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CANADA

SOFTWOOD LUMBER AGREEMENT BETWEEN CANADA AND THE UNITED STATES

Report of the Standing Committee on International Trade

**Hon. Mark Eyking
Chair**

JUNE 2016

42nd PARLIAMENT, 1st SESSION

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THE STANDING COMMITTEE ON INTERNATIONAL TRADE

has the honour to present its

SECOND REPORT

Pursuant to its mandate under Standing Order 108(2), the Committee has studied the Softwood Lumber Agreement between Canada and the United States and has agreed to report the following:

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SOFTWOOD LUMBER AGREEMENT BETWEEN CANADA AND THE UNITED STATES

INTRODUCTION

Canada's forest sector is an important contributor to the nation's economy and is the primary source of economic activity in many regions of the country. As with many other sectors of Canada's economy, international trade is vital to the economic health of Canada's forest sector. In 2015, Canada's forest products exports totalled \$32.9 billion. In that year, softwood lumber exports accounted for 26.1%, or \$8.6 billion, of this total.¹ The largest export market for Canadian softwood lumber is the United States, where it is mostly used to build houses.²

On 18 February 2016, the House of Commons Standing Committee on International Trade ("the Committee") decided to undertake a study on the [Softwood Lumber Agreement Between the Government of Canada and the Government of the United States of America](#) (SLA), which came into force in 2006 and expired on 12 October 2015.

As part of its study, the Committee held two hearings in spring 2016 to hear from Canada's forest sector stakeholders about the impact that the SLA has had on the sector and to determine the steps that the Canadian government should consider taking now that the agreement has expired.

This report provides information on the topic studied, summarizes the evidence heard by the Committee and makes recommendations to the federal government.

BACKGROUND

During the most recent Canada–U.S. softwood lumber dispute, which began in the early 2000s, U.S. softwood lumber producers alleged that the prices charged to Canadian softwood lumber producers by provincial governments for the right to harvest timber on provincial Crown lands – known as stumpage rates or fees – were too low and constituted a subsidy that benefited Canadian softwood lumber producers and harmed U.S. producers.³ In 2002, the U.S. Department of Commerce responded to a petition submitted by a group of U.S. softwood lumber producers by imposing countervailing duties (CVDs) and anti-dumping duties (ADs) on shipments of Canadian softwood lumber to the United States.⁴

1 These data are based on Statistics Canada, [Canadian International Merchandise Trade Database](#), accessed through [Trade Data Online](#), 19 May 2016.

2 Natural Resources Canada, [Forest products and applications](#), 2016.

3 Peter Berg, [The Canada-U.S. Softwood Lumber Dispute](#), Publication No. TIPS-98E, Parliamentary Information and Research Service, Library of Parliament, Ottawa, 10 June 2004.

4 Softwood lumber exports from the Atlantic provinces were excluded from the CVDs but not from the ADs.

These duties were revoked when Canada and the United States concluded the SLA in 2006. The agreement included the following provisions:

- revocation by the United States of the CVDs and ADs that it had applied on softwood lumber imports from Canada, and an agreement by the United States to not impose CVDs or ADs for the duration of the agreement;
- the return to Canadian producers of US\$4.4 billion of the estimated US\$5.4 billion in CVDs and ADs that had already been collected by the U.S. government on softwood lumber imports from Canada;⁵
- the option for Canadian provinces subject to the SLA to choose either an export tax on softwood lumber exports to the United States, or a quota and an export tax at a lower rate.⁶ The export tax rate and quota values depended on the price of framing lumber. When the price exceeded US\$355 per thousand board feet, no export taxes or quotas applied to Canadian exports; and
- the establishment of a binding dispute-settlement process, and a final dispute-settlement body comprised of three commercial arbitrators appointed by the London Court of International Arbitration (LCIA).

The SLA expired on 12 October 2015, its original seven-year term having been extended by an additional two years following joint agreement by Canada and the United States. In accordance with Article XVIII of the SLA, the United States may not initiate CVD or AD investigations with respect to softwood lumber shipments from Canada to the United States for one year following the expiration of the agreement. This period will expire on 12 October 2016.

On 10 March 2016, Prime Minister Trudeau and President Obama directed their ministers to submit a report within 100 days on the “key features that would address the issue.”⁷

CANADIAN SOFTWOOD LUMBER EXPORTS

As shown in Figure 1, the value of Canadian softwood lumber exports to the United States dropped sharply in the years after the SLA came into force in 2006 before recovering in recent years. Between 2006 and 2009, a period during which U.S. housing starts were declining, the value of these exports fell from \$7.2 billion to \$2.4 billion before rising to \$5.9 billion in 2015. The value of Canadian softwood lumber exports to other

5 Daowei Zhang, *The Softwood Lumber War: Politics, Economics, and the Long U.S.–Canadian Trade Dispute*, Resources for the Future, Washington, 2007, p. 233.

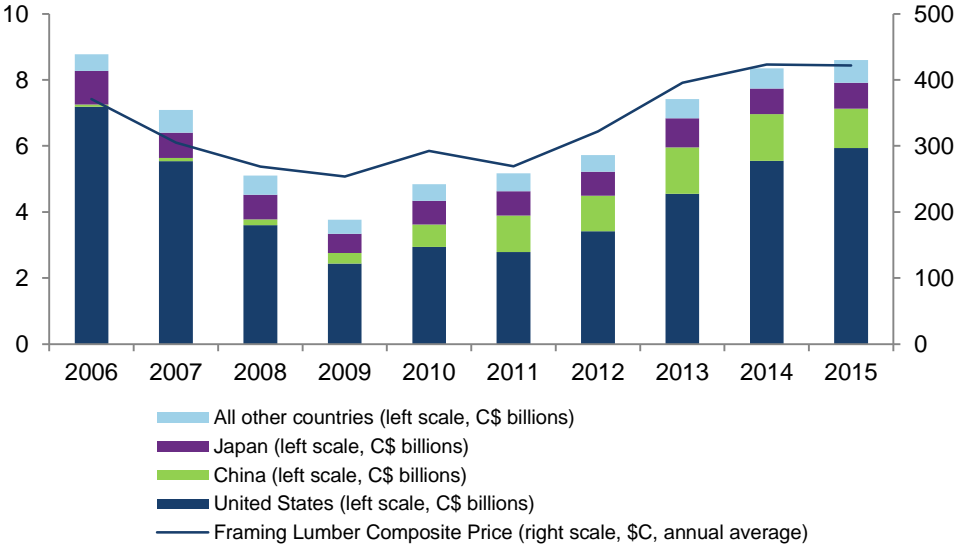
6 Softwood lumber producers in British Columbia, Alberta, Saskatchewan, Manitoba, Ontario and Quebec were subject to the provisions of the SLA signed in 2006. Regarding British Columbia, two regions were identified – B.C. Coast and B.C. Interior – and each region could choose between the two options.

7 Prime Minister of Canada, [Fact Sheet: Canada – United States: Neighbours, Partners, Allies](#), 10 March 2016.

countries remained relatively stable over the 2006–2015 period, other than a sharp increase in the value of exports to China starting in 2010.

The value of Canadian softwood lumber exports to the United States during the period covered by the SLA appears to be correlated to the framing lumber composite price, which in turn is largely dependent on the strength of the U.S. residential construction sector. Fluctuations in the framing lumber composite price over the 2006–2015 period are also shown in Figure 1.

Figure 1 – Value of Canadian Softwood Lumber Exports, By Destination, and Average Annual Framing Lumber Composite Price, 2006–2015



Note:

The framing lumber composite price is an overall measure of the prices of framing lumber consumed in the United States. These prices, which are in U.S. dollars, were converted to Canadian dollars using US\$–C\$ historical annual exchange rates.

Sources:

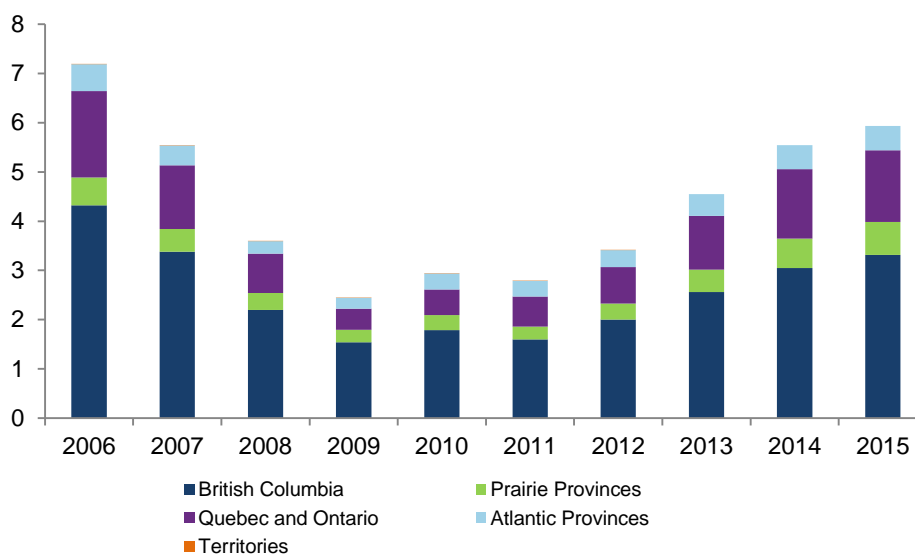
Statistics Canada, [Canadian International Merchandise Trade Database](#), accessed through [Trade Data Online](#), 19 May 2016.

Random Lengths, [Random Lengths Framing Lumber and Structural Panel Composite Prices, by month](#), 29 April 2016.

Bank of Canada, [“Foreign exchange rates in Canadian dollars, Bank of Canada, annual \(dollars\),”](#) CANSIM (database), accessed 20 May 2016.

Of the \$7.2 billion in Canadian softwood lumber exports to the United States in 2006, 60.1% was from British Columbia; in 2015, this proportion was 55.8%. Moreover, in 2015, Quebec and Ontario, the Prairie provinces and the Atlantic provinces accounted for 24.5%, 11.4% and 8.3% of Canadian softwood lumber exports to the United States, respectively; no exports from the territories were reported in 2015. Figure 2 presents the regional distribution of Canadian softwood lumber exports to the United States from 2006 to 2015.

Figure 2 – Value of Canadian Softwood Lumber Exports to the United States, By Province/Territory, 2006–2015 (\$ billions)



Source: Statistics Canada, [Canadian International Merchandise Trade Database](#), accessed through [Trade Data Online](#), 19 May 2016.

IEWS EXPRESSED BY BRITISH COLUMBIA’S FOREST SECTOR STAKEHOLDERS

British Columbia’s forest sector stakeholders told the Committee that the province’s softwood lumber producers have expended a great deal of energy in recent years to reduce their dependence on the U.S. market. [Susan Yurkovich](#), President of the B.C. Lumber Trade Council, said that the province’s exports to China have risen substantially over the past decade due to a partnership with Natural Resources Canada and the Province of British Columbia. Added to these exports to China are exports to other Asian countries, such as Japan. However, in spite of this effort, due to the proximity of the United States and its extensive use of wood as a construction material, the United States remains the largest market for B.C. softwood lumber, and access to that market is critical for the health of the province’s forest sector.

According to the B.C. forest sector stakeholders who provided testimony to the Committee, the SLA – while not perfect – did provide certainty of access to the American

market. As stated by [Duncan Davies](#), President and Chief Executive Officer of Interfor Corporation, Co-Chair of the B.C. Lumber Trade Council and Co-Chair of the Canadian Lumber Trade Alliance, managing a business that depends on softwood lumber exports is difficult when the rules of access to the world's primary market are unknown. He believed that one of the key benefits of a managed trade agreement with the United States is that it allows businesses to focus on their operations, on the success of their business and on growing their markets. In particular, [Mr. Davies](#) said:

The 2006 SLA provided certainty of access to the U.S. market during one of the worst economic downturns we've seen since the Depression. It encouraged the development of offshore markets and it provided an opportunity for the industries in Canada and the U.S. to work together constructively to grow the market for our products against competing products such as steel, cement, and composites. It allowed companies like mine to make investment decisions about our plants in Canada that have been highly beneficial to the economic viability of those facilities, and to provide greater security of employment for the people employed in our operations. While the 2006 agreement was not perfect, it did provide certainty of access to producers on both sides of the border for nearly a decade.

The Committee heard several times that, without a new SLA with the United States, both countries would once again face trade disputes. According to [Mr. Davies](#), such disputes would weaken B.C.'s softwood lumber sector. More specifically, according to [Ms. Yurkovich](#), having to pay CVDs or ADs in the absence of an SLA could strain the ability of forest companies operating across the country to invest in plants and equipment, or to train and recruit employees.

Regardless of the outcome of the Canada–U.S. negotiations underway for a new SLA, [Cameron Milne](#), Fibre Supply Manager with Harmac Pacific, a company that uses wood chips from softwood lumber mills, stressed the importance of also looking at longer-term solutions to avoid having to negotiate a new SLA with the Americans every five or six years.

As discussed earlier, the SLA allowed the Canadian provinces that were subject to the agreement's export measures to choose either an export tax, or a quota combined with an export tax at a lower rate. The B.C. forest sector stakeholders who appeared before the Committee were unanimous in stating that this option was a good arrangement in that it met the respective needs and interests of the different provinces, and allowed them to adjust to changing circumstances.

That said, based on the evidence heard during the study, it appears that the export tax option benefits British Columbia. As explained by [Harry Nelson](#), Assistant Professor with the Faculty of Forestry at the University of British Columbia, who appeared as an individual, "if you are a small producer and you don't have quota, you cannot access that U.S. market, so there's no benefit to you from that higher price. Under an export tax, if you can cover the cost of production, at least you can get some of that benefit. From my perspective at least, that's why there is a benefit to the tax, even for the smaller producer." [Mr. Milne](#) said that he preferred the export tax for the same reasons.

Regarding the softwood lumber negotiations between the Canadian and American governments, the Committee's witnesses explained that the negotiators must demonstrate

goodwill. [Mr. Nelson](#) said that the involvement of the Canadian prime minister and the American president, and their commitment to lay the groundwork for a new agreement, are a positive development. [He](#) also believed that the current circumstances are conducive to striking a good agreement, stating that: “I think that perhaps some of the American fears that there is this wall of wood that’s going to come crashing down from B.C. or western Canada may have abated, so perhaps there’s some latitude for a reasonable agreement that allows us flexibility such as we had in the past agreement. I feel somewhat encouraged by that.”

[Mr. Davies](#) reminded the Committee that time is running out to reach a new agreement with the United States given the American political cycle and the presidential election taking place in November 2016. He hoped that the elements of a new agreement would be available in mid-June.

Although all of the B.C. forest sector stakeholders appearing before the Committee hoped that a new SLA would be reached as quickly as possible, [Ms. Yurkovich](#) added that if such an agreement could not be reached, the members she represented would be willing to work closely with the Government of Canada and the Canadian forest sector to defend Canada’s forest practices and policies against any trade dispute that the United States may launch.

[Mr. Nelson](#) said it was important for Canada to maintain the flexibility needed to develop policies that do not just meet American objectives, but are also in Canada’s best interests. [He](#) also suggested that a new agreement must not prevent B.C. or other regions in Canada from managing their forests in accordance with new partnerships, such as with Aboriginal communities.

VIEWS EXPRESSED BY CENTRAL CANADA’S FOREST SECTOR STAKEHOLDERS

Some stakeholders in Central Canada’s forest sector viewed the outcomes of the SLA signed in 2006 differently than their B.C. counterparts. These stakeholders believed that the agreement harmed the softwood lumber sector in Quebec and Ontario. Rather than negotiate a new agreement with the United States that would extend managed trade in softwood lumber, most of the Central Canadian forest sector stakeholders said that the Canadian government should instead try to establish free trade in softwood lumber between Canada and the United States, or – at a minimum – between Central Canada and the United States.

[Richard Garneau](#), President and Chief Executive Officer of Resolute Forest Products, stated that the SLA did not provide stability and predictability, and was “incredibly destructive for [C]entral Canada.” He and [André Tremblay](#), President and Chief Executive Officer of the Quebec Forest Industry Council, believed that Canada was winning the arbitrated disputes over softwood lumber with the United States that preceded the SLA signed in 2006. They would have preferred to see Canada continue with the arbitration process that was underway prior to the agreement’s entry-into-force in 2006. As described by Mr. Tremblay, “despite repeated Canadian victories ... the Canadian

government decided to forgo free trade for an agreement designed to offer trade peace and predictability. In hindsight, this alternative proved costly for Quebec's industry."

Both witnesses were particularly critical of the implementation, or rather the lack of any implementation, of Article XII of the SLA,⁸ an article that they said was never properly applied. According to [Mr. Tremblay](#), Quebec instituted a new stumpage system in 2013 to exempt its softwood lumber producers from the border measures in the SLA. Under the new system, "timber volumes from the public forests are traded directly through auction or re-allocation." Both Mr. Tremblay and [Mr. Garneau](#) said that Quebec's new system is market-based and complies with the changes sought by the United States.

[Mr. Garneau](#) and [Mr. Tremblay](#) said that the Province of Quebec and its softwood lumber producers repeatedly asked Canada's federal government to begin verifying Quebec's new system under Article XII of the SLA but never received a response. To prevent such a situation from reoccurring, [Mr. Tremblay](#) said that a new agreement should include a mechanism enabling a province to have its stumpage system assessed based on the changes it has made.

[Mr. Tremblay](#) told the Committee that Quebec's new stumpage system has resulted in higher prices for Quebec timber, making it some of the most expensive in North America. He said that Quebec producers have borne the financial consequences of this new system since they had to continue complying with the SLA.

[Mr. Tremblay](#) summed up the Quebec forest sector's argument by stating: "Quebec cannot afford to enter into a new agreement that will restrict downstream access to the U.S. market, while constraining its upstream fibre supply by a substantial increase in supply costs."

[Mr. Garneau](#) also cited the Ontario softwood lumber sector as an example showing the compliance of Central Canada's softwood lumber producers with Canada's international trade commitments. He told the Committee that, in 2005, a *North American Free Trade Agreement* (NAFTA) panel determined that softwood lumber producers in Ontario were not subsidized and should therefore be excluded from the CVDs collected by the United States on softwood lumber from that province before the SLA came into force.

[Mr. Garneau](#) gave two other reasons why a new SLA based on managed trade could be more harmful for softwood lumber producers in Central Canada than in British Columbia: Central Canada's producers do not benefit from the ease of access that B.C. producers have to the Asian market; and B.C. producers bought about 40 sawmills in the United States in recent years, insulating them somewhat from possible future U.S. border measures.

8 Article XII provided for the establishment of a Working Group on Regional Exemptions to be tasked with developing "substantive criteria and procedures for establishing if and when a Region uses market-determined timber pricing and forest management systems." Once these criteria were developed by the Working Group, the regions in Canada that satisfied the criteria and were subject to the agreement's export measures would have been able to exempt their softwood lumber from these measures.

According to [Mr. Garneau](#), removing restrictions on log exports could be used as a bargaining chip to provide Central Canadian softwood lumber producers with free access to the U.S. market as these restrictions are a major irritant for the United States.

[Kevin Edgson](#), President and Chief Executive Officer of Eacom Timber and member of the Canadian Lumber Trade Alliance, presented a different opinion about the possibility of establishing free trade in softwood lumber between Canada and the United States, arguing that although free trade is a “fantastic principle,” it is also impractical. To illustrate the risks of not renewing the SLA or negotiating a new agreement, [he](#) urged the Committee to look at the current dispute over supercalendered paper.⁹

[Mr. Edgson](#) did concede that Canada should not sign an SLA at any cost: “What I am not sure about is whether the counterparty is interested in being reasonable. If they are not, then we have to go down the path of protecting our industry against a sovereign attack.”

The Committee was told that, if a new SLA is not signed, a new dispute over trade in softwood lumber could occur. [Mr. Tremblay](#) said that, if that were the case, Canada’s federal government could support the Canadian softwood lumber sector by providing guaranteed funding to help pay the duties that could be imposed by the United States.

Although some Canadian softwood lumber stakeholders warned that such legal battles could be costly, [Mr. Garneau](#) suggested that managed trade also had a cost, referring to the export taxes paid by the Canadian softwood lumber sector.

[Mr. Garneau](#) was of the opinion that NAFTA could serve as a legal framework for the trade in softwood lumber between Canada and the United States, as is the case for most other goods traded between the two countries. According to [him](#), “just about every industry enjoys free trade in North America [under NAFTA], except for softwood lumber.” However, [he](#) conceded that, in the past, NAFTA panels have had difficulty issuing decisions within the deadlines set out in the agreement. In his view, the Canadian government should make sure that NAFTA, including the dispute-settlement system, works.

VIEWS EXPRESSED BY THE ATLANTIC PROVINCES’ FOREST SECTOR STAKEHOLDERS

The Committee also heard from one witness representing the Atlantic provinces’ softwood lumber producers. [Gaston Poitras](#), Chairman of Atlantic Lumber Producers, stated that more than 50% of the Maritimes provinces’ timber supply comes from private lands. He also said that stumpage rates from Crown timber in the Maritimes are based

9 On 30 March 2016, Canada requested formal consultations with the United States under the World Trade Organization’s dispute-settlement procedure regarding CVDs imposed by the United States on supercalendered paper imports from Canada. Supercalendered paper is a type of paper mechanically processed to make it smooth and shiny. Canada alleges that the CVDs, and the investigation on which these duties are based, are inconsistent with the World Trade Organization’s *Agreement on Subsidies and Countervailing Measures* and *General Agreement on Tariffs and Trade 1994*.

according to the market value of timber harvested in those provinces. Mr. Poitras stressed that the Maritimes are constantly improving the surveying methods to ensure that the data used for setting stumpage rates are as accurate and up-to-date as possible.

[Mr. Poitras](#) also said that the Maritime provinces were excluded from the border measures in the SLA that was signed in 2006.¹⁰ He claimed that, over the last 35 years of softwood lumber trade disputes between Canada and the United States, neither the United States Trade Representative nor the U.S. Department of Commerce has ever alleged that softwood lumber production in the Maritimes is subsidized because a substantial share of the Maritime provinces' lumber comes from private lands.

[Mr. Poitras](#) suggested that Canada should try to reach a new SLA, but argued that – since most of the Maritime provinces' forest land is privately owned and these provinces continue to improve their system for setting Crown stumpage rates – softwood lumber from the Maritime provinces should continue to be excluded from the softwood lumber export measures in a future agreement.

CONCLUSION

Based on the evidence heard as part of its study of the SLA between Canada and the United States, the Committee believes that the interests of Canada's softwood lumber producers and other forest sector stakeholders around the country are best served by the Canadian and American governments quickly agreeing on the parameters of a new SLA between the two countries. This agreement should reflect not only the interests of Canadian forest companies, but also those of the workers that these companies employ, and the communities in which the companies operate.

However, the importance of quickly reaching an agreement with the United States does not mean that the Canadian government should forego proper consultations with the various stakeholders likely to be affected by a future SLA; such an agreement must be in the best interest of all forest stakeholders across the country. These consultations should include stakeholders that may have been overlooked in the past, such as Aboriginal stakeholders.

The Committee believes that a future SLA with the United States should adequately reflect the stumpage systems in the Canadian provinces, and ensure that softwood lumber from provinces where stumpage systems reflects market forces are excluded from border measures that would limit Canadian softwood lumber producers' access to the U.S. market.

As well, the Committee noted significant differences in forestry management, and the way in which the softwood lumber sector is structured, across the country. Accordingly, a future SLA with the United States needs to be flexible, and – in relation to export measures – needs to give the various regions subject to these measures the ability to choose a formula suited to their particular circumstances.

10 In the SLA, "Maritimes" refers to the four Atlantic provinces.

Accordingly, the Committee recommends:

Recommendation 1

That, on a priority basis and as soon as possible, the Government of Canada establish the parameters of a new softwood lumber agreement with its American counterpart. The agreement should reflect the best interests of Canadians.

Recommendation 2

That the Government of Canada ensure that its consultations regarding the negotiations for a new softwood lumber agreement with the United States include stakeholders that may have been overlooked in the past, especially Aboriginal stakeholders and small producers.

Recommendation 3

That the Government of Canada insist that provinces with market-based stumpage systems be excluded from any border measures in a future softwood lumber agreement with the United States if such measures limit softwood lumber exports from these provinces.

Recommendation 4

That the Government of Canada insist that a future softwood lumber agreement with the United States be flexible and provide – to the regions of Canada that would not be excluded from the border measures included in a future agreement – options regarding export duties or volume restraints.

Recommendation 5

That, in the future, the Government of Canada evaluate the options in relation to a long-term solution with respect to Canadian softwood lumber trade with the United States. As part of the evaluation, the government should explore measures that would enhance export opportunities in other markets.

APPENDIX A LIST OF WITNESSES

Organizations and Individuals	Date	Meeting
<p>Atlantic Lumber Producers Gaston Poitras, Chairman</p> <p>Quebec Forest Industry Council André Tremblay, President and Chief Executive Officer Michel Vincent, Director, Economics Markets and International Trade Branch</p> <p>Resolute Forest Products Karl Blackburn, Director, Canadian Public Affairs and Government Relations – Canada Richard Garneau, President and Chief Executive Officer Seth Kursman, Vice President, Corporate Communications, Sustainability and Government Affairs</p>	2016/04/12	8
<p>As an individual Harry Nelson, Assistant Professor, University of British Columbia, Faculty of Forestry</p> <p>B.C. Lumber Trade Council Duncan Davies, Co-Chair, BCLT, President and Chief Executive Officer, Interfor Corporation Susan Yurkovich, President</p> <p>Canadian Lumber Trade Alliance Duncan Davies, Co-Chair, CLTA, President and Chief Executive Officer, Interfor Corporation Kevin Edgson, Member, CLTA, President and Chief Executive Officer, Eacom Timber</p> <p>Harmac Pacific Cameron Milne, Fibre Supply Manager</p>	2016/05/03	14

APPENDIX B LIST OF BRIEFS

Organizations and Individuals

Nelson, Harry

REQUEST FOR GOVERNMENT RESPONSE

Pursuant to Standing Order 109, the Committee requests that the government table a comprehensive response to this Report.

A copy of the relevant Minutes of Proceedings ([Meetings Nos. 8, 14, 25 and 26](#)) is tabled.

Respectfully submitted,

Hon. Mark Eyking
Chair

Supplementary Opinion New Democratic Party of Canada

The New Democratic Party of Canada (NDP) is pleased that the Standing Committee on International Trade (Committee) undertook a study of the Softwood Lumber Agreement (SLA) between Canada and the United States.

Canada and the U.S. have a long history of trade disputes over softwood lumber. Before the 2006 SLA, the U.S. was applying massive countervailing duties (CD) and anti-dumping duties (AD) which caused significant job losses in Canada. Canada had won a series of tribunal warnings under CAFTA, NAFTA, and the WTO which found that U.S. tariffs were unjustified.

Many questioned the need for a negotiated agreement given that these tribunals consistently found Canada was not unfairly subsidizing its producers. The 2006 SLA, which was renewed in 2012, hurt Canadian exports and did not adequately address the significant regional differences in the Canadian forestry sector. It took \$50 million from Canadian industry to create a system under which the U.S. was able to bring actions against Canada as part of the billion dollars given away under the deal.

The Committee heard from witnesses who acknowledged that while technically an SLA should not be needed, the absence of an agreement would hurt Canadian exporters and expose them to even more costly litigation. Witnesses also said that any new SLA must be flexible and provide options to regions regarding export duties or volume constraints.

Witnesses testified that it is important that changes in forestry management practices are taken into account during the negotiations and throughout the life of the agreement. We heard that a new agreement should include exemptions for provinces with market-based regimes and stronger provisions to review changes in stumpage systems or other practices during the life of the deal.

The NDP is concerned by reports that talks between Canadian and U.S. negotiators have stalled and that our forest sector may face a new round of unfair trade measures with impacts on Canadian companies and workers.

The NDP urges the government to secure a deal that respects the significant regional differences in Canada's forestry sector and that protects Canadian jobs. We also urge the federal government to put forward a broader vision for supporting Canada's forestry sector, which provides tens of thousands of good jobs and has high growth potential.

