan Assistance
  - f. Market Development Assistance Program
  - g. Log Storage Cost
  - h. Provincially Funded Forestry Job Program
  - i. Government Built Roads
  - j. Inventory Financing of Produced Products
2. Quebec
  - a. Forest Subsidiary Program
  - b. Grants (for construction or expansion of mills)
  - c. Property Tax Abatement in Labour Surplus Areas
  - d. Export Promotion Assistance
  - e. Société de Récupération, d'Exploitation et de Développement Forestiers du Québec (REXFOR)
  - f. Other Provincial Equity Programs
3. Ontario
  - a. Stumpage Payment Deferrals
  - b. Forest Subsidiary Agreement
  - c. Employment Development Fund
4. Alberta
  - a. Alberta Opportunity Company
  - b. Inventory Financing

Source: Countervailing Duty Petition, pp. 82-97.

According to the petitioners, the federal and provincial programs listed were "subsidies as that term is defined under Section 711 of the Trade Agreements Act of 1979."<sup>11</sup> Specifically, the programs were alleged to be covered by one of the four following subsections:

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<sup>11</sup>Countervailing Duty Petition, p. 93.

1. the provision of capital, loans or loan guarantees on terms inconsistent with commercial considerations
2. the provision of goods or services at preferential rates
3. the grant of funds for forgiveness of debt to cover operating losses sustained by a specific industry
4. the assumption of any costs or expenses of manufacture, production, or distribution.<sup>12</sup>

The U.S. producer's coalition requested in the petition that the definition of the domestic industry exclude those American mills with operations in Canada. The coalition felt that such operations enabled those American producers to evade the impact of Canadian subsidization.

Petitioner believes that domestic softwood lumber companies which are related to Canadian softwood lumber companies, or which in fact are not related but are importers of subsidized Canadian softwood lumber, may be able to avoid the full impact of the injury being suffered by entirely domestic companies caused by subsidized imports. If so, to include these companies in the domestic industry for the purpose of an investigation by the Commerce Department and the International Trade Commission would not truly reflect the injury being suffered by the domestic industry.<sup>13</sup>

The petition included a list of sixteen companies with mills in both Canada and the U.S. which the petitioners wanted excluded from the domestic industry.<sup>14</sup> This list of producers included five of the top ten, and eight of the top twenty-five North American softwood lumber producers.<sup>15</sup> A total of eleven of

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<sup>12</sup>Countervailing Duty Petition, pp. 94-96.

<sup>13</sup>Ibid., p. 10.

<sup>14</sup>Ibid., p. 9.

<sup>15</sup>For rankings of the top 400 lumber producers in 1981 see the "1981 Annual Lumber Review", *Forest Industries*, July 1982, pp. 20-24.

the sixteen firms listed by the petitioners were among the top fifty lumber producers in 1981.

M.J. Kuehne, a U.S. pacific northwest producer, testified in a 1981 Senate hearing on the difficulty in precisely defining the domestic industry and the importance of such a definition to the petitioners.

One of the most significant problems dealing with this issue is that many of the major forest products companies in the United States also have manufacturing operations in Canada. In a number of cases these companies are benefitting directly from the difference in price of standing timber in the United States and in Canada. . . . This also proposes [sic] a significant problem in anti-dumping and countervailing duty actions in the definition of the industry and in definition of the market.<sup>16</sup>

The attempt to exclude companies with operations in Canada from the definition of the U.S. industry was apparently an effort to strengthen the ability of the petitioners to meet the required 'injury test'. The petitioners must have been aware that an earlier Section 332 investigation conducted by the ITC found that large integrated U.S. firms were in a stronger financial position than small-to-medium sized American producers.

The divisions resulting from the continuing debate within the U.S. industry over the sources of the financial distress

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<sup>16</sup>M.J. Kuehne, testimony in United States Senate, *United States-Canadian Trade Policies: Impact on Border State Industries, Hearing before the Subcommittee on Oversight of Government Management of the Committee on Governmental Affairs, Ninety-seventh Congress, First Session (November 17, 1981) pp. 65-66.*

experienced by producers were reflected in this attempt to exclude companies with operations in Canada from the definition of the domestic industry. Many American lumber producers felt that the economic problems of the industry were the result of a depressed housing market, and in some areas due to earlier speculation in stumpage. Dissension within the industry on the relative impact of Canadian imports certainly contributed to the low profile of the countervailing action in U.S. industry journals. There was no coverage of the proceedings after the petition was filed in *Forest Industries*, the main national industry journal, except for two short articles reporting the ITA and ITC decisions.<sup>17</sup> The general asymmetry of attention to disputes between the U.S. and Canada, and the lack of unity in the American industry also contributed to the absence of mass media coverage of the softwood issue. Furthermore, these divisions also affected the ability of the coalition members to raise the funds to effectively pursue their case before the various investigatory bodies and gain public support.<sup>18</sup>

The opposition or disinterest of the majority of the American industry to the petitioner's objectives simply

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<sup>17</sup>*Forest Industries* took a very neutral stance towards the issue of Canadian imports throughout 1982 and 1983. However, by 1986 it had become supportive of the move to limit Canadian softwood lumber. There was no coverage of the issue of Canadian imports in southern producer journals during the 1981-83 period, but in 1984 one journal had an article and an editorial urging readers to assist in the attempt to reduce Canadian lumber imports.

<sup>18</sup>See Grif Griffin, "Coalition gains clout on Lumber Import Issue," *Forest Industries*, July 1986, pp. 28-29; and John C. Milliner Jr., "As Import Increase, U.S. Industry Mobilizes," *Forest Industries*, January 1985, p. 31.

reinforced the coalition's self-image as the smaller and weaker party in the dispute. From the start of their 1981 campaign, coalition members saw themselves as engaged in a desperate battle to protect their livelihood from the impact of Canadian imports. Coalition members felt that they had received very little support from either federal and state governments and their own industry organizations. The lack of interest in the issue on the part of the major forest products association was attributed to the divisions within the industry reflecting the fact that some companies had operations in Canada and because "Canadian companies themselves are members" and "they have representatives on the Board of Directors of this association and the association directly receives approximately \$400,000. per year in dues from that Canadian production."<sup>19</sup>

### Canadian Response

The Canadian government reacted quickly to the filing of the petition by sending a delegation to Washington, D.C. to request that the International Trade Administration refuse to accept it. The delegation argued that stumpage practices should not be considered a subsidy.<sup>20</sup> This was the first of a series of visits by various federal and provincial officials. In February 1983, the B.C. Forestry Minister, Tom Waterland, and the Ontario and

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<sup>19</sup>Kuehne, pp. 65-66.

<sup>20</sup>Leyton-Brown, p. 49.

Quebec resource ministers, Alan Pope and Bernard Landry,<sup>21</sup> met with U.S. Commerce Department officials in Washington, D.C. During the countervailing proceedings, the softwood lumber issue was also discussed in three separate meetings between Canada's Trade Minister Gerald Regan and U.S. Commerce Secretary Malcom Baldrige.<sup>22</sup> In an unusual departure from the norm, since this was the first instance of a case under investigation having been taken up by a Secretary of State, the issue was also discussed by Canadian External Affairs Minister, Allan MacEachen and U.S. Secretary of State George Schultz who had established a practice of holding regular meetings.<sup>23</sup>

Although Canadian governments disputed the subsidy charges, overt involvement of Canadian federal and provincial officials in the countervail proceedings was limited to providing information to the investigators, helping the industry with material to refute the charges, and sensitizing American officials to the importance of this case to Canada. Public officials avoided overt political pressure or counter threats, which might have been construed as confirmation of the legal charge.<sup>24</sup> While some news media expressed concern regarding the

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<sup>21</sup>"Waterland Meets U.S. Minister," *Vancouver Sun*, February 11, 1983, p. C4.

<sup>22</sup>Carl Mollins, "Canada Goes to Bat for Lumber Industry," *Winnipeg Free Press*, March 1, 1983, p. 27.

<sup>23</sup>*Vancouver Sun*, February 2, 1983, p. E1.

<sup>24</sup>"B.C. Plans Careful Battle Against U.S. Lumber Threat," *Toronto Star*, January 7, 1983, p. D7.

lack of direct official Canadian advocacy on the issue, the CSLC supported the decision of officials to refrain from direct political action.<sup>25</sup> The decision to avoid direct official involvement in the case was motivated by the implications of an appeal to the U.S. Court of International Trade of another countervail case involving Mexican vegetables. In this case, a negative ITA decision was being challenged on the grounds of excessive political interference.<sup>26</sup> The CSLC clearly wanted public officials to avoid statements that could be construed as implied threats, since the U.S. could then maintain that a decision favourable to Canada was based on political considerations.<sup>27</sup>

Consequently, political representations by Canadian policymakers, federal and provincial, were aimed at making Americans aware of the importance of the case for Canada and urging that it be decided on its merits. Politicians' visits to Washington were used to sensitize U.S. government officials to the importance of the issue, but Canadians were cautioned not even to appear to apply pressure and to avoid inflammatory claims in the media, such as might be directed to a home audience.<sup>28</sup>

Even in statements on the issue made to Canadian audiences, there was a careful attempt to ensure that they could not be

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<sup>25</sup>For examples of this attitude in the media see: Marjorie Nichols, "Socreds Belatedly Awaken to Threat to Forest Industry," *Vancouver Sun*, January 21, 1983 p. A4; and "On the Offensive", (editorial) *Vancouver Sun*, February 1, 1983, p. A4.

<sup>26</sup>Gordon V. Jansen, "Canada-United States Trade Relations: The Lessons of the Softwood Lumber Countervail Case," *Executive Bulletin*, No: 27, August 1984, p. 15.

<sup>27</sup>Ibid.

<sup>28</sup>David Leyton-Brown, *Weathering the Storm: Canadian-American Relations 1980-83*, (Toronto: Canadian-American Committee and C.D. Howe Institute, 1985) p. 54.

construed as political pressure on the American administration. Dave Barrett the N.D.P. opposition leader in B.C. was publicly criticized as jeopardizing the Canadian case by his comments on the dispute.<sup>29</sup> Barrett suggested that if an N.D.P. government were in power, it would retaliate against any countervailing duty imposed on softwood products.<sup>30</sup>

Despite the Canadian government's request, the ITA's decision to accept the U.S. Coalition for Fair Canadian Softwood Lumber Import's petition cannot have been unexpected by any of the parties involved. Due to their experience with the ITC Section 332 investigation the Canadian Softwood Lumber Committee was prepared to co-ordinate the countervail defence. An important aspect of the CSLC's strategy was to create a unified Canadian front composed of federal and provincial governments as well as industry and labour unions. The decision of the Canadian branch of the International Woodworkers of America to support the CSLC added to Canadian unity.<sup>31</sup> IWA support was important since it has up to 50,000 members in Canada and "is influential in matters pertaining to the resource because it includes the

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<sup>29</sup>"Bennett Raps 'Opponents' for Lumber Duty Remarks," *Vancouver Sun*, December 11, 1982, p. A16.

<sup>30</sup>"Barrett Warns Against U.S. Tariffs," *Vancouver Sun*, November 19, 1982, p. D3.

<sup>31</sup>The possibility that the softwood dispute would lead to a split between the American and Canadian branches of the IWA was realized in 1986. The breaking away of the Canadian branch was attributed to differences over concessions granted in labour negotiations in the U.S. and to the softwood lumber dispute.



majority of the organized labour force in logging."<sup>32</sup> The handling of the softwood lumber issue by the federal government was occasionally questioned in B.C., but it was never divisive in either a federal-provincial or an inter-provincial context. This relative unanimity between the provinces and the federal government is a fairly unusual occurrence in Canadian politics.

Federal-provincial relations surface in most cases involving Canada, but throughout this episode they caused almost no problems.<sup>33</sup>

Certainly, the nature of the petitioner's complaint could have resulted in antagonism among provinces over the possibility that all producers might be penalized by programs available only in one province. Most federal government assistance to the forest industry was directed to Ontario and Quebec, while B.C. received almost no assistance. Therefore, there had been a possibility that B.C. as the largest lumber producing province would request a separate ruling from the ITA.<sup>34</sup> It might have been difficult to maintain provincial unity in the face of a positive preliminary ruling if "it appeared that some provinces were responsible for subsidies that early in the proceedings also carried non offending provinces above the allowable level."<sup>35</sup>

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<sup>32</sup>Marchak, pp. 60-61.

<sup>33</sup>Leyton-Brown, p. 55.

<sup>34</sup>Jansen, p. 14.

<sup>35</sup>Leyton-Brown, p. 55.

While questions as to the federal government's response to the petition were raised in the House of Commons on four separate occasions between April 1982 and the final ITA ruling in May 1983, the countervail action was never a source of contention between federal or provincial parties.<sup>36</sup> There were reports that the federal Conservative caucus was approached by the forest industry and agreed to not raise the issue.<sup>37</sup> In addition, there was never any serious suggestion that the substance of the American producers' complaints be evaluated despite the fact that stumpage rates had previously been a salient issue in provincial politics, particularly in B.C.

The necessity for a unified Canadian position and the importance of softwood lumber being treated in a non-partisan manner within the Canadian political system was recognized by the CSLC. As part of its defence strategy, the CSLC established a communications subcommittee whose purpose was to maintain a unified Canadian opposition to the countervail action.

Its objectives were to ensure that both countries' lumber industries, media, and public were accurately and fully informed of the CSLC's position. To successfully maintain a low profile and sustain a unified Canadian position it was necessary to keep the issue non-partisan at home.<sup>38</sup>

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<sup>36</sup> "Canadian Lumber Exports," *International Canada*, October and November 1982, p. 3 (supplement to *International Perspectives* January/February 1983); "Canadian Lumber Exports," *International Canada* December 1982 & January 1983, p. 3 (supplement to *International Perspectives* March/April 1983); "Canadian Lumber Exports," *International Canada*, February and March 1983, p. 5 (supplement to *International Perspectives*, May/June 1983).

<sup>37</sup> Nichols.

<sup>38</sup> Jansen, p.16.

Another major goal of the Canadian defence was to maintain the prevalent disinterest or neutral attitude towards the issue of Canadian imports among the majority of the American lumber producers. The Canadian defence was also interested in gathering support for its position in the U.S., and the CSLC's communications subcommittee took the responsibility for implementing this strategy.<sup>39</sup> Canadians were successful in making alliances with elements of the U.S. home-building industry who were concerned about the impact of higher lumber costs on an already depressed housing market.

To return to the case of softwood lumber as an example, the Canadian Organization of Forest Industries was effective in aligning itself with the American construction trade and various homebuilders associations, whose welfare depended on the use of low-priced Canadian lumber. American interests were demonstrated to be clearly at stake.<sup>40</sup>

The alliances that Canadians formed with American groups, as well as the ties that already existed between the industries, were an important element in the Canadian success. It is evident in the softwood lumber case that, as Keohane and Nye suggest, transnational organizations and alliances can sometimes improve rather than weaken the Canadian position, because the interests of these organizations are sometimes closer to the Canadian position.<sup>41</sup>

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<sup>39</sup>Jansen, p. 16.

<sup>40</sup>R.G.P. Styles, "Organizing A Canadian Business Presence in the United States: The Alternatives," *Behind the Headlines*, Vol. XLII, No. 1, 1984, p. 22.

<sup>41</sup>Robert O. Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, (Boston: Little,

Earlier contingency planning by the CSLC, including the retainment of the Washington, D.C. legal firm of Arnold & Porter, and preparatory research, enabled Canadian producers to meet procedural deadlines. The first hearing in the countervail proceedings was on November 3, 1983 before the U.S. International Trade Commission, and the advance planning meant that the legal staff was ready to provide testimony and question witnesses. That hearing and the briefs submitted by both the petitioners and the CSLC addressed the issue of injury to the American industry by imported Canadian softwood lumber products.

The CSLC's November 9th brief maintained that an interdependent North American market existed and that:

. . . the practices of Canada's provincial governments in establishing stumpage prices, and the various other programs larded [sic] into the petition cannot as a matter of fact or law be construed as subsidies.<sup>42</sup>

The brief also stated that even if there was some government subsidy involved, the petitioners had failed to adequately show "a reasonable indication that the United States industry has been materially injured or threatened by injury by allegedly subsidized imports from Canada."<sup>43</sup>

According to the CSLC brief, the economic decline apparent in the softwood lumber industry could be directly attributed to

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<sup>41</sup>(cont'd) Brown and Co., 1977) p. 207.

<sup>42</sup>Canadian Softwood Lumber Committee, *Post-Conference Brief and Statement of Information*, Brief before the U.S. International Trade Commission, November 9, 1982, pp. 1 & 4.

<sup>43</sup>CSLC, *Post-Conference Brief*, p. 5.

a combination of economic factors in the U.S. Indeed, high U.S. interest rates and the precipitous decline in housing starts had hurt both Canadian and U.S. producers.

Rampant speculation and side effects of United States tax policies, however, resulted in bid stumpage prices by some United States companies for government timber that had little to do with the economic value of timber, and even less to do with the costs actually being incurred by the United States industry as a whole. To the extent such inflated prices injured United States producers, the injury was self-inflicted, and the remedy, as petitioners have argued before Congress, lies in modifying Forest Service contracts to reflect real timber value.<sup>44</sup>

Significantly, this analysis of the causes of financial distress within the American lumber industry was not new. Similar U.S. explanations of the problem had been made by the Oregon Governor's Timber Panel and in Congressional hearings by wholesalers and trade officials.

The CSLC brief asserted that the petitioners presented little evidence of injury by subsidized imports and relied on a few stories of lost sales and underselling by Canadian producers. "If there are any price leaders--low cost producers with low raw materials costs--they are usually the large, integrated United States forest products companies."<sup>45</sup> The brief also contended that the increase in market share (measured in board feet, not dollar value) attributed by the petitioners to the "stumpage price differential" was more readily explained by the difference in currency exchange rates.

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<sup>44</sup>CSLC, *Post-Conference Brief*, p. 61.

<sup>45</sup>Ibid., p. 10.

The correlation between Canadian market share and currency exchange rate is nearly perfect. There appears to be no correlation whatever between Canadian market share and petitioner's alleged 'Stumpage Price Differential'.<sup>46</sup>

The investigation into injury was important to Canadians, since the injury test has been viewed as one means of stopping cases that are either frivolous or intended to harass foreign producers.

The United States has adopted the technique of having a formal preliminary inquiry into injury (for both anti-dumping and countervail). This appears to have had the effect of 'turning off' a number of cases before any provisional action had been taken and of discouraging ill-founded complaints.<sup>47</sup>

If the ITC did not find that injury was being caused to the American industry then the proceedings would halt and the ITA would not be required to render a determination on the issue of subsidization. Therefore, the central thrust of the CSLC brief was to show that "there is no reasonable indication of material injury to the United States industry by reason of subsidized imports from Canada."<sup>48</sup>

As had been the case with the ITC Section 332 hearings, both the North American Wholesale Lumber Association (NAWLA) and the National Association of Home Builders testified in support of the Canadian position at the November 3rd conference. Harlan M.

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<sup>46</sup>CSLC, *Post-Conference Brief*, p. 26.

<sup>47</sup>Rodney de C. Grey, *Trade Policy in the 1980s: An Agenda for Canadian-U.S. Relations*, (Montreal: C.D. Howe Institute, 1981) p. 60.

<sup>48</sup>CSLC, *Post-Conference Brief*, p. 63.

Niebling of NAWLA was quite adamant that his association had no indication of Canadian underselling, and he referred to one instance of a large sale made by a U.S. firm at below market rates. He further commented that if any underselling of market price was occurring then large integrated firms were probably responsible.

But we are not aware of any specific industry wide underselling of Canadian product by Canadian or U.S. sellers that could in anyway be attributed to [an] alleged competitive edge from timber manufacturing costs in Canada.<sup>49</sup>

In its November 9th post-conference brief to the ITC, the U.S. Coalition for Fair Canadian Lumber Imports reiterated its view that the "stumpage subsidy" and not an exchange rate differential or speculative bidding accounted for the financial problems of the American industry.

Increases in import market penetration, such as those attained by Canadian softwood lumber imports, cause material injury. Petitioner acknowledges that housing start declines during the present recession also have affected the domestic softwood lumber industry. However, petitioner is not required to prove that the decline in housing starts or some other factor than imports is not the cause of material injury. . . . petitioner for the preliminary determination must only establish that there is a reasonable indication that Canadian imports are a cause of material injury--not establish them as a major cause or even a predominant cause.<sup>50</sup>

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<sup>49</sup>CSLC, *Post-Conference Brief*, p. 11.

<sup>50</sup>U.S. Coalition for Fair Canadian Lumber Imports, *Post-Conference Brief and Responses to Questions Raised by Commission Staff and Comments on Certain Statements by Speakers Opposing Petitioner at Preliminary Conference*, Brief before the U.S. International Trade Commission, (Washington, D.C., November 9, 1982) p. 14.

The petitioner's view that it was not required to establish Canadian softwood lumber imports as the primary cause of injury corresponded with Canadian analyses of the relevant American trade legislation.

Further, material injury in the amendments is defined as 'harm which is not inconsequential, immaterial, or unimportant.' This is an extremely weak and quite ambiguous definition which is open to wide interpretation. It requires the ITC to demonstrate only a casual relationship between an industry's poor performance and export subsidies in other countries. The subsidies need not in fact be the principal cause of poor performance or, given the various interpretations possible, even a significant cause of it.<sup>51</sup>

### ITC Preliminary Ruling

On November 22, 1982 the International Trade Commission issued its preliminary determination on the impact of Canadian softwood lumber imports.

The Commission determines . . . that there is reasonable indication that an industry in the United States is materially injured by reason of imports from Canada of softwood lumber.<sup>52</sup>

The commission qualified its conclusion by noting that its assessment of whether there had been or was a threat of material injury to the domestic industry was "limited by the sparseness of the information received in response to Commission

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<sup>51</sup>Fred Lazar, *The New Protectionism: Non Tariff Barriers and their Effects on Canada*, (Ottawa & Toronto: Canadian Institute for Economic Policy, and James Lorimer & Co., 1981) pp. 30-31.

<sup>52</sup>U.S. International Trade Commission, *Determination of the Commission in Investigation No. 701-7A-197 (Preliminary) under Section 703(a) of the Tariff Act of 1930, Together with the Information Obtained in the Investigation*, (Washington, D.C., November 1982) USITC Publication 1320, p. 1.



questionnaires."<sup>53</sup> The impact of other factors on the U.S. industry were noted in the commission's conclusion.

. . . although the drop in consumption due in large part to the decline in residential housing construction has greatly affected this industry, we find a reasonable indication that allegedly subsidized imports from Canada have caused material injury. . . . While the absolute volume of imports has declined, the percentage of the U.S. market held by imports has increased slightly during this period of declining competition.<sup>54</sup>

### International Trade Administration's Investigation

Once the International Trade Commission made its preliminary determination, the focus of the countervailing case switched to the International Trade Administration's investigation of the subsidy allegations. The ITA submitted two extensive questionnaires to the Canadian government on the nature and operations of the softwood lumber industry. The December and February questionnaires requested detailed information on Canadian practices from federal and provincial governments and from private firms.<sup>55</sup> Because of the scope and complexity of the investigation, the ITA "invoked a special provision that permitted it to delay its preliminary determination by 65 days."<sup>56</sup>

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<sup>53</sup>USITC, *Preliminary Determination*, p. 5.

<sup>54</sup>Ibid., p. 8.

<sup>55</sup>Leyton-Brown, p. 50; and "U.S. Lumber Team has 205 Questions," *Vancouver Sun*, December 16, 1982, p. D3.

<sup>56</sup>Leyton-Brown, p. 50.

The CSLC presented a memorandum to the ITA in February concerning the petitioner's allegation of a Canadian stumpage subsidy. This memorandum echoed, to a large extent, the diplomatic note submitted by the Canadian government to the U.S. government on January 7, 1983.

Besides arguing that Canadian stumpage practices did not constitute a subsidy, the note pointed out that the petition, in effect alleged that the true market value for standing timber in Canada was the price established at contract auctions in the United States. Moreover, it said, in many cases those auction values were based on little more than speculation about the level of future demand and prices; in some instances they were also subject to noncommercial considerations such as U.S. income tax treatment of stumpage sales. The Canadian government contended it was unreasonable to suggest that Canadian timber rights must also be auctioned or that the difference between the Canadian price and U.S. auction prices be considered a measure of subsidization.<sup>57</sup>

Both the diplomatic note and the CSLC memorandum expressed concern over the creation of a dangerous international precedent if the ITA found that provincial stumpage rates constituted a countervailable subsidy. The Canadian government was clearly worried that a precedent in the area of stumpage practices could have a detrimental effect on Canada's ability to determine its own natural resource policies. An immediate concern was the potential impact of a ruling that provincial stumpage rates constituted a subsidy on Canada's pulp and paper industry.

Petitioners are thus raising a novel and unprecedented claim. Because of important public policies, established economic principles, and various practical considerations, there should be a strong presumption against extending the concept of countervailable subsidy to this type of practice. . . . It is questionable

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<sup>57</sup>Leyton-Brown, p. 51.

whether one should even consider countervailability in connection with foreign government natural resource policies.<sup>58</sup>

The CSLC memorandum also warned of the possible impact on American exporters of an extension of the concept of subsidy to include natural resource pricing by governments.

In addition the United States might consider the precedent that would be established by finding 'stumpage' a countervailable subsidy. Such a precedent could well be seized upon by other countries as a basis for countervailing against United States products on the ground that government-influenced natural resource prices . . . make possible the export of products which are unfairly competitive abroad.<sup>59</sup>

A similar warning was made in a New York Times editorial which supported Canadian practices.<sup>60</sup>

Soon after delivery of the January diplomatic note, some Canadian officials were informed by their counterparts at the U.S. Department of Commerce that:

. . . the ITA intended to apply the 'targeting test' of U.S. law. Subsidies would be defined in terms of special advantages to particular industries or plants in particular regions. Administered prices *per se* would not be viewed as subsidies."<sup>61</sup>

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<sup>58</sup>Canadian Softwood Lumber Committee, *Memorandum of Canadian Softwood Lumber Committee Concerning the Alleged Stumpage Subsidies*, Before the International Trade Administration of the U.S. Department of Commerce, (Washington, D.C., February 4, 1983) p. 2.

<sup>59</sup>CSLC, *Memorandum*, p. 5.

<sup>60</sup>"Don't Fence Lumber," (editorial) *New York Times*, February 11, 1983; p. A26.

<sup>61</sup>Leyton-Brown, p. 51.

The CSLC's February memorandum argued that timber was available to a wide range of industries and no specific industry was given a special advantage. This memorandum argued that governmental targeting was not taking place in the Canadian lumber industry.

In short, Canadian government timber policies do not single out any specific industry for any special advantages. Nor do they discriminate against users of timber resources on the basis of foreign or domestic ownership or control. And of course, producers for domestic and foreign markets are treated in exactly the same way.<sup>62</sup>

The CSLC memorandum also criticized the methodology used by the coalition's consultants in their comparisons of stumpage costs in the U.S. and Canada.

The data on United States prices utilized in petitioners' cross-border comparisons were the prices *bid* in 1980, reflecting speculation as to the value of timber to be cut in the future under different market conditions, and assuming substantial inflation. These bid prices were compared with prices *paid* by Canadian producers for trees cut in 1980. The only even arguably legitimate comparison--leaving aside the fact that no such comparison is legally relevant here--is between the price paid by United States producers for timber cut in 1980 and the price paid by Canadian producers for timber cut in 1980.<sup>63</sup>

Consultants retained by the CSLC conducted a separate comparison of stumpage costs. They concluded that if any difference in stumpage costs existed, the differential would show that Canadian producers paid more for stumpage than U.S. producers.

Attached . . . is a joint report prepared by a team of expert Canadian and United States forestry consulting firms. That report makes the adjustments omitted by

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<sup>62</sup>CSLC, *Memorandum*, p. 46.

<sup>63</sup>*Ibid.*, p. 75.

petitioners, and compares, to the greatest extent possible, like payments for like trees in the same year. When errors in petitioner's analysis are corrected, the supposed Canadian advantage disappears. Indeed, if anything, delivered log costs in Canada appear to be somewhat higher than in the United States.<sup>64</sup>

The CSLC issued a separate memorandum on February 8th that discussed the other programs listed in the petition as providing countervailable benefits to Canadian producers. In commenting on the variety of programs cited in the petition, the memorandum questioned whether the petitioners were interested in redressing tangible grievances. The CSLC suggested that the petitioners were "using the countervailing duty procedure to launch a broad-ranging investigation into Canadian government practices they little understand."<sup>65</sup>

It has also been suggested that the motive behind the variety of programs cited in the countervailing petition was the hope that some combination of programs might place a subsidy finding above the *de minimus* level.

Some observers felt that these other complaints were merely atmospheric to show the interventionary nature of the Canadian state. Nevertheless, the possibility existed that even if the ITA rejected the central claim of a stumpage subsidy, the incremental subsidizing effects of other programs. . . would raise the total level of subsidization above the 0.5 percent *de minimus* level and thus activate a countervailing duty.<sup>66</sup>

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<sup>64</sup>CSLC, *Memorandum*, p. 77.

<sup>65</sup>Canadian Softwood Lumber Committee, *Memorandum of Canadian Softwood Lumber Committee Concerning Non-Stumpage Programs*, Before the International Trade Administration of the United States Department of Commerce, (Washington, D.C., February 8, 1983) p. i.

<sup>66</sup>Jansen, p. 48.

The CSLC's February 8th memorandum stressed that the various programs cited by the petition did not either individually or collectively provide any significant benefits to Canadian producers.<sup>67</sup>

*The ITA's Preliminary Determination*

The ITA issued its preliminary determination on March 8, 1983, and its decision was favourable to Canada on the issue of provincial stumpage practices. It found that the "stumpage programs of the Canadian federal and provincial governments do not confer a subsidy on the products under investigation."<sup>68</sup> The ITA's reasons for this determination addressed the issue of stumpage constituting either an export or domestic subsidy. It found that stumpage programs did not confer an export subsidy, "because they do not operate and are not intended to stimulate export rather than domestic sales, and because they are not offered contingent upon export performance."<sup>69</sup> According to the ITA, the fact that a significant quantity of the products made from stumpage were exported to the U.S. did not necessarily mean that Canadian stumpage programs constituted an export subsidy.<sup>70</sup> Stumpage programs also did not constitute a domestic

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<sup>67</sup>CSLC, *Memorandum Concerning Non-Stumpage Programs*, p. v.

<sup>68</sup>U.S. Department of Commerce, International Trade Administration, *Preliminary Negative Countervailing Duty Determinations, Certain Softwood Products from Canada* (Washington, D.C., March 8, 1983) p. 50.

<sup>69</sup>Ibid.

<sup>70</sup>Ibid.

subsidy according to the ITA, because they were not provided to a "specific enterprise or industry." Stumpage was found to be generally available in Canada regardless of product with the type of industry using stumpage limited only by the "characteristics of the resource and the current level of technology."<sup>71</sup> As the Canadian officials had been informed earlier, the ITA applied a targeting test and found "no evidence of governmental targeting regarding stumpage."<sup>72</sup>

The ITA did not accept the petitioner's arguments that the provision of stumpage by the provinces constituted an assumption of a cost of production.

. . . we preliminarily determine that Canadian stumpage programs do not 'assume' a cost of production. We believe that the most reasonable interpretation of 'assumption' is that it refers only to government activity which relieves an enterprise or industry of a pre-existing statutory or contractual obligation.<sup>73</sup>

The ITA viewed the residual value system utilized by the provinces to determine stumpage rates as a reasonable basis for determining the "true market value" of stumpage. The similarity of the ITA's determination with the arguments raised by the Canadian defence is clear in the ITA's discussion of why (even if the relevant sections of the tariff act were given a broad interpretation) provincial stumpage practices would still not constitute a subsidy.

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<sup>71</sup>ITA, *Preliminary Negative Countervailing Duty Determinations*, p. 51.

<sup>72</sup>Ibid.

<sup>73</sup>Ibid., pp. 53-54.

As implied above, a comparison of Canadian stumpage prices with U.S. prices would be arbitrary and capricious in view of (1) the wide disparity between quality and accessibility of the standing timber in the U.S. and throughout Canada; (2) the significant in-kind payments which are required generally in Canada in addition to monetary payments, but not generally in the United States; and (3) the fact that in recent years prices in the U.S. usually have been bid anywhere between two to five years in advance of use, without having taken into account the decline in the housing industry. We are not convinced that there is a rational basis to adjust for these significant differences.<sup>74</sup>

The ITA felt that even if adjustments were made for the significant differences between U.S. and Canadian timber and stumpage pricing systems, then petitioner's allegation of a vast "stumpage price differential" would not be substantiated.

If, alternatively, one believes that there is a rational basis for adjustments, the record of these investigations includes studies showing that once appropriate adjustments are made to take into account these differences, Canadian prices for standing timber do not vary significantly from U.S. prices. Indeed, in some cases the Canadian price may be higher. Therefore, even if one were to use U.S. prices as a benchmark, there is evidence in the record which establishes that Canadian governments do not assume costs of production through their stumpage programs.<sup>75</sup>

In its preliminary determination, the ITA found that some of the programs cited in the petition did provide subsidies to Canadian softwood lumber producers. However, the total estimated net subsidies of 0.32 percent *ad valorem* were deemed by the ITA to be *de minimus*.<sup>76</sup> The decision to declare the small subsidies

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<sup>74</sup>ITA, *Preliminary Negative Countervailing Duty Determinations*, p. 58.

<sup>75</sup>Ibid.

<sup>76</sup>Ibid., p. 2.



involved as *de minimus* was reportedly made by Commerce Secretary  
Baldrige.<sup>77</sup>

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<sup>77</sup>"B.C. Breathes A Sigh of Relief as Threat to Lumber Sales  
Lumber Sales Lifted," *Vancouver Sun*, March 8, 1983, p. A1.

*Programs Preliminarily Determined by the ITA to Confer Subsidies*

1. Federal Programs
  - a. Investment Tax Credit
  - b. Program for Export Market Development
  - c. Forest Industry Renewable Energy Program
  - d. Regional Development Incentives Program-Grants
  
2. Federal/Provincial Programs
  - a. Agriculture and Rural Development Agreements
  - b. General Developments Agreements
    - 1) Federal/Provincial Industrial Development Subsidiary Agreements
    - 2) British Columbia - Assistance to Small Enterprise Program
    - 3) New Brunswick
      - a) Northeast New Brunswick Development Program (NED)
      - b) Kent Region Pilot Project (KED)
      - c) Industrial Development Subsidiary Agreement (SIFAP)
    - 4) Canada/Nova Scotia Forestry Subsidiary Agreement - Sawmill Improvement Component Grants
  
3. Provincial Programs
  - a. Alberta - Timber Salvage Incentive Program
  - b. British Columbia
    - 1) Low-Interest Loan Assistance
    - 2) Stumpage Payment Deferral
  - c. Ontario - Stumpage Billing Deferral
  - d. Quebec
    - 1) Société de Récupération, d'Exploitation et de Développement Forestiers du Québec (REXFOR)
    - 2) Fonds de Relance Industrielle (FRI) Tax Abatement Program
    - 3) Société de Développement Industriel (SDI) Export Expansion Program

Source: ITA, *Preliminary Negative Countervailing Duty Determinations*, pp. 3-5.

The ITA's preliminary ruling was a great relief to Canadian producers, forestry workers and municipalities, as well as the federal and provincial governments. In British Columbia, where the impact of a negative decision would have been the greatest, the ITA ruling became the major news story of the day.<sup>78</sup>

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<sup>78</sup>"B.C. Breathes a Sigh of Relief as Threat to Lumber Sales

Clearly, the preliminary ruling was a victory for Canada. However, the investigation into the allegations of subsidization would continue as ITA investigators verified the accuracy of the information obtained during the preliminary investigation from producers and Canadian governments.<sup>79</sup> Based on its investigation, the ITA in its final ruling could have found that the level of subsidization involved was over the *de minimus* amount of .5 percent. At the time of the ITA's investigation, the CSLC was concerned about the possibility "that some of the government grants in Ontario might have pushed us over."<sup>80</sup>

The U.S. Coalition for Fair Canadian Lumber Imports was disappointed by the ITA's preliminary determination and remained convinced that Canadian softwood lumber products were subsidized.<sup>81</sup> As a result of the preliminary determination, the Coalition had several choices available as to how it wished to proceed. One option was to request a hearing prior to the final determination due in May and to restate its view. A second option was to appeal to the U.S. Court of International Trade within ten days of the publication of the preliminary ruling.

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<sup>78</sup>(cont'd) Lifted, " *Vancouver Sun*, March 8, 1983, p. A1.

<sup>79</sup>Mike Sasges, "U.S. Sleuths Go Into Government's Books," *Vancouver Sun*, March 16, 1983, p. C7.

<sup>80</sup>Rod Nutt, "Firing the Campaign: Masterful Effort Marshalled Facts to Win Lumber War," *Vancouver Sun*, May 26, 1983, p. F8.

<sup>81</sup>"Oregon Foresters Surprised," *Vancouver Sun*, March 9, 1983, p. C6.

The coalition initially chose to pursue both options filing its legal appeal on March 21 and asking for a formal hearing. In its appeal, the coalition requested that the court render a speedy ruling prior to the ITA's final determination date of May 23.<sup>82</sup>

The coalition challenged two of the grounds on which the ITA predicated its ruling: that Canadian stumpage programs are not directed to a specific industry and that Canadian stumpage did not confer an assumption of the costs of production.<sup>83</sup>

It was apparent in the softwood lumber dispute that different U.S federal departments had concerns which led them to take actions in opposition to the goals of the U.S. Coalition for Fair Canadian Softwood Lumber Imports. The U.S Department of Justice and the CSLC both filed motions for dismissal of the coalition's challenge to the ITA's preliminary ruling. The motion for dismissal was granted by Judge Nils Boe on April 13, 1983.<sup>84</sup> The court held that rendering opinions on the preliminary determination would constitute interference in the administration of the ITA as it made its final ruling.<sup>85</sup>

On April 7, another U.S. federal agency indicated that because of its concerns for consumer interests it was opposed to a countervailing duty. The U.S. Federal Trade Commission

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<sup>82</sup>"Lumber Firms Appeal Import Ruling," *Winnipeg Free Press*, March 22, 1983, p. 50.

<sup>83</sup>Jansen, p. 17.

<sup>84</sup>"Judge Rejects Lumber Appeal," *Vancouver Sun*, April 14, 1983, p. F8.

<sup>85</sup>Jansen, p.17.

supported Canada in a brief prepared for an ITA hearing that was eventually cancelled when the petitioners withdrew their request for a hearing.<sup>86</sup>

The Commission's analysis supports the preliminary determination of the Department of Commerce that no countervailable subsidy results from the methods used by Canadian Federal and Provincial governments to set a price for stumpage. . . . As one of the federal agencies charged with promoting competition and consumer welfare, the Federal Trade Commission is concerned that unjustified imposition of countervailable duties on Canadian lumber would raise costs to the United States lumber consumers and adversely affect other segments of the economy including the housing industry.<sup>87</sup>

The final ITA determination differed only slightly from the preliminary ruling. The total value of subsidies involved was still considered to be *de minimus*. Three programs, which were originally thought to provide countervailable benefits, were not included in the final list of subsidy programs: (1) Federal/Provincial Industrial Development Subsidiary Agreements; (2) The Canada/Nova Scotia Forestry Subsidiary Agreement (Sawmill Improvement Component Grants); and (3) Alberta-Timber Salvage Incentive Programs. The ITA found that these programs either were not in use or did not provide subsidies. Five other programs, which were not originally considered to provide countervailable benefits were added to the list of programs

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<sup>86</sup>United States Department of Commerce, International Trade Administration, *Final Negative Countervailing Duty Determinations: Certain Softwood Products from Canada*, (Washington, D.C., May 23, 1983) p. 5.

<sup>87</sup>Federal Trade Commission, *Prehearing Brief: In the Matter of Certain Softwood Lumber Products from Canada, Countervailing Duty Proceedings before the International Trade Administration*, April 7, 1983, p. i.

conferring subsidies.

## *Programs Determined to Confer Subsidies*

1. Federal Programs
  - a. Certain Aspects of the Investment Tax Credit
  - b. Program for Export Market Development
  - c. Forest Industry Renewable Energy Program
  - d. Regional Development Incentives Program - Grants
  - e. Federal Employment Program - Community-Based Industrial Adjustment Program (CIAD)\*
  
2. Federal/Provincial Programs
  - a. Agriculture and Rural Development Agreements (ARDA)
  - b. General Development Agreements
    - 1) British Columbia - Assistance to Small Enterprise Program (ASEP)
    - 2) New Brunswick - Northeast New Brunswick Development Program (NED), Kent Region Pilot Project (KED), and Industrial Development Subsidiary Agreement (SIFAP)
    - 3) Ontario - Eastern Ontario Subsidiary Agreement
  
3. Provincial Programs
  - a. Alberta - Stumpage Payment Deferral
  - b. British Columbia
    - 1) Low-Interest Loan Assistance
    - 2) Stumpage Payment Deferral
  - c. Quebec
    - 1) Stumpage Pricing on Timber Limits\*
    - 2) Aide à la Promotion des Exportations\*
    - 3) Société de Récupération, d'Exploitation et de Développement Forestiers du Québec (REXFOR)
    - 4) Fonds de Relance Industrielle (FRI) Tax Abatement Program
    - 5) Société Développement Industriel (SDI) Export Expansion Program

Source: ITA, *Final Negative Countervailing Duty Determinations*, pp. 2-3.<sup>88</sup>

### An Evaluation of the Countervail Proceedings

The ITA's final determination marked the conclusion of the countervail process since the petitioners did not appeal the ruling. However, the American petitioners were still not

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<sup>88</sup>Asterisked programs were not included among those listed as providing subsidies in the Preliminary Determinations.

satisfied that Canadian stumpage practices did not constitute a subsidy. Even though the U.S. Coalition for Fair Canadian Lumber Imports had decided not to appeal the ITA's final ruling, the coalition attempted to assess the possibilities for further action to obtain their goal of restricting the Canadian share of the market.

The decision not to appeal the final ruling was largely based on financial constraints. The countervail process was enormously expensive for all parties both in terms of financial costs and human resources. The CSLC spent over 4 million dollars and over half of that amount went directly in legal fees for its Washington, D.C. attorneys.<sup>89</sup> Estimates of the cost of the proceedings to the petitioners varied from \$700,000<sup>90</sup> to a figure slightly greater than the CSLC's 4 million.<sup>91</sup> Since the coalition did base its petition in part on the ITC Section 332 study of the Canadian and American industries, it seems most likely that the actual cost of the countervail proceedings to the petitioners was somewhat less than the CSLC's expenses. The lack of support for the countervail action in the U.S. certainly limited the petitioners' ability to raise the funds necessary to continue the case.<sup>92</sup> Canadian producers also raised the funds to cover the costs of the proceedings from within their industry.

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<sup>89</sup>Nutt.

<sup>90</sup>Milliner.

<sup>91</sup>Jansen, p. 14.

<sup>92</sup>Dave Pease, "Coalition Prospects Never Better," *Forest Industries*, July 1986, p. 2.



The CSLC decided not to ask the federal government to contribute to the financial costs of the case, since it was probable that any government assistance would have been added to the list of alleged subsidies.<sup>93</sup>

The CSLC maintained that its victory was directly attributable to the strength of the Canadian case, and that its strategy was based on facts not politics.<sup>94</sup> Canadian analysts who examined the case were interested in determining the factors which contributed to Canada's success, since the softwood lumber case was viewed as illustrative of a strategic approach which could be utilized in other disputes with the United States. These analyses of the countervail proceedings supported the CSLC's contention that the countervail case was won on the merits of the Canadian position rather than by political lobbying. Gordon Jansen stressed that despite the importance of Canadian unity during the dispute the "countervail case was decided on its merits,"<sup>95</sup> while David Leyton-Brown found that "the system worked fairly and was free from political influence."<sup>96</sup>

On the other hand, the American producer's coalition was equally convinced that Canadian lobbying played an important role in the ITA's decision. Soon after the ITA's preliminary

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<sup>93</sup>Jansen, pp. 14-15.

<sup>94</sup>Nutt.

<sup>95</sup>Jansen, p. 19.

<sup>96</sup>Leyton-Brown, p. 56.

decision in March 1983, allegations of Canadian political pressure arose in a letter from the Southern Forest Producers Association circulated among lumber producers and U.S. Congressmen. The letter claimed that the Canadian victory was due to intense political pressure from the Canadian government. According to the head of the Southern Forest Producers Association, the two diplomatic notes and the visits by provincial and federal officials were examples of such pressure.<sup>97</sup> It is clear that the coalition continues to attribute the Canadian victory in part to political lobbying, but their complaint ignores the assistance that they received from the ITC's study of the lumber trade in formulating the countervail petition.

Moreover, the Canadian Industry received valuable support from provincial governments and the Canadian government in the form of lobbying activities and technical assistance.<sup>98</sup>

The legislative framework, which determines the procedures under which a U.S. countervailing investigation takes place, appears to substantiate the claims of the CSLC that the decision was based largely on the merits of the case. The U.S. Congress has attempted to limit the discretion available to officials in their determinations. In the softwood lumber case for the ITA to decide in favour of the petitioners would have involved an interpretation of statutes that was not supported by domestic

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<sup>97</sup>David Hogben "U.S. Lumbermen Say Politics Interfered," *Vancouver Sun*, May 4, 1983, H5.

<sup>98</sup>Milliner

and international precedents.<sup>99</sup> Since the legislative framework is, in part, shaped by multilateral commitments that both the U.S. and Canada are parties to, it has been suggested that multilateral commitments can work to Canada's advantage in a dispute.

Multilateral commitments and dispute settlement procedures can be an effective means of preventing or resolving bilateral disputes. In the softwood lumber case, the GATT agreements had shaped the remedies available to the U.S. producers under their country's trade legislation.<sup>100</sup>

However, it is important to recognize that the U.S. Congress had an impact on the design of the GATT agreements. It is clear that the outcome of the softwood lumber case did not coincide with the intentions of some Congressmen. Ironically, Canadian producers were able to utilize elements of the system that were intended in the U.S. legislation to be helpful to American producers.

The new U.S. legislation is cast in great detail; accordingly, it offers protection to those producers willing and financially able to pay for the legal skills necessary to work the system."<sup>101</sup>

Canadian success in the countervailing process was not only a result of the impact of multilateral agreements and having the

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<sup>99</sup>Prior to the second countervail inquiry in 1986, the ITA in a ruling on carbon black manufactured in Mexico altered its interpretation of general availability, which encouraged American producers to believe that a 1986 countervail petition would be more successful than was the case in 1982. This American view was supported by the subsequent ITA ruling that subsidies were provided to Canadian lumber producers.

<sup>100</sup>Leyton-Brown, p. 77.

<sup>101</sup>Grey, p. 10.

financial resources necessary to hire skillful legal representation. Other factors that contributed to the Canadian success in the countervail action have to do with the manipulation of the elements of interdependence within the Canadian-American relationship. In the softwood lumber dispute, as in the cases examined by Keohane and Nye:

. . . the political processes of complex interdependence, and more particularly the role of transnational, and transgovernmental actors, lead to a more equal pattern of outcomes in intergovernmental bargaining than one would predict from the overall structure.<sup>102</sup>

Throughout the countervail proceedings, Canadian officials presented a united front and actively sought the support of American groups. The Canadian case was strengthened by alliances with American wholesalers and sectors of the U.S. housing industry. Canada also gained support from federal government departments and agencies who opposed the petitioners due to concerns about U.S. consumer welfare or the implications of a legal appeal of a preliminary decision. Moreover, transgovernmental contacts helped assure that the importance of the softwood case to Canada was recognized and that Canadian producers were given a fair hearing.

Canada's success is partly due to "the intensity and coherence of the smaller state's bargaining position."<sup>103</sup> But,

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<sup>102</sup>Robert O. Keohane and Joseph S. Nye, *Power and Interdependence: World Politics in Transition*, (Boston: Little, Brown and Co., 1977) p. 179.

<sup>103</sup>Keohane and Nye, p. 206.

perhaps as important to Canadian success in the countervail process were the failures of the American producers' coalition. While membership in the coalition increased from twenty percent to thirty percent of U.S. producers during the proceedings, the majority of the American industry never supported the countervail action. The U.S. Coalition for Fair Canadian Lumber Imports was never able to move beyond the limits of its identification with the parochial interests of the Pacific Northwest and small producer to become a truly national organization.<sup>104</sup> The potential ability of the American producers to politicize the issue of Canadian softwood lumber imports and so increase the pressure on the ITA to provide protection was limited by the divisions within the industry. The expectation that a housing recovery would solve the problems in the lumber industry certainly contributed to the lack of national interest in the countervail process. As well, the coalition was hampered by concurrent attempts on the part of some of its members to obtain legislation which would allow firms to cancel economically unviable contracts for U.S. forest service timber.<sup>105</sup>

After the countervailing proceedings commenced, the U.S. Congress was not involved as a supporter of the petitioners.

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<sup>104</sup>Pease, "Coalition Prospects Never Better"

<sup>105</sup>In 1984, the U.S. Congress passed the Federal Timber Contract Payment Modification Act, which provided companies with an opportunity to "turn back contracts upon the payment of a buy-out charge." United States Department of Agriculture, Forest Service, *Report of the Forest Service: Fiscal Year 1985*, February 1986, p. 19.

Although American producers have been able to exert pressure through the Congress on other trade issues, in the softwood lumber dispute the divisions within the industry prevented effective lobbying.<sup>106</sup> In the lumber case, the structure of the U.S. political system worked against the American producers group.

Politicization of issues from below in the United States is carried out by more narrowly based groups, focusing primarily on Congress. The United States public does not consider either Canada or Australia important enough to generate broad, popular movements. As a result, politicization from below in the United States . . . often leads to divisions between Congress - or vocal elements in Congress - and the executive.<sup>107</sup>

The inability of the American producers group to politicize their concerns over the extent of the Canadian market share, ensured the continuing disinterest of the vast majority of Americans. However, the potential cost of a countervailing duty to the Canadian economy was great enough not only to ensure cooperation from all levels of Canadian government and members of the forest industry, but also from the general public. In a larger more diverse U.S. economy, a victory would have provided few economic benefits to anyone other than the U.S. producers. Therefore, Canada was able to make alliances with consumer groups and a large portion of the housing industry, who felt that their interests lay with Canadian producers rather than with the petitioners.

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<sup>106</sup>Joan Edelman Spero, *The Politics of International Economic Relations*, (2nd ed.) (New York: St. Martin's Press, 1981) pp. 88-95.

<sup>107</sup>Keohane and Nye, p. 206.

The failure of the American producers group to politicize the softwood issue so that it became a salient Congressional issue was instrumental in assuring the neutral stance of the Reagan administration during the countervail proceedings. The softwood lumber case showed that Canada could win a dispute under procedures established by the U.S. However, to an extent Canadians were able to successfully utilize their resources in the interdependent relationship because of American heterogeneity and minimal attention to the dispute.

The final chapter presents some conclusions about the softwood lumber dispute, and the interdependence approach. There is also a discussion of the relevance of this study to the 1984-87 period, when there was greater U. S. unity and increased attention to trade issues in general.

## CHAPTER V

### CONCLUSION

This thesis has examined the dispute over Canadian softwood lumber exports to the United States. Due to time and length restrictions the main focus has been on the 1981-83 period, but this final chapter will discuss the relevance of the earlier analysis to later events. In the course of this study we have examined the pattern of trade in lumber between the U.S. and Canada; the structures of the forest industries in both states; the organizations and strategies of both sides of the dispute; and the decisions by the U.S. International Trade Commission (ITC) and the U.S. International Trade Administration (ITA). Canada had its primary success in 1983, when the ITA ruled in its favour and countervailing duties were not levied. But Canada was not completely successful in the dispute, since the ITC's preliminary ruling found that imported Canadian lumber had injured U.S. producers. This thesis has shown that two aspects of the interdependence framework help to explain Canada's 1983 success: the greater heterogeneity in the U.S. compared to the homogeneity in Canada; and asymmetry of attention. In Canada the dispute was viewed as more important and warranting more attention than was the case in the United States.

The interdependence framework postulates that there is a greater homogeneity of interests in Canada as compared to the United States. Canada's 1983 success is partly due to the



intensity and coherence of its bargaining position, and to cooperation among producers, governments, and forestry workers. In Canada an external threat to its main market combined with fewer differences in the structure of the industry made it easier to obtain the support of these actors. Regional variations in government aid to producers did not result in inter-provincial dissension over the issue, and there was no evidence of federal-provincial conflict over how the Canadian defence was conducted nor reservations over the active involvement of provincial governments. However, there were some apprehensions about maintaining Canadian unanimity if the ITA ruled that lumber products were subsidized.

In contrast to Canada, there was little agreement among American producers over the issue of Canadian lumber imports. The potential ability of American producers to politicize the issue of Canadian softwood lumber imports, and indirectly put pressure on the ITA to provide protection, was limited by the lack of cohesion within the industry. The U.S. Coalition for Fair Canadian Lumber Imports was never able to evolve beyond its identification with the parochial interests of small, pacific northwest producers to become a truly national organization. While membership in the coalition increased from twenty to thirty percent of American producers during the proceedings, the majority of firms never supported the countervail action. The expectation that a housing recovery would solve the problems of the lumber industry contributed to the lack of national interest

in the countervail process. Concurrent attempts by its members to obtain legislation which would allow firms to cancel economically unviable federal timber contracts also hampered the coalition's ability to gain support for its goals. The U.S. producers' coalition was unable to present the issue of Canadian imports as one that transcended traditional divisions in the industry.

The heterogeneity of the American industry was reflected in the varying positions of the federal government. In part, these differences are due to the divergent interests of American consumers and lumber producers arising from the fact that the U.S. is both a major lumber producer and consumer. Restrictions on Canadian lumber in 1983 would have increased the cost of softwood products to homebuilders and probably raised the price of homes to consumers. Congressmen from Oregon, Washington, and Maine were generally supportive of the U.S. Coalition for Fair Canadian Lumber Imports and assisted it in gathering the necessary information to file a countervailing duty petition by requesting that the International Trade Commission conduct an investigation into Canadian lumber imports. However, there was no evidence of wide support within the Congress for restrictions on Canadian lumber, since the issue was regarded as a purely regional problem and western officials could not agree on how to solve the industries' problems. If there had not been significant divisions within the Pacific Northwest, then it might have been possible to gather congressional support for

some action against Canadian lumber through a process of trade-offs and log-rolling. The neutral attitude of the Administration and the limited involvement of the U.S. Congress was important to Canada in that it provided an environment in which the question of Canadian subsidies could be considered in a quasi-judicial manner and the case decided on its merits according to U.S. law.

Both the divisions within U.S. lumber industry, and the conflicting interests of American producers and consumers contributed to Canada's ability to acquire U.S. allies. The interdependence framework draws attention to the significance of the alliances that Canada formed with American groups and the ties that already existed between producers in both states. It is evident in this instance that transnational organizations and alliances improved rather than weakened Canada's position. The term transnational is used to refer to "interactions across the border in which at least one actor is nongovernmental."<sup>1</sup> Canada gained support from U.S. federal government departments and agencies who opposed the petitioners due to concerns about American consumer welfare or the implications of a legal appeal of a preliminary ruling by the International Trade Administration. Also, meetings involving Canadian provincial and federal representatives and U.S. officials helped to assure that

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<sup>1</sup>Robert O. Keohane and Joseph S. Nye, Jr. "Introduction: The Complex Politics of Canadian-American Interdependence," *Canada and the United States: Transnational and Transgovernmental Relations*, (eds.) Annette Baker Fox, Alfred O. Hero, Jr., and Joseph S. Nye, Jr. (New York and London: Columbia University Press, 1976) p. 4.

the importance of the softwood issue to Canada was recognized and that Canadian producers were given a fair hearing.

In addition to U.S. heterogeneity, asymmetry of attention was also a major factor in the dispute. Little attention was paid to the issue of Canadian imports in either American lumber journals or in the general media, and aside from elected officials from lumber producing areas, few politicians appeared to be aware of the dispute. By comparison, the issue was reported on regularly in British Columbia, and consistently but less frequently in the rest of Canada. Although there was a deliberate attempt to minimize statements by elected officials in Canada which might be construed as political pressure, Canadian politicians treated the dispute as important and were actively involved in the defence. Both federal and provincial politicians visited Washington, D.C. and discussed their concerns with U.S. federal officials. The issue first surfaced during a tense period in Canada-U.S. relations, as the recently elected Trudeau and Reagan administrations asserted conflicting national objectives. However by November 1982 when the formal countervail investigation started some contentious issues had been partially resolved and tensions had eased. In British Columbia, where the softwood lumber dispute was a major concern, there was no provincial election until after the ITA's preliminary ruling.

This analysis of the lumber dispute indicates that other factors not included in Keohane and Nye's interdependence

approach are also important to an understanding of the conflict. Contributing to Canada's success was the validity of the case it presented before the ITA. Canada's position was supported by evidence and in accordance with the precedents established under U.S. trade law as well as international agreements. Another element not fully considered by Keohane and Nye is the costs incurred in these bilateral conflicts. During the countervail proceedings the Canadian defence spent over four million dollars, which was raised from contributions by lumber producers to avoid further allegations of government subsidy. Moreover, the defence required a major commitment of governmental and industry time and manpower. The 1984-87 period of the dispute was even more expensive than the first countervail investigation had been. The CSLC was estimated to have spent over seven million dollars primarily for attorney fees.<sup>2</sup> Even though the U.S. coalition also had substantial legal expenses, its total costs were lower, because of ITC investigations, which provided it with the basic information needed to file both countervailing duty petitions. Nevertheless, one of the difficulties American producers faced was the problem of raising the funds necessary to adequately finance their case. The lack of widespread support for the countervailing action and particularly the limited participation of the large forest firms affected the ability of the U.S. coalition to raise funds. In Canada, the involvement of large producers ensured the availability of the financial

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<sup>2</sup>J. F. McCracken, Executive Director Canadian Lumbermen's Association, "Where Do We Go From Here?", *Canadian Forest Industries* in *B.C. Lumberman*, January 1987, p. B23.

resources necessary to hire the expensive legal and technical expertise needed.

However, the most important feature of the case which the Keohane and Nye framework does not account for is the ongoing nature of the dispute. Despite its apparent settlement in 1983, like some other bilateral conflicts, the lumber dispute was revived at a later date. Canada's chances for being successful decreased as the issue continued into the mid-eighties and the issue became more visible and important to the United States. The cost of the countervail process increases over time as does the possibility that an issue may be 'taken over' by other events, for example, in the lumber case, the Canada-U.S. free trade agreement. The ongoing nature of the lumber conflict raises doubts as to whether Canada is as successful as Keohane and Nye have concluded. Whether or not Canada is seen as winning a particular conflict may be a product of when the dispute is viewed as beginning and ending. If the softwood lumber conflict is perceived as starting in 1981 and ending in 1987 then Canada achieved only a partial victory. However, if the 1984-87 period is viewed as a separate conflict then the 1983 period ended with a Canadian victory. In Keohane and Nye's win-loss tabulation, would the earlier Canadian success then effectively cancel the 1987 defeat? If so, the benign nature of the interdependent relationship may be overstated.

## The Relevance of this Study to the 1984-87 Period

The conclusions reached as a result of the analysis of the 1981-83 period can also be examined in relation to the events which led to the Canada-U.S. agreement that imposed a fifteen percent export tax on Canadian lumber. In the aftermath of the ITA's 1983 final ruling that Canadian softwood lumber was not subsidized, the dispute appeared to have ended, and between May 1983 and August 1984 there was no mention of the issue in either lumber journals or the general news media. Immediately prior election of Brian Mulroney as Canadian Prime Minister the lumber issue re-emerged, just as it appeared that the bilateral relationship was heading towards a new period of closeness and cordiality.

The renewed American attention on Canadian lumber was directly attributable to Canada's growing market-share as new housing starts in the U.S. increased. In 1984, the import issue was raised by southern U.S. lumbermen not western producers.<sup>3</sup> The increasing Canadian market-share was attributed to a large extent to a high U.S. dollar and Canadian productivity gains, but whatever its cause, Canadian imports were blamed for the fact that rising lumber sales had not returned prices to their

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<sup>3</sup>John C. Milliner Jr., "As Imports Increase, U.S. Industry Mobilizes," *Forest Industries*, January 1985, p. 31; and William R. Ganser Jr, "U.S. Needs Trade Policy to Compete with 'Giveaway' Canadian Timber," *Forest Farmer*, July/August 1985, pp. 20-21.

pre-recession values or increased company profits.<sup>4</sup> In the 1985-87 period, divisions within the U.S. industry substantially diminished and almost all American producers agreed on the desirability of obtaining some type of relief from Canadian lumber imports.<sup>5</sup> In August 1985 the U.S. Coalition for Fair Canadian Lumber Imports was reorganized with a much broader base of support.<sup>6</sup> An estimated seventy percent of American producers joined the U.S. Coalition for Fair Lumber Imports (CFLI) a substantial increase over the previous groups thirty percent membership. American producers continued to argue that Canadian provincial stumpage practices constituted a subsidy, despite the ITA's 1983 ruling. For many producers the issue of whether or not Canadian practices were allowable under trade laws was less significant than Canada's growing share of the American market.<sup>7</sup> One indication of the increasing agreement within the industry about Canadian lumber was the decision by the National Forest Products Association (NFPA) to support restrictions on Canadian lumber.<sup>8</sup> During the 1981-83 period the NFPA had remained neutral and its decision to support restrictions caused

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<sup>4</sup>"Overall Economy Looks Okay, But Lumber's Woes Persist," *Forest Industries*, July 1985, p. 25.

<sup>5</sup>Grif Griffin, "Coalition Gains Clout on Lumber Import Issue," *Forest Industries*, July 1986, pp. 28-29.

<sup>6</sup>"Lumbermen Organize Against Imports Again," *Forest Industries*, August 1985, p. 7.

<sup>7</sup>"U.S. Northwest Cool to 15 Per Cent Tariff on Canadian Lumber," *Globe and Mail*, October 28, 1986, p. B19.

<sup>8</sup>"Lumber Vote Slaps Canada," *The Province*, May 16, 1985, p. 23.



problems within the organization as its Canadian members considered resigning.<sup>9</sup> A second indication of the new cohesiveness of American producers was the decision of several American divisions of multi-national firms with Canadian branches to support the countervail effort.<sup>10</sup>

The differences in Canadian and U.S. attention to the lumber dispute, which had characterized the 1981-83 period, diminished during the 1985-87 period. With a resolution of the problem of federal timber contracts in the pacific northwest, Canadian lumber became the major topic in lumber journals and at producer meetings. Coverage of the Canadian lumber issue increased dramatically from 1984 to 1987. In the 1981-83 period there were eight articles on Canadian lumber imports in *Forest Industries*, compared to forty-six articles between 1985 and May 1987. During this period *Forest Farmer*, which had not reported on the earlier dispute, had two articles on the issue. To an extent the increase in media coverage may be due to the outcome of the 1983 countervail case and to the passage of time, since one aspect of asymmetry of attention is the longer time it takes for the U.S. to become aware of issues involving Canada than the reverse.

The CFLI initially focused its efforts on the U.S. Congress where it sought to have either direct restrictions placed on Canadian lumber or to have the trade laws defining

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<sup>9</sup>Dave Pease, "Import Issue: More Polarization," (editorial) *Forest Industries*, January 1986, p. 2.

<sup>10</sup>Griffin, p. 28-29.

countervailable subsidies re-written to cover provincial stumpage practices.<sup>11</sup> Lumber imports gained more federal and Congressional notice in the U.S. when the issue was linked to a number of trade disputes with Canada and other countries.<sup>12</sup> During this period the American trade deficit was growing, as were protectionist feelings, and Canada had the largest trade surplus with the U.S. after Japan.<sup>13</sup> The lumber issue gained national attention in the U.S. when it was linked with Senate approval of a fast-track approach to negotiations on a free-trade agreement with Canada.<sup>14</sup>

### Canadian Response

While divisions within the U.S. industry decreased after 1984, in Canada the 1985-87 period was marked by increasing heterogeneity. British Columbia disagreed with the federal government's decision to participate in a series of formal discussions with the U.S. about lumber in 1986.<sup>15</sup> However it was not until the 1986 countervail petition was filed that real

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<sup>11</sup>Jean Sorensen, "U.S. Launches Three-Pronged Attack on Canadian Wood," *Canadian Forest Industries*, August 1985, pp. 25-26 & 28.

<sup>12</sup>"Raw Deal on Trade," *The Province*, May 5, 1985, p. 10.

<sup>13</sup>Roger Newman, "U.S. Protectionist Mood on Rise," *Globe and Mail*, May 29, 1985, p. B5; and "Members Seek Initiative on Trade Fever," *Congressional Quarterly: Weekly Report*, September 14, 1985, pp. 1793-1795.

<sup>14</sup>Jennifer Lewington, "US Senators Approve Trade Talks," *Globe and Mail*, April 24, 1986, pp. A1 & A8.

<sup>15</sup>"B.C. Cool On Lumber Envoys," *Vancouver Sun*, May 16, 1986, p. B1.

dissension between producers, provinces, and the federal government over the handling of the dispute emerged. Initially, there was not much concern over the possibility that the ITA would rule that provincial stumpage charges provided a subsidy to Canadian lumber producers. Canadian producers were primarily frustrated at the prospect of another round of investigations because they felt that the issue had been settled in 1983.<sup>16</sup> The prevailing lack of concern discounted the impact of a recent U.S. court decision which changed the way the ITA would be interpreting the general availability principle cited in the 1983 ruling.<sup>17</sup> During the ITC and ITA investigations Canadian producers would again be represented by the Canadian Softwood Lumber Committee (CSLC), which had become the Canadian Forest Industries Council.

The 1982-83 consensus among producers, labour, and governments over what the Canadian strategy during the investigation would be was less evident. For example, Jack Munro, head of the western Canadian branch of the International Woodworkers of American (IWA), discussed alternative approaches to the dispute which had not been considered during the 1982-83 period. These included reviewing stumpage rates, pursuing the possibility of a negotiated settlement, and Canadian producers suspending any attempts to increase their present U.S.

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<sup>16</sup>Vaughn Palmer, "Lumber Wars: A Battle Rejoined," *Vancouver Sun*, June 21, 1985, p. A4.

<sup>17</sup>The countervail petition cited the court decision relating to carbon black from Mexico, as a sufficient basis for a new investigation of Canadian softwood lumber. See Griffin, p. 28.

market-share.<sup>18</sup> Munro argued that changes in the U.S. since the 1983 decision necessitated a different approach, but his statements were condemned producers and governments. Due to their pressure the union agreed to back the federal government's request to speak with unity on the issue.<sup>19</sup> Munro's statement and the reaction it provoked proved to be a precursor of the different positions that would develop between producers, provinces, and the federal government during the course of the countervail investigation. Producers on the whole continued to advocate pursuing the legal options, a position which Ontario supported. Other lumber producing provinces and the federal government argued that Canada should cut its losses and negotiate the best agreement it could. In hindsight, Munro appears to have had a clearer understanding of the changes in the American political and economic environment since 1983 than Canadian producers and governments.

The understanding in 1982-83 that the trade dispute would not be treated as a domestic political issue dissolved when lumber became entangled with the Canadian-American free trade negotiations.<sup>20</sup> As it became evident that the Canadian case was in trouble, particularly after the U.S. decided to apply tariffs on Canadian cedar shakes and shingles, inter-provincial

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<sup>18</sup>"United Front Vital on Lumber Issue," (editorial) *The Province*, June 8, 1986, p. 24.

<sup>19</sup>Jennifer Hunter, "U.S. Softwood Duties Opposed by Coalition," *The Globe and Mail*, June 14, 1986, p. B5.

<sup>20</sup>Vaughn Palmer, "Squabbling Ill Serves B.C.'s Cause." *The Vancouver Sun*, May 21, 1986, p. B4.

dissension increased, as well as criticism of the federal government's handling of the dispute.<sup>21</sup>

Despite the greater homogeneity of U.S. interests during the 1986 countervail investigation, some American groups continued to support the Canadian position including U.S. housing industry organizations; consumer associations; lumber wholesalers; and a group of American petrochemical, timber, and agricultural companies.<sup>22</sup> Drawing on the earlier Canadian example the U.S. producers coalition attempted to gain Canadian allies by publicizing its view that lumber producers were overcutting Canadian forests.<sup>23</sup> These allegations were reported in B.C., but received minimal national coverage<sup>24</sup>

#### *Divergence in the Approach to the Dispute*

By 1986, the recognition of Canadian dependence on the U.S. market caused a divergence from the earlier approach to the lumber dispute. It had become clear, that the American approach to trading issues was changing due in part to the "relative demise of the United States as an international economic power in recent years".<sup>25</sup> From the neo-realist view interdependence

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<sup>21</sup>Brian Kieran, "Tories Were Naive in Lumber Dealings, Turner Charges," *Vancouver Sun*, October 17, 1986, p. A12.

<sup>22</sup>"'War Parties' Gather," *The Province*, June 30, 1985, p. 35; and Patrick Durrant, "American Groups Stump Against Bill," *The Province*, October 20, 1985, p. 48.

<sup>23</sup>Griffin, p. 28-29.

<sup>24</sup>"Overcutting Alleged," *The Province*, July 10, 1985, p. 18.

<sup>25</sup>David G. Haglund, "Unbridled Constraint: the Macdonald

was now a constraint on Canada's options and Washington's increasing awareness of Canada was not necessarily a positive development for Canadian economic interests.<sup>26</sup> As American attention to the lumber issue increased the dispute was handled on a more traditional state to state basis than in 1983.

During the countervailing proceedings British Columbia's Premier Bill Bennett, who had opposed negotiations throughout the dispute, resigned. The new Premier, Bill Vander Zalm appeared more willing to consider a negotiated settlement, and announced that the provincial government would review stumpage practices. U.S. producers were pleased with the announcement of the review, but they were not willing to withdraw or delay the countervail petition as the B.C. government had hoped.<sup>27</sup> Later, critics charged that this move had contributed to the ITA's ruling that provincial stumpage practices constituted a subsidy.<sup>28</sup> Immediately before the ITA was due to announce its preliminary ruling, the Canadian Trade Minister, Pat Carney made an offer of a self-imposed tax on Canadian lumber exports. This offer, which was refused, also created dissension and was blamed

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<sup>25</sup>(cont'd) Commission Volumes on Canada and the International Political Economy," *Canadian Journal of Political Science*, Vol. 20, No. 3 (September 1987) p. 607.

<sup>26</sup>Ibid., p. 602 & 621.

<sup>27</sup>"U.S. Lumbermen Unswayed," *Vancouver Sun*, September 9, 1986, p. A1.

<sup>28</sup>"Lumber Fury Flies," *The Province*, October 17, 1986, p. C5; and "Vander Zalm to Blame for Tariff, Broadbent Claims", *Vancouver Sun*, October 17, 1986, p. A3.

for the ITA's decision.<sup>29</sup>

On October 22, the ITA issued its preliminary ruling and a fifteen percent duty was imposed on Canadian lumber. In reaching its decision, the ITA cited changes in the interpretation of the general availability principle in its ruling that provincial stumpage rates were a countervailable subsidy.<sup>30</sup> American producers were pleased with the initial ITA ruling but were unhappy with the rate since they had asked for a twenty-seven percent duty.<sup>31</sup> The ITA's ruling marked the end of any appearance of unanimity in Canada. While Canadian lumber industry spokesmen condemned the duty, some producers and labour representatives suggested that they could live with the tariff and that it could have been much worse.<sup>32</sup> Initially, the Canadian government announced that it would appeal the ITA's ruling to the GATT. This decision had the support of producers and the Ontario government, which reiterated its opposition to a

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<sup>29</sup>Christopher Waddell and Jennifer Hunter, "Americans Turn Down Price Deal of Lumber," *Globe and Mail*, October 11, 19 1986, p. A1.

<sup>30</sup>International Trade Administration, Department of Commerce, *Preliminary Affirmative Countervailing Duty Determination: Certain Softwood Lumber Products from Canada* as published in *Federal Register (Notices)*, October 22, 1986 (Vol. 51, No. 204), p. 37455.

<sup>31</sup>"Tariff Ruling 'Makes Day' of SFPA Committee," *Forest Industries*, December 1986, p. 9.

<sup>32</sup>Brian Martin, "Carney Got the Best Deal," *B.C. Lumberman*, March 1987, p. 76; Richard Holmes, "Export Charge: Industry Says No to Stumpage Adjustments", *B.C. Lumberman*, June 1987, p. 337; and Andrew Ryder, "Effects of the Tariff on Canadian Producers," *Forest Industries*, January 1987, p. 30.

negotiated settlement.<sup>33</sup> Ontario, which produced only five percent of the lumber shipped to the U.S., was concerned about the precedent a negotiated settlement might make, and its implications for Canadian sovereignty.<sup>34</sup> On the other hand, B.C., the largest exporter of lumber to the U.S., indicated that it would consider imposing its own tax to avoid the duty and to keep any taxes collected in the province.<sup>35</sup>

The agreement negotiated at the last minute between the U.S. and Canada provided for a fifteen percent export tax and the withdrawal of the countervail petition. The notice of termination was to state that the ITA's preliminary ruling was without legal force or effect, and Canada was to withdraw its appeal to GATT.<sup>36</sup> The negotiated settlement was viewed by the B.C and federal governments as a success since it provided that the tax would be collected in Canada rather than in the U.S., and because they felt that it would eliminate the precedent established in the ITA's preliminary ruling.<sup>37</sup> Critics of the agreement, including lumber producers and the Ontario

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<sup>33</sup>Don Whiteley, "Forest Firms Get \$60 Million Break on Wood Exports to the U.S.," *Vancouver Sun*, October 23, 1986, p. C6; and "Ontario Opposes Compromise," *Vancouver Sun*, October 21, 1986, p. C1.

<sup>34</sup>"Peterson Blasts Protectionism," *Vancouver Sun*, November 25, 1986, p. A6.

<sup>35</sup>"B.C. Tax on Lumber Considered," *Vancouver Sun*, October 21, 1986, p. C1.

<sup>36</sup>*Memorandum of Understanding*, included with *Statement on Softwood Lumber Settlement by the Honourable Pat Carney, Minister of International Trade*, (Vancouver, January 5, 1987).

<sup>37</sup>*Statement On Softwood Lumber*, p. 2.



government, felt that Canada could have won the issue on appeal to GATT and that negotiations established a dangerous precedent.<sup>38</sup>

Since the fifteen percent export tax was imposed in January 1987, there have been a few preliminary discussions of its impact, but at this point the main source of information on its effects are a number of studies conducted during the countervail investigation. These studies attempted determine what impact different levels and types of trade restraints on lumber would have in the U.S. and Canada. When the impact of a fifteen percent countervailing duty was examined, most of the studies concluded that there would be some loss of jobs in Canada and an increase in the prices of new homes in the United States. One 1987 report estimated eventual job losses in Canada at 1000, while other studies by the Canadian industry put potential job losses at 10,000 to 15,000.<sup>39</sup> In 1985, it was estimated that in the long run restrictions could reduce exports by at least one-third.<sup>40</sup> The impact of the Canadian export tax on the U.S. has been a matter of contention. One study suggested that only Oregon, Georgia, Alabama, and Mississippi would gain sawmilling jobs, and the overall result would be a net loss of up to 13,000

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<sup>38</sup>Kimberley Noble, "Forest Council is Outraged by Ottawa's reversal," *Globe and Mail*, November 22, 1987, p. B3.

<sup>39</sup>"Canadians Move Quickly to Adjust Stumpage Fees," *Forest Industries*, March 1987, p. W6; and John Clarke, "Tackling Contracting Out", *B.C. Lumberman*, April 1987, p. 165.

<sup>40</sup>Sorensen, p. 25.

American jobs.<sup>41</sup> Another analysis concluded that the eventual beneficiaries of the export tax would be U.S. timber owners in the south and west rather than American lumber producers.<sup>42</sup> Part of the difficulty in determining the impact of the export tax is that in 1986, Canadian lumber exports declined as a result of the IWA strike in B.C. In 1987, with a strong housing market in the U.S. American analysts have suggested that the export tax did not have a major impact on Canadian market-share.<sup>43</sup> However, B.C. producers argued that a combination of changes in provincial stumpage charges, a stronger Canadian dollar, and the export tax was having a negative impact on lumber sales in U.S. and eastern Canada.<sup>44</sup>

Keohane and Nye's interdependence framework has proven to be of use in examining the softwood lumber dispute between Canada and the United States. Canada's success in 1983 can be attributed to heterogeneity of interests in the U.S. versus Canadian homogeneity and to asymmetry of attention. However, other factors also played a significant role in the dispute including the validity of the Canadian case according to U.S. trade regulations. The expenses involved in a dispute are

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<sup>41</sup>Ted Blackman, "Canadian Logs Cheaper, But Would a Tariff Help?" *Forest Industries*, January 1986, pp 32-33.

<sup>42</sup>"Tariff May Increase U.S. Stumpage Prices," *Forest Industries*, May 1987, p. 7.

<sup>43</sup>"Records Fall as 1986 Production Figures Tallied," *Forest Industries*, April 1987, p. 7.

<sup>44</sup>"Export Tax A Boon to U.S. Lumber," *Vancouver Sun*, November 7, 1987, p. C3.

substantial even when Canada is successful in obtaining its goals, and the costs of a dispute become more onerous if an issue is prolonged. Keohane and Nye's analysis of Canadian-American relations is limited in that it ignores the costs of disputes. This study of the softwood lumber dispute has illustrated some of the difficulties involved in examining ongoing conflicts within the interdependence framework. The re-emergence of the dispute in 1984 and the 1987 agreement indicates that when the U.S. does decide to devote more attention to a contentious issue, Canada's chances of success are greatly diminished.

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