

NON-CONFIDENTIAL VERSION

In the LCIA
No. 81010

THE UNITED STATES OF AMERICA,

Claimant,

v.

CANADA,

Respondent.

UNITED STATES POST-HEARING BRIEF

TONY WEST
Assistant Attorney General

JEANNE E. DAVIDSON
Director

Of Counsel:

TIMOTHY M. REIF
General Counsel
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508
UNITED STATES

JOAN E. DONOGHUE
Principal Deputy Legal Adviser
United States Department of State
2201 C Street, N.W.
Washington, D.C. 20520
UNITED STATES

PATRICIA M. McCARTHY
REGINALD T. BLADES, JR.
Assistant Directors
CLAUDIA BURKE
Senior Trial Counsel
MAAME A.F. EWUSI-MENSAH
GREGG M. SCHWIND
DAVID S. SILVERBRAND
ANTONIA R. SOARES
STEPHEN C. TOSINI
Trial Attorneys
United States Department of Justice
Commercial Litigation Branch
Civil Division
1100 L Street, N.W.
Washington, D.C. 20530
UNITED STATES
Tel: +1 (202) 514-7300
Fax: +1 (202) 514-7969
national.courts@usdoj.gov;
Patricia.McCarthy@usdoj.gov

October 15, 2009

Attorneys for Claimant,
The United States of America

TABLE OF CONTENTS

	<u>Page(s)</u>
INTRODUCTION	1
LIABILITY	6
I. Canada Failed To Rebut Or Even To Address Clear Evidence Of Liability	6
A. Canada’s Interpretation And Application Of “Non-Discretionary” Are Illogical	7
B. Canada’s Theory Of What Constitutes A “Forest Management Measure” Is Far Too Broad And Unsupported By The Evidence	11
1. Cost-Reimbursement Programs Are Not “Forest Management”	13
2. Quebec’s Silvicultural and Fire/Pest Control Measures Are Not “Forest Management” Under Any Part Of The Anti-Circumvention Provision	19
C. Canada Ignores The Difference Between “ Administered” And “Existed”	22
1. Administered	23
2. Existed	24
REMEDY	27
I. The SLA Requires Full Compensation For All Portions Of The Breach	29
II. Canada Must Remedy All Consequences Of Its Breach	34
A. The Remedy Must Be Tied To The Breach	35
B. The Amount Of Benefits Includes All Of The Consequences Of The Breach	38
1. Ontario Programs	40

2.	Quebec Programs	47
C.	Canada Misinterprets The Nature Of The Prohibitions In The SLA	50
D.	Canada's Ultimate Quantification of Remedy Is Significantly Undervalued	52
III.	An Appropriate Framework For Determining Remedy	55
CONCLUSION	60

THE UNITED STATES POST-HEARING BRIEF

1. Pursuant to the Tribunal's communication dated August 3, 2009, claimant, the United States, respectfully submits its Post-Hearing brief.

2. This Post-Hearing brief consists of the following sections: (1) an introduction; (2) a discussion of the evidence demonstrating Canada's liability and Canada's failure during the hearing to rebut any of that evidence; (3) an assessment of the testimony addressing an appropriate remedy, including an explanation of the SLA's retroactive remedy provisions and a framework for determining how to quantify the benefits; and (4) a conclusion.

3. Cognizant of the Tribunal's intention that Post-Hearing submissions "are not meant to be repetitions" of earlier briefs but, rather, "assessment[s] of the evidence gathered" during the hearing, Tr. 1068:18-24, this brief focuses upon the evidence marshaled during the hearing held from July 20-24, 2009 — in particular, upon issues still in contention in this proceeding, and upon the Tribunal's questions to the parties during the hearing.

INTRODUCTION

4. In the 2006 Softwood Lumber Agreement ("SLA" or "Agreement"), the parties agreed to a unique scheme to limit exports to the United States, a scheme in which Canada would *collect and keep* export charges from its own softwood lumber exporters, rather than allowing the United States to collect duties from those same exporters under its own trade remedies. For the system to function properly, however, Canada had to agree not to offset or circumvent those export charges. This promise was memorialized in Article XVII of the SLA, the Anti-circumvention provision, which explicitly prohibits Canada from providing grants or other benefits to softwood lumber producers or exporters. This provision states, as a matter of law, that such grants or benefits are considered to offset the export measures.

5. At the hearing, the United States demonstrated with abundant and un rebutted evidence that Canada has breached the Anti-circumvention provision with six distinct government benefit programs that provide grants or other benefits to softwood lumber producers and exporters. Instead of confronting the evidence, or offering competing, exculpatory evidence, Canada ignored the evidence almost entirely and argued only that many of the disputed government programs were the *sort* of programs the parties intended to exempt from the Anti-circumvention provision. Canada did not offer a shred of evidence to support these contentions, but rather made sweeping assumptions about all of the contested provisions of Article XVII.

6. Canada's diversions notwithstanding, on the question of liability, only four issues remain in dispute. Should this Tribunal adopt the views of the United States on these four issues, it will then be uncontested that these programs violate the Anti-circumvention provision. Notably, not all of the issues apply to each program. In fact, with respect to some of the programs, the Tribunal need only answer one question of interpretation or fact to reach a conclusion on liability. Nevertheless, we set forth these four issues together here: (1) is a program "non-discretionary"; (2) is a program a "forest management" program; (3) did it "exist" on July 1, 2006; and (4) was it "administered" on July 1, 2006. To answer each of these questions, Canada relies entirely upon unwritten and unsupported assumptions about the purpose of the Anti-circumvention provision, or upon interpretations of the provision that contradict the ordinary meaning of the terms of the Agreement.

7. In contrast, during the hearing, the United States relied upon the unambiguous terms of the Anti-circumvention provision, combined with concrete, documentary proof, to demonstrate that Canada had breached the SLA through the six contested programs.¹

8. The ordinary meaning of the Anti-circumvention provision, read in the context of the SLA as a whole, is clear. As a general matter, Canada agreed in the SLA to abide by a largely self-policing system of assessing and collecting export charges in exchange for the United States abandoning its domestic trade remedies *and* returning the approximately \$5 billion in cash deposits being held as a result of those trade remedies.² Because Canada administers, collects, and keeps the export charges assessed on its lumber exporters, the Anti-circumvention provision exists to prevent Canada from thwarting the effect of the Agreement and returning the export charges to the producers and exporters who paid the charges in the first place. This makes

¹ During the hearing, Canada contended that there are actually nine programs in dispute, not the six that the United States identified. Tr. 132:19-22. The United States identified each of the programs based upon the manner in which Ontario and Quebec announced them:

1. The Ontario Forest Sector Prosperity Fund;
2. The Ontario Forest Sector Loan Guarantee Program;
3. The Ontario Forest Access Road Construction and Maintenance Program;
4. The Quebec “Forest Management Measures” (comprising the road cost reimbursement program, silvicultural benefits, and relief from paying for pest control and firefighting costs);
5. The Quebec Capital Tax Credit; and
6. The Quebec Forest Industry Support Program (“PSIF”)

Canada contends that Quebec’s self-titled “Forest Management” measures are actually four distinct programs. Tr. 159:19-160:3. Whether the Tribunal considers there to be nine or six categories of breach is irrelevant to the question of whether the evidence demonstrates breach.

² Canada called “preposterous” the United States’ characterization of the approximately US \$5 billion dollars in returned cash deposits as “consideration” for the promises made in the SLA. Tr. 1176:8. Canada fails to acknowledge that the return of the deposits was a central part of the Agreement. Instead, Canada contends that the United States was legally obligated to return the money. As the United States demonstrated during the hearing, there was no final judgment requiring the United States to return the money. Tr. 1093:11-1094:12. Indeed, if there had been, the parties hardly would have included the requirement in the SLA, or included the settlement of claims in Annex 2A.

practical sense. If the export charges are part of a scheme to limit Canadian exports and encourage a certain balance of lumber shipped to the United States, returning the export charges to the payors would undermine the purpose of the scheme.

9. The very terms of the provision demonstrate this, explaining that “grants or other benefits” “*shall be considered* to reduce or offset the Export Measures.” SLA, art. XVII ¶ 2 (emphasis added). In other words, when there is a grant or other benefit provided by Canada to a softwood lumber producer or exporter, it *shall* be considered to reduce or offset the export measures, without any inquiry or relevance whatsoever about the effect or impact. This *per se* rule is subject to limited exceptions intended to grandfather certain programs already in existence when the SLA was being negotiated.

10. Canada has interpreted this language and its exceptions in such a way as to eviscerate any meaningful protections. To identify just a few examples, in Canada’s view, so long as Canada characterizes a program as “forest management,” the program is permissible even though it provides benefits and even though there exists no evidence showing the program to be forest management. Similarly, as long as Ontario awards a grant or loan guarantee to all program applicants, Canada deems the program to be “non-discretionary,” and therefore permissible, despite the uncontroverted evidence that Ontario officials can and did exercise discretion to deny or to allow all or part of a requested grant or loan guarantee. Finally, conflating what it means to “exist” with what it means to “administer,” Canada refuses to acknowledge that certain programs were not able to disburse funds until *after* July 1, 2006, and therefore cannot be said to have been administered on or before that date.

11. Canada’s position on remedy suffers from the same flawed assumptions that permeate its liability defenses. As a threshold matter, Canada interprets the language in Article

XIV, the dispute resolution provision, to allow Canada to breach without consequences as long as it ceases breaching after the Tribunal issues its Award. Canada has yet to offer any interpretation that would explain why the United States would have agreed to forgo its trade remedies so that Canada could breach without repercussion. Instead, Canada attempts to draw similarities to the World Trade Organization (“WTO”) Dispute Settlement Understanding (“DSU”) and the North American Free Trade Agreement (“NAFTA”) — similarities that simply do not exist.

12. As a substantive matter, Canada mistakenly assumes – again, without any basis in the Agreement – that to be entitled to a remedy, the United States must demonstrate that the breach offset the export measures or otherwise adversely affected U.S. producers. Nothing in the Agreement contemplates, much less requires, such showings. In fact, the Agreement contemplates the opposite. The Anti-circumvention provision states, as a matter of law, that Canada will have breached if it provides a grant or other benefit to a softwood lumber producer or exporter. In other words, the breach itself is the awarding of benefits that the parties *have already determined* reduce or offset the export measures. The United States need not show that grants or benefits have reduced or offset the export measures, nor show an effect upon U.S. producers. Rather, the United States need demonstrate only the existence and amount of benefit so that the amount of benefit can be recouped in the form of adjustments to the export measures. The breach is the providing of a grant or other benefit, not the effect that the grant or other benefit has upon the export measures, U.S. producers, or the U.S. market.

13. Although the parties disagree about how to quantify the benefits provided, one thing is clear — the amount collected by a remedy must represent, at the very least, the amount of financial benefits provided by the breaching programs. As lumber expert Tom Beck

explained, an appropriate remedy should do more as well. It should also account for the proximate consequences of the breach. Regardless of whether the Tribunal limits the remedy to financial benefits provided by the programs or includes all benefits attributable to the programs, the Anti-circumvention provision contemplates that those benefits, and not the effect of the breach on United States producers, should serve as the basis for any remedy.

LIABILITY

I. Canada Failed To Rebut Or Even To Address Clear Evidence Of Liability

14. As stated above, regarding liability, the issues in dispute were considerably narrowed during the hearing. They are:

- **What is the ordinary meaning of “non-discretionary,”** read in light of the term’s context in the Anti-circumvention provision, and are the two Ontario grant and loan guarantee programs non-discretionary?
- **What is a “forest management measure,”** and are road cost reimbursement programs (in Ontario and Québec), Québec’s silvicultural credits, and Québec’s assumption of costs traditionally borne by the industry, part of “forest management” simply because Canada has labeled them so in these proceedings?
- **What does it mean for a program to have “existed” prior to July 1, 2006,** and did the Québec road cost reimbursement program and Québec Capital Tax Credit “exist” before July 1, 2006 despite lack of legislative assent?
- **What does it mean for a program to have been “administered” prior to July 1, 2006,** and was the Ontario road cost reimbursement program “administered” prior to that date despite being unable to disburse funds until after July 1, 2006?

15. As demonstrated below, Canada continued to offer increasingly illogical interpretations of the plain terms of the Agreement and almost entirely ignored the evidence demonstrating breach of the Anti-circumvention provision.

A. Canada's Interpretation And Application Of "Non-Discretionary" Are Illogical

16. The parties agreed in the SLA that, even if a program provided a grant or benefit to a softwood lumber producer or exporter, it would not circumvent the SLA if, among other things, it was provided "on a non-discretionary basis." SLA, art. XVII ¶ 2(b) ("exception 2(b)"). Consistent with its ordinary meaning, "non-discretionary" means the absence of the opportunity to exercise judgment when evaluating applications for benefits under any given program. Tr. 26:8-11; 1103:22-1104:4. When program officials are called upon to make judgments based upon subjective criteria and to make recommendations, program benefits are conferred on a discretionary basis, and the exception does not apply. Tr. 26:11-15.

17. Indeed, Canada conceded that the exercise of discretion requires "the exercise of judgment." Tr. 25:12-14 (citing Rejoinder ¶¶ 137-38); *see also* Tr. 150:10-11 (stating program officials "make judgments based on legal criteria"). Canada even relied upon the Black's Law Dictionary definition of "administrative discretion," defining the term as "[a] public official's or agency's power to exercise judgment in the discharge of its duties." RA-27; Tr. 1103:25-1104:4.

18. Canada's concession and its authorities notwithstanding, Canada continued during the hearing to advance a convoluted definition of "discretionary," arguing that it means "decision-making subject to *reasonable* constraints." Tr. 1191:3-5 (emphasis added); Rejoinder ¶ 129. In Canada's view, a decision can be non-discretionary even when the decision maker has the choice to apply or to disregard certain criteria. Canada's definition is unlike any dictionary definition advanced by either party. *See* Stmt. Defence, ¶ 111 (discussing R-25; R-26; R-27); *see also* Tr. 25:14-26:3.

19. After creating and advancing its own unsupported interpretation of the term, Canada then applied that flawed interpretation to the evidence. Canada contended that the only

relevant program evaluation criteria were the threshold eligibility criteria (or “mandatory criteria”) because the remainder of the criteria – which Canada deemed “supplementary” – were never used. Canada concluded, without evidence or explanation, that these “supplementary” criteria were never used because the programs were “undersubscribed.” Tr. 151:9-12; Tr. 1195:1-20.

20. However, Canada did not cite a single piece of evidence to support its position that the subjective criteria were never used, nor any evidence to support its position that the subjective criteria would never be used. That is, Canada has not argued that the criteria are irrelevant or superfluous or cannot influence the decision whether to grant the application. Rather, Canada appeared to contend that the subjective or “supplementary” criteria might be used at some time in the future, under different circumstances. For example, in Canada’s view, then, a program is non-discretionary when it is undersubscribed, and suddenly becomes discretionary if oversubscribed. Tr. 1195:5-20. This position is untenable.

21. Not only did Canada’s definition become increasingly confused as it was applied to the facts, it was wholly inconsistent with the purpose of exception 2(b). Both Canada and the United States agreed that exception 2(b) was intended to exclude known quantities — programs whose existence and form were known on July 1, 2006, and the benefits of which were guaranteed. Tr. 16:1-11; 148:13-18. The exception makes logical sense as it would be difficult to quantify on any given date the amount of benefits that might be provided under a discretionary program.

22. During the hearing, Canada contended that the very nature of the program changes depending upon how many companies have taken advantage of it, effectively positing that the program allows discretion but that discretion is not currently being exercised. There is

CONFIDENTIAL

no basis to conclude that a program can be non-discretionary one moment and discretionary the next. It is illogical to conclude that administrators can extinguish discretion that has been admittedly authorized by the program. This would effectively mean that any program would be rendered non-discretionary simply by virtue of the decision maker declining to exercise discretion (which is itself, an exercise of discretion). The manner in which officials exercise their discretion is not the issue; the issue is the discretion created and provided by the program. And, notably, Canada has offered no evidence to support its contentions regarding how the program actually functions.

23. In any event, the record establishes that Ontario program officials were required to exercise discretion — and did *in fact* exercise discretion — during the application review process. *See* Tr. 32:20-24 (discussing C-15); Tr. 1102:15-1103:4 (discussing C-1, Att. AJ; C-1, Att. AU; C-4; C-12; C-13; C-14; C-63-69 (Kalt Hrg. Binder Tabs 8-12, 15-17)).³ Indeed, when faced with clear evidence of discretionary decisions, Canada’s expert, Dr. Kalt, was forced to concede the point.

24. During his cross-examination, Dr. Kalt was presented with several Ontario Ministry documents demonstrating the internal decision making process involved in disbursing funds under the Ontario grant and loan guarantee program. For example, when questioned about the [] project file, Dr. Kalt agreed that the Minister was presented with three options: (1) []

]; (2)

³ During the hearing, Dr. Kalt testified regarding a series of documents that he considered in his reports. The Tribunal determined that these documents “were made part of the record when Professor Kalt referred to them as materials considered . . .” Tr. 827:9-13. Nevertheless, these documents do not have exhibit numbers. For ease of reference, we refer to them in this brief both with newly assigned Claimant Exhibit numbers (C-63 – C-69) and with the tab numbers used in the hearing binders referred to by Dr. Kalt and Mr. Schwind.

CONFIDENTIAL

[

; or (3)]

] Tr. 810:7-21 (discussing C-63 (Kalt Hrg. Binder Tab 8)). Dr. Kalt then agreed that the Minister chose from these options based upon the recommendations from program officials. Tr. 811:1-5.

25. Similarly, regarding the [] application, Dr. Kalt agreed that the Minister was presented with a choice of options before deciding what combination of grant and loan guarantee to approve. Specifically, when asked “from your review of the files Dr. Kalt, would you agree that this is what the minister would typically see when he’s exercising his discretion and whether or not which option to pick,” Dr. Kalt responded, “This is one of the things he was presented with.” Tr. 820:14-21 (discussing C-65 (Kalt Hrg. Binder Tab 9)).

26. Again, when discussing the [], Dr. Kalt agreed that the Ministry’s employees presented three options for consideration: (1)

Tr. 840:9-19 (discussing C-68 (Kalt Hrg. Binder Tab 15)). Dr. Kalt also agreed that the Ministry recommended that the Minister offer a [

Tr. 841:1-14. Dr. Kalt then agreed that the Ministry decided to offer a package *different from that recommended*. *Id.* Specifically, the Ministry made a [

]. *Id.* In

other words, the Ministry’s own documents demonstrate that the Minister was presented with various options and could either choose one of them or create his own package of benefits. This

ability to exercise individual judgment is the essence of discretionary decision making. *See* RA-27 (defining “administrative discretion”).

27. In a last ditch effort, Canada contends that this program is simply not the type of program the parties intended to exclude from the “safe harbours,” contending, without any attribution, that “the 2(b) safe harbour is designed to protect government grant programs,” Tr. 1192:9-10, and that the United States’ interpretation of “non-discretionary” would preclude the “normal government grant program” from satisfying exception 2(b). Tr. 1192:8-16. Canada has not explained what a “normal government grant program” is, but even if the Ontario programs were “normal government grant programs,” they are still subject to the limitations placed upon them by the terms of the SLA.

B. Canada’s Theory Of What Constitutes A “Forest Management Measure” Is Far Too Broad And Unsupported By The Evidence

28. Even if programs provide a benefit to a softwood lumber producer or exporter, they will not be considered to offset or reduce the export measures if they are “provincial timber pricing or forest management systems as they existed on July 1, 2006” SLA, art. XVII, 2(a) (“exception 2(a)”).

29. The programs will also not be considered to offset or reduce the export measures if they are actions taken “for the purpose of forest or environmental management . . . provided that such actions or programs do not involve grants or benefits that have the effect of undermining or counteracting movement toward the market pricing of timber.” *Id.* at 2(c) (“exception 2(c)”).

30. “Forest Management” is not defined in the SLA. However, Canada’s own documents comprehensively define the term. According to Ontario’s 2004 Forest Management Planning Manual, “forest management” is defined as follows:

Generally, the practical application of scientific, economic and social principles to *the administration and working of a forest for specified management objectives*; more particularly, that branch of forestry concerned with the overall administrative, economic, legal and social aspects, and with the essentially scientific and technical aspects, especially silviculture, protection and forest regulation.

Stmnt. Defence ¶ 126 (quoting R-37 at Glossary-8 (emphasis added)). The Manual also explains that “forest sustainability [is] the primary objective of forest management.” Tr. 42:7-43:5 (discussing R-37 and CD-8); Tr. 1109:21-1110:4 (discussing R-37); *see also* R-47 at ON00074966 (explaining that the purpose of forest management planning is “to direct the harvest, renewal, maintenance, and access operations required to promote the long-term health of the local forest and to provide for a sustainable supply of forest resources”). The Manual defines “sustainability” to mean the “long-term Crown forest health [which is] the condition of a forest ecosystem that sustains the ecosystem’s complexity while providing for the needs of the people of Ontario.” R-37 at 66. Thus, forest management is concerned with ensuring the sustainability of forests *qua* forests — as a sustainable natural resource. According to the evidence, then, cost reimbursements form no part of “forest management.”

31. More specifically, Part B of the Manual sets forth “Forest Management Plan Content Requirements” for forest management plans that are submitted to the provincial government. The requirements all include actions that will be taken by the tenure holders who submit the plans. These plans include an analysis of the site, long term management goals, planned operations (including planned roads and harvest areas), and certification that the planned operations are sustainable. R-37 at 169-70. The plan requirements never mention the government taking over any costs of doing business associated with logging operations.

32. Ignoring its own document’s definition, Canada instead created a novel definition of “forest management” so broad that it would (if applicable) encompass any activity that related

to the Crown Forests. It then applied that flawed definition to conclude that the Ontario and Québec road cost reimbursement programs, as well as Québec's silvicultural benefits and Québec's assumption of other pest control and firefighting costs, are forest management measures that should be exempt from the Anti-circumvention provision. Canada's position is untenable.

1. Cost-Reimbursement Programs Are Not "Forest Management"

33. Canada entirely ignored the extensive evidence from both public and internal government documents explaining that both the Ontario and Québec road cost reimbursement programs were "industry relief programs," Tr. 41:3-11 (quoting C-32 at ON00617898) (Ontario), intended to "enhance the profitability of forest sector activities," C1-U § 6, p. 8 (Québec). Instead, Canada insisted during the hearing that the programs' objectives were beside the point because roads are contained in forests and – taking Canada's position to its logical conclusion – anything involving an activity in the forest is, in Canada's view, part of forest management. *See, e.g.,* Tr. 157:20-158:5.

34. Canada primarily contended during the hearing that the United States was inserting a so-called "purpose test" into the Agreement. In Canada's view, a program's stated objective should be irrelevant to the question of whether a program falls within or outside the forest management exception. Tr. 155:13-156:8; Tr. 1198:7-24. But Canada never explained why this is so, or why it is impermissible for the United States to rely upon Ontario's own public and confidential documents in its analysis of whether the road cost-reimbursement programs constitute forest management. These documents constitute compelling evidence, reflecting Ontario's contemporaneous understanding of the road cost-reimbursement program at the time the policy framework for the program was formulated. This Tribunal should rely on such

contemporaneous evidence – which reflect the reality of the program – rather than the opportunistic theories created and advanced by Canada in this arbitration. Tr. 43:24-44:20 (citing C-33); 1109:3-15. In any event, Canada has never contended that the execution of the programs was in any way divergent or inconsistent with the programs’ stated objectives. Nor has Canada offered any reasonable framework that identifies the nature of the program *without* considering the program’s purpose — to provide the industry relief and to enhance the profitability of forest sector activities.

35. Rather, Canada contended that, when the parties intended to require the demonstration of purpose, they said so explicitly, relying upon exception 2(c), which excludes actions taken “for the purpose of forest or environmental management” from being considered to have offset or reduce the export measures. Tr. 155:24-156:8. But Canada failed to compare sections 2(a) and 2(c). The 2(c) exception makes clear that, when determining whether an action satisfies the exception, it must have been taken for “*the* purpose of forest or environmental management, protection of conservation.” SLA, art. XVII ¶ 2(c) (emphasis added). That is, the inquiry must elicit one purpose and that purpose must be forest or environmental management. In contrast, the exception 2(a) inquiry must simply determine whether something *is* a forest management measure, an inquiry that necessarily includes consideration of the purpose and execution of the program — the program in action. As demonstrated, the evidence establishes that the Ontario and Québec road cost reimbursement programs were intended to enhance, and indeed did enhance, the competitiveness of Canada’s industry.

36. On this point, the Tribunal asked whether, if there are multiple, discernible purposes to a program, there should there be a “dominant purpose” test. Tr. 1111:18-24. When determining whether exception 2(c) applies, the use of the singular “the purpose” contemplates

that the Tribunal should discern whether the program has a single purpose and whether that purpose falls into the exception. If there are multiple purposes, then exception 2(c) by its very terms would not apply.

37. In contrast, when assessing whether a program falls under exception 2(a), if a program were to have more than one stated purpose, the Tribunal should consider whether, on balance, the program is a “forest management” program or some other program. Here, there is no evidence whatsoever that the contested programs are forest management. Canada has merely asserted that they are, without support. The evidence establishes that the programs were industry relief programs intended to enhance profitability.

38. In any event, after castigating the United States for purportedly introducing a “purpose test” into exception 2(a), Canada itself relied upon its own “purpose test” in arguing that the programs constitute forest management. For example, Canada contended that the road cost-reimbursement programs are an integral part of Ontario’s and Québec’s forest management systems because the *purpose* of the programs is to construct and maintain forest roads, which Canada argued is an integral part of forest management. *See* Stmt. Defence, ¶ 172 (“The purpose of the Ontario roads program in FY 2005-06 was to reimburse the [sustainable forest license (“SFL”)] holders for a portion of the costs incurred from maintaining Ontario’s vast multiple use forest roads network on Crown land.”); *see also id.* Stmt. Defence, ¶¶ 132-137, 143, 146, 175, 259 (“the purposes of the road credit – to improve distribution of harvesting areas, improve accessibility of forests for fire-fighting, pest-control, and silvicultural activities, and improve public access to forest resources are those enumerated under the paragraph 2(c) safe harbor”). Of course, in contrast to the myriad documents that demonstrate both the Ontario and Québec

programs' purposes, Canada merely stated, without evidence, that the programs were intended to be forest management measures.

39. Canada then attempted to convince the Tribunal that road cost-reimbursement programs could be forest management programs under the Agreement. Thus, despite the declared competition-enhancing nature of the road cost-reimbursement programs, Canada insisted that forest management includes “not just the tasks involved” but “how the costs and responsibilities for these various tasks are allocated.” Tr. 156:9-21; *see also* Tr. 1199:6-9. However, Canada did not present any evidence to support this definition. For example, Canada referred to the Manual as “a pivotal document for all aspects of forest management planning,” Tr. 418:14-419:3 (discussing R-37), but then failed to identify any part of the Manual stating or even suggesting that forest management includes cost-reimbursements to industry. In fact, when roads *are* discussed in the Manual, no mention is made of cost-reimbursements to industry — only to “planning requirements.” Tr. 43:11-18 (discussing R-37 at A-58-64 and CD-8); Tr. 1109:16-21 (discussing R-37).

40. Similarly, with respect to Québec, Canada contends that the “the express recommendation of the Coulombe [C]ommission” for eco-management of the Québec forests were the genesis of Québec’s assumption of the costs of doing business. *See, e.g.*, Tr. 172:1-15 (discussing Québec’s reimbursement for the cost of building logging roads). This recommendation does not change the reality of the program, which was intended to assume costs normally borne by Québec lumber companies. *See* Tr. 417:13-418:2.

41. Canada essentially asks the Tribunal to presume that a road cost-reimbursement program is a forest management measure simply because logging roads are involved. Under Canada’s theory of “forest management,” then, a province’s assumption of *any* forest industry

costs in any way related to Crown Forests would constitute “forest management.” During the hearing, Canada boldly advanced this broad reading of “forest management” when accusing the United States of “claim[ing] that Canada’s great natural endowment, a large productive forest, is a subsidy.” Tr. 134:7-9.

42. The United States does not contend that Canada’s Crown Forests themselves are grants or other benefits. However, when a cost traditionally borne by softwood lumber producers or exporters is now assumed by the government for the stated purpose of increasing competitiveness and profitability of the lumber industry, such a cost falls outside the forest management sphere and circumvents the SLA.

43. This is fully consistent with the testimony elicited and documents discussed during the hearing. The record shows that forest management is concerned with forest sustainability — not with assuming the forest industry’s costs of doing business. *See* Tr. 42:16-43:10 (discussing R-37 and CD-8 and defining “forest management”); Tr. 1109:21-1110:4 (discussing R-37 and defining “forest management”); *see also* R-47 at ON00074966.

44. In addition, as Mr. Beck explained, the road cost-reimbursement program is not forest management:

While road building itself may be part of a forest management system, Ontario’s road [cost-reimbursement] program is not a road building program. Instead, the program transfers the cost of road building and maintenance to the government. The stated purpose of the program is not to manage the forest but to enhance industry competitiveness by reducing delivered wood costs.

Tr. 416:15-417:7. Mr. Beck also testified that “reimbursement, in my mind, is a separate issue” from forest management activities. Tr. 418:1-2; *see also* Tr. 1112:15-1114:25. Thus, while planning for road building may be part of forest management, the road cost-reimbursement programs do not function as forest management measures; the programs were set up to be, and in

fact, are “industry relief” programs. Tr. 38:10-41:24 (discussing C-33 and C-32); Tr. 1110:20-25; C-, Att. U at § 6, p. 8 (single purpose of so-called “forest management measures” is “[t]o enhance the profitability of forest sector activities.”).

45. Finally, Canada contends that official statements and press releases are not credible evidence for purposes of establishing liability. *See* Tr. 139:15-22 (“The U.S. simply assumes that benefits were provided based, to a large extent, on press releases, statements of government and company officials and statements made by politicians in Parliament and elsewhere. None of these constitute any proof that the provincial programs at issue confer benefits that circumvent the export measures under the SLA.”); *see also* Tr. 139:23-140:7 (discussing the United States Government Accountability Office’s position regarding credibility of politicians’ statements).

46. The experts who were questioned about the credibility of the official statements and press releases – even Canada’s own experts – saw no reason to doubt the accuracy of official statements and government and industry press releases. *See, e.g.*, Tr. 487:7-10 (Beck testimony); Tr. 497:2-12 (Beck testimony); 562:10-564:4 (Reilly testimony); 799.23-800:22 (Kalt Testimony). Indeed, it is difficult to fathom why a large Ontario forest company such as Tembec would “react[] very positively” to a government benefit that it did not expect to actually receive. *See* C-26 (Tembec press release supporting funding announcement).

47. Yet Canada contended during its opening statement and in briefing that it would be inappropriate to rely upon these statements. Tr. 139:15-22; Rejoinder ¶¶ 72-73. But Canada fails to distinguish the types of statements at issue in this arbitration. Canada admits that certain kinds of public statements, depending upon their genesis and publication, can corroborate the existence of a fact. Rejoinder ¶¶ 72-73 (citing RA-85, ¶ 61 (citing *Case Concerning Military*

and Paramilitary Activities in and Against Nicaragua 1986 I.C.J. 14)). Additionally, statements made by high ranking political figures can be of high probative value and can be construed as a form of admission. RA-85 at ¶ 64.

48. Importantly, in this case, all of the statements relied upon by the United States, whether in the form of press releases or official statements by politicians, are corroborated by a wealth of additional internal documentation from the governments of Ontario and Québec. For example, regarding Ontario, the evidence presented by the United States also included Ministry program documents (*see, e.g.*, C-33), including confidential Ministry documents (*see, e.g.*, C-38). Canada has not advanced any reasons why these constitute unreliable evidence regarding benefits.

2. Québec’s Silvicultural and Fire/Pest Control Measures Are Not “Forest Management” Under Any Part Of The Anti-Circumvention Provision

49. Contrary to Canada’s suggestion, in large part made for the first time during the hearing, neither the silvicultural nor pest and fire control programs (and indeed, none of the Québec programs) is subject to exception 2(c) for certain forest or environmental measures. Exception 2(c) is limited to programs “for *the purpose* of forest or environmental management” As discussed earlier and in response to the Tribunal’s question, Tr. 1111:18-24, the use of the singular “the purpose” in the context of exception 2(c) demonstrates that the Tribunal should discern whether the reimbursement program has a single purpose and if that purpose falls into the exception.⁴ Tr. 111:25-1112:13. If there are multiple purposes, then this exception should

⁴ Again, this is not to be confused with exception 2(a), which excepts certain forest management measures from being considered benefits, and which does not mention “purpose.” As demonstrated earlier, the absence of the word “purpose” in exception 2(a) does not mean that the purpose of the program is irrelevant when determining whether the program is a forest management measure. Rather, it is critical. And in any event, although, as the Tribunal noted, a

not apply at all or, at most, Canada must prove that the program's stated purpose is "forest or environmental management" — something Canada has not done. Indeed, the United States and Canada could have drafted the agreement to state "*includes* the purpose of forest or environmental management . . ." if they had intended the provision to exempt any program that had forest or environmental management as one of its many purposes. The parties did not do so.

50. In any event, as previously explained, the *only* articulated purpose of the Québec "Financial Initiatives to Support the Forest Sector," C-1 Att. U at § 6, p. 5, was to "enhance the profitability of forest sector activities." *Id.* at § 6, p. 8. Similarly, with respect to the fire and pest control measures (SOPFIM and SOPFEU), regardless of whether the activities themselves involve "forest or environmental management," the objective of these benefit programs is to relieve softwood lumber companies of costs of doing business. Canada has not identified any evidence indicating that either the singular "purpose" or *any* purpose of Québec's reimbursement of these activities is "environmental or forest management."

51. Finally, Canada does not contest that Québec's \$135 million silvicultural reimbursement program provides a benefit to producers and exporters of softwood lumber. Indeed, these reimbursements simply relieve softwood lumber companies of a cost of doing business — preparing and replanting forest areas after removal of trees. Rather, Canada contends that this program falls within the 2(a) exception for "provincial timber pricing or forest management systems" as they existed on July 1, 2006, because these benefits allegedly began before the cutoff date. However, Canada was unable to meet its burden of demonstrating that these benefits "existed and were administered" before the cutoff date.

program with multiple purposes might require special analysis, here, the programs at issue had only one stated purpose — to enhance industry competitiveness.

52. Specifically, at the hearing, Canada could not explain how its proffered evidence was linked to the initiation of these benefits. Tr. 394:15-412:5. Indeed, Mr. Beck carefully analyzed Canada's evidence and explained that Canada's documents did not establish this link. Tr. 380:15-24; 384:5-385:12; 390:13-393:9; 406:10-407:13. Moreover, given the \$135 million magnitude of this benefit, Québec would certainly have made clear the mechanism used to administer the benefit if benefits had been disbursed prior to July 1, 2006. Moreover, the only documentary evidence that Canada proffers, R-148, Ex. S (an apparent screenshot from a provincial government database and government forms), does not reference the reimbursements announced in the March 2006 Budget Speech. Tr. 399:9-405:15. Likewise, no Canadian official with actual knowledge of the challenged benefit program attempted to introduce or explain the late-filed screen shots and forms. The materials are, therefore, wholly unreliable. Lastly, the Québec ministerial memorandum explained that the new measures involved a "[c]redit granted for gardening works, which was *increased* to 660 \$/ha (an increase of 330 \$/ha)." C1-AD at 15 (emphasis added). Canada has not disputed that the Quebec silvicultural measures provided a benefit to lumber producers.

53. Because the \$135 million in silvicultural credits merely increased previously existing credits, there is no way to determine whether the amounts reflected in the screen shot and forms represent the pre- or post-increase credit. Tr. 394:19-395:6 (including discussion with Tribunal). Accordingly, Canada failed to meet its burden of demonstrating that the \$135 million silvicultural benefit existed and was administered on the July 1, 2006, cutoff date.

C. Canada Ignores The Difference Between "Administered" And "Existed"

54. A program that benefits softwood lumber producers and exporters will nevertheless not be considered a breach if it is provided in the same form and amount in which it

“existed *and* [was] administered on July 1, 2006.” SLA, art. XVII ¶ 2(b) (emphasis added). As a threshold matter, the choice of the July 1, 2006 date by the parties is significant — it was the date on which the parties reached agreement on the framework for the SLA. Tr. 15:18-16:1; 47:21-24; 1095:18-1096:9. Thus, the requirement that programs be administered by July 1, 2006, was not a hyper technical or random requirement, rather, it reflected the terms of the parties’ agreement as it stood on July 1, 2006. *Id.*

55. More importantly, this aspect of the exception has two independent parts. First, the program must have existed on July 1, 2006, and second, it must have been administered on July 1, 2006 in the same form and amount as it existed after the SLA entered into force. Canada conflates these two requirements and, in doing so, destroys any meaning inherent in the terms. Despite the two distinct and independent requirements, Canada contends that the exception does not impose “an independent test of administration.” Tr. 58-59; Tr. 1201:17-20. During the hearing, Canada blurred this distinction even more vigorously than in its briefing. For instance, Canada contended the road cost-reimbursement program was “administered” as soon as program development and preparatory activities commenced. *See* Tr. 159:14-17 (stating that “the *existence* of pre-July 1, 2006 activity on the Ontario Roads Program” “constituted program *administration*”) (emphasis added). Canada’s reading of exception 2(b) is not supported by the text; the exception contains both the terms “existed” and “administered,” each of which requires an independent inquiry. Tr. 1117:21-1118:3.

1. Administered

56. Pursuant to its ordinary meaning, “administered” means “[m]anaged, carried on; dispensed, tendered.” CA-14; Tr. 45:9-15 (quoting CA-14); Tr. 1117:12-18 (substantially same), or (in its present tense) “[t]o manage as a steward, to carry on, or execute . . .” and “[t]o

dispense, furnish, supply, or give (anything beneficial or assumed to be beneficial, to the recipient . . .).” Tr. 45:9-15 (quoting CA-14); Tr. 1117:12-18 (substantially same). The ordinary meaning of the term “administered,” then, is dispensing or supplying something beneficial to a recipient. Tr. 45:16-18; 1117:19-21.

57. Based upon the ordinary meaning of the term “administered,” Ontario’s road cost reimbursement program was not “administered” until after July 1, 2006, when the Ministry made program benefits available to the public for the very first time. Three key pieces of evidence demonstrate Ontario’s inability to reimburse costs under the program until July 14, 2006, at the earliest.

58. Ontario’s ability to issue reimbursements is first reflected in the July 14, 2006 email from the Ministry of Natural Resources to forest companies and District Managers, that attaches a July 12, 2006 letter stating that the Ministry was “pleased to officially rollout the 2006/07 Road Construction and Maintenance Funding Program for implementation.” Tr. 45:22-47:20 (discussing C-3131 at ON00617796); Tr. 1116:18-22 (same). The program could not have been “administered” until the program had been officially “rolled out,” prospective beneficiaries notified, and program benefits made available for distribution. In other words, the program could not have been “administered” in the same form and amount as on July 1, 2006, if the amounts were not authorized for release until after that date.

59. Second, along with the July 14, 2006 email, the Ministry distributed, for the very first time, the documents required to obtain reimbursements under the program: the legal agreement form and the invoice form — both of which were required to apply for and to claim reimbursements under the program. Tr. 45:22-47:20 (discussing C-31 at ON00617793-617809,

617810-812). The program was not being administered, and could not have been administered, prior to the availability of the necessary new form and agreement released on July 14, 2006.

60. Third, the “2006-07 Road Program – Final Summary & Request for Comments” issued the following year expressly stated that “[t]he 2006-07 program was officially rolled out on July 14, 2006.” Tr. 47:12-20 (discussing C-34 at ON00617951); 1117:2-4 (discussing same).

61. Canada fails to address any of these critical documents. Rather, Canada contends that the Ontario program “existed” prior to July 1, 2006, and, therefore, was administered prior to that date simply by virtue of its existence. Tr. 153:1-154:12. A program cannot be administered if the core goal of the program – to distribute funds – is not operational. In any event, the program’s *existence* as early as February 2006 is distinct from the program’s actual *administration* — the point in time when program benefits became available to the public for consumption. The date on which the benefits became available to the public is indisputably July 14, 2006. Tr. 45:22-47:20 (discussing C-31 and attachments); *see also* Tr. 47:12-20 (discussing C-34 at ON00617951); Tr. 1117:2-4.

2. Existed

62. Even when Canada does not conflate “existed” with “administered,” and applies the “existence” requirement independently, it misinterprets the ordinary meaning of the term. The Oxford English dictionary defines “exist” to mean, in relevant part: (1) To have place in the domain of reality, have objective being; (2) To have being in a specified place or under specified conditions. CA13. Pursuant to the plain meaning of “existed,” a program must have more than mere potential — it must have “objective being.”

63. Thus, contrary to Canada’s contention otherwise, the subjective beliefs of those companies or individuals that may be affected by programs *if* those programs are legally

authorized are not relevant to the question of “objective being” or existence. Rather, to exist, a program must be legally authorized and implemented.

64. Québec’s Capital Tax Credit, which provides investment incentives to the forest sector in the form of a tax credit of 15 percent for purchases of new manufacturing and processing equipment, provided \$7,328,607 in benefits through expiration of the program. Tr. 55:9-21 (discussing C-61 at 42 (Table 13)). Canada does not challenge that the Capital Tax Credit offsets the export measures by providing a benefit to softwood lumber producers and exporters. Stmt. Case ¶ 135; Stmt. Defence ¶¶ 281-296. Nor does Canada challenge that the Capital Tax Credit is specific to the forest industry. SLA, art. XVII, ¶ 2(e); C-1 at 33-34 (citing C-1, Att. § U 6, p. 5, Att. AR at QC003700, QC003444, QC003501); *see* C-1 at 33 (citing C-1, Att. AR at QC003700).

65. Instead, Canada argues that the date of the program’s existence is a question of fact because the SLA specifies that the measure must have existed on July 1, 2006, not that the measure must have been assented to on July 1, 2006. Tr. 1213:12-20. This statement is circular. The SLA does not define what it means to “exist.” Accordingly, the Tribunal must determine as a matter of law, the ordinary meaning of “exist,” and then determine, as a matter of fact, whether the evidence shows the program to have satisfied that ordinary meaning prior to July 1, 2006.

66. As we demonstrated in our statement of the case and reply, as a legal matter, the Québec Capital Tax Credit did not exist until legally authorized because it did not have “objective being” until final legislative assent. Contrary to Canada’s arguments that there is no need for legislative action to implement a tax credit after a budget speech, Tr. 1215:9-25, in order to exist in law, new tax credits require amendments to the Taxation Act. C-1 at 34. Final passage of Bill 41 occurred on November 30, 2006, and final assent took place on December 6,

2006. *Id.* (citing C-1, Att. V at 177-78). Thus, the Québec Capital Tax Credit could not have been in existence until it was legally authorized in December 2006. *Id.* All actions associated with the announcement of the program were, at best, only anticipatory and preparatory to an expectation that the program would come into existence by legislative act and final assent. Such an expectation is irrelevant to the question of existence.

67. During the hearing, Canada argued that the program existed because companies acted in reliance on the Capital Tax Credit immediately after the March 2006 budget announcement. Tr. 177:8-17, 328:3-329:21. However, based upon the ordinary meaning of “existed,” the subjective belief of companies is not relevant. Rather:

[d]uring the period until the proposed legislation is enacted by Parliament with retroactive effect, the system is, in effect, voluntary and is not backed by the force of law. In the case of taxes provisionally collected, until the legislation is enacted there is no legal requirement to pay, nor any legal authority to collect, the proposed tax. . . . Revenue Canada has in the past declined to assess or to issue refunds where these are dependent on budget proposals that are incorporated in a Ways and Means Motion but are not yet law.

CA-16, Michael H. Wilson, Minister of Finance, Dep’t of Finance Canada, *The Canadian Budgetary Process Proposals for Improvement*, p. 15 (May 1985). Thus, it does not matter whether a company chose to rely on a tax credit at its own risk because there is *no obligation to pay or to collect the tax*. Even Canada conceded that “[i]f a catastrophe occurs, as posited by the [T]ribunal, such as the government falling before adoption of the measure, tax authorities may announce the tax measures are void.” Tr. 1215:18-22 (hastening to add that the government did not fall before final assent of the Québec Capital Tax Credit). Therefore, even if companies relied upon the likelihood of the credit obtaining final assent, they did so at their own risk, until final assent actually took place and the credit had the force of law.

68. In any event, Canada did not offer any testimony to demonstrate that companies acted in reliance on the proposed Capital Tax Measure. Nor did either of Canada's experts perform any analysis of the Québec programs. Therefore, they could not draw any conclusions regarding the Capital Tax Credit. Tr. 544, 705. In any event, as we demonstrated in our reply memorial, Canada has not shown that any company applied for the Capital Tax Credit prior to July 31, 2006. *See Reply at ¶¶ 115-118; Tr. 330-331.*

69. For the same reasons, Québec's road cost reimbursement program became part of Québec's timber pricing and forest management systems only after final assent by the General Assembly, on December 6, 2009. C-1, Att. V at 112. Until final assent, the program did not legally exist.

70. As a final matter, and notwithstanding these four, discrete areas of dispute, Canada attempted to create confusion during the hearing by addressing another issue, under the broad guise of liability. Specifically, Canada alleged that certain benefits (the Québec PSIF program, for example) were not benefits at all because of their particular lending terms. *See, e.g., Tr. 742:3-15.* Because we view this as a remedy issue, we address it below but wish to be clear that we do not concede that Canada has disproved the existence of a benefit.

REMEDY

71. The majority of witness testimony at the hearing related to the appropriate remedy for Canada's breach. Canada's presentation and testimony attempted to restrict the scope of a permissible remedy in a variety of ways. First, Canada maintained that it need only cease the breaching behavior in the future because, in its view, the SLA provides only prospective remedies. As discussed below, Canada's contention is belied by the ordinary meaning of the dispute settlement provision.

72. Second, although the testimony of Mr. Beck and Dr. Kalt confirmed that the challenged programs provided hundreds of millions of dollars in benefits to softwood lumber producers and exporters, Canada believes it should be permitted to ignore those benefits and instead return only a tiny fraction of them in its remedy.

73. Third, when assessing the amount of those benefits, Canada vastly underestimates its liability by failing to acknowledge that in many circumstances, its grants, loans, and loan guarantees allowed lumber companies to institute projects they could not have undertaken on their own, and to survive when the companies would have otherwise perished.

74. If Canada had its way, and if the Tribunal imposed Canada's suggested compensatory measures that incorporate all of Canada's flawed assumptions and estimates, Canadian softwood lumber producers and exporters would actually profit from the breach by allowing Canada to pay so little in comparison to the magnitude of its breach, even as conservatively estimated. Such a result would contravene the SLA's requirement that compensatory adjustments to the export measures be "appropriate" and "in an amount that remedies the breach." SLA, art. XIV, ¶¶ 22(b), 23. In the context of Canada's breach in this case, an "appropriate" remedy must include immediate cessation of the breaching programs, and adjustments to the export measures to offset all of the benefits and other consequences received and enjoyed by Canadian producers and exporters.

I. The SLA Requires Full Compensation For All Portions Of The Breach

75. The ordinary meaning of the dispute settlement provisions make clear that the breaching party must remedy all aspects of a breach — both past and continuing. The analysis begins with paragraph 22 of Article XIV, which states:

If the tribunal finds that a Party *has breached* an obligation under the SLA 2006, the tribunal shall:

- (a) identify a reasonable period of time for that Party *to cure the breach* . . .
- (b) determine appropriate adjustments to the Export measures *to compensate for the breach* if that Party fails to cure the breach within the reasonable period of time.

SLA, art. XIV, ¶ 22 (emphasis added).

76. Importantly, the parties used the past tense “*has breached*,” instead of the present tense “*is breaching*,” indicating that the breach to be remedied is not simply a continuing aspect of a breach, but the past aspects of a breach as well. Because the Agreement refers to the same “breach” throughout the paragraph, and indeed throughout paragraphs 22-31, the breach referenced in paragraph 22 is the same breach that must be cured within 30 days or otherwise remedied by compensatory adjustments to the export measures. For example, paragraph 23 explicitly refers to the same breach, requiring compensatory adjustments “to be in an amount that remedies the breach.” SLA, art. XIV, ¶ 23. In other words, the SLA contemplates only one breach for purposes of remedy, and that breach is the entire breach, comprising all past and continuing actions, not just continuing aspects of a breach.

77. Canada’s interpretation of “cure” as limited to cessation of the breaching behavior while the compensatory adjustments that “remedy” the breach apply only to the period of time after the award, if Canada does not cure, defies logic. As a threshold matter, the position is contrary to the Tribunal’s Award in *United States v. Canada*, LCIA No. 7941, in which the Tribunal has already determined that simply ceasing the breaching behavior does not cure a breach under the SLA. CA-12 ¶¶ 284-298.

78. Even beyond that Award, Canada’s interpretation fails. Canada stated that a full cure would be difficult during 30 days but that “a government can reasonably be asked to stop most non-conforming behavior within 30 days.” Tr. 1185:9-11. Yet Canada fails to explain why

the parties would need the remainder of the Article (which provides the breaching party the chance to attempt a cure and then litigate whether the attempt has actually cured) if it were so easy to cure the breach. Instead, Canada assumes that it is free to disregard an Award ordering it to cure a breach and can simply weather the imposition of compensatory measures imposed by the nonbreaching party. Canada is not free to disregard the Tribunal's Award.

79. That paragraphs 22 and 23 refer to both "cure" and "remedy" in no way alters the inherently retrospective nature of the provision. As we stated during the hearing, "cure" and "remedy" have the same ordinary meaning, and that is to wipe out all consequences of the breach. Tr. 1162:24-1163:19.

80. Notably, although the English version of the SLA requires the breaching party to "cure" the breach within 30 days of the Award, and requires compensatory adjustments to be in an amount that "remedies" the breach, the French translation, which has equal weight, uses the same word for "remedy" as it uses for "cure." When the English version of the SLA requires the Tribunal in paragraph 22 to "identify a reasonable period of time for [the breaching] Party to *cure* the breach," the French version of paragraph 22 requires the Tribunal to "fixe à la Partie en défaut un délai raisonnable pour *remédier* à son manquement." R-1, p. 123 (emphasis added). Indeed, every reference to "cure" is translated to some form of the verb "remédier." Compare R-1 (English translation) with R-1 (French translation) of SLA, art. XIV, ¶¶ 22(a), (b), 23(a), (b), 24, 26, 27, 29(c), 31.

81. Importantly, the French version then uses the same verb, "remédier," in paragraph 23. When the English version requires that compensatory adjustments "be in an amount that remedies the breach," the French version requires that such adjustments "doit permettre de remédier au manquement." *Id.* Thus, the parties intended for the two concepts to be equivalent.

It is not permissible to read the French version and conclude that a cure means simply ceasing the breach in the future, but that compensatory adjustments apply only during the period of time after Award, if Canada fails to cease breaching. Such a conclusion would imply that the goals of “cure” versus compensatory adjustments “in an amount that remedies the breach” are different. But if “cure” and “remedy” have the same meaning, the only correct reading of the provisions contemplates that both a cure and compensatory adjustments should remedy the breach *in the same way* — that is, by wiping out all consequences of the breach. Canada declined to address this issue in its closing statements.

82. By using different translations for “remédier,” the English version of the SLA merely reveals the equivalent, but different, routes a breaching party may take to accomplish the same goal of remedying the breach. First, if the breaching party wishes to have full resolution and certainty, it may impose the compensatory adjustments ordered by the Tribunal. If the breaching party wishes to have more flexibility, however, it may attempt to remedy the breach in some other way — by attempting to cure the breach within the reasonable period of time. Of course this route is less certain because it can lead to more disputes. If the nonbreaching party determines that the breaching party has failed to cure the breach, it can impose its own compensatory measures. The breaching party can also bring a second arbitration to determine whether the breach has been cured in whole or in part. Finally, the parties can always agree to a solution that will effectively end the proceedings.

83. If the breaching party chooses the second option, it must devise a cure that remedies the breach. Because traditional concepts of “remedy” require the breaching party to wipe out all consequences of the breach, a cure of the party’s own devising must do the same.

84. This was recently confirmed by the Tribunal in *Canada v. United States*, LCIA No. 91312 (September 28, 2009), a proceeding that illustrates the proper procedures under the dispute resolution provision of the SLA. CA-49. The arbitration in LCIA No. 91312 was brought by Canada pursuant to its right under paragraph 29 of Article XIV to have a Tribunal determine whether the breach has been cured in whole or in part. In that case, a Tribunal had already determined Canada in breach and found that Canada had 30 days within which to cure the breach. CA-12 at I.2. If Canada failed to cure the breach within those 30 days, the Tribunal determined appropriate compensatory adjustments to the export measures which, generally speaking, required Canada to impose approximately CDN \$68 million in additional export charges. *Id.* at I.3. The adjustments were directly tied to the breach, which involved an overshipment of lumber as a result of a flawed application of a calculation. *Id.* ¶ 333.

85. Instead of imposing the compensatory adjustments, Canada offered to pay a lump-sum payment of US \$34 million to the United States in exchange for certain promises from the United States. CA-49 ¶ 158. The United States rejected the offer primarily because, if accepted, it would have failed to wipe out the consequences of the breach. *Id.* Canada then requested a second arbitration, before a reconstituted Tribunal of the same members, to adjudicate the question of whether it had cured the breach in whole or in part, and, if so, whether the compensatory adjustments should be modified or terminated.

86. In evaluating whether a certain action taken by Canada “cured the breach in whole or in part,” the Tribunal stated, “[w]hile it may be true that the ‘cure’ according to § 22(a) must not necessarily be of the same character as ‘compensatory adjustment’ according to subsection (b), what both require in common is that they must be able to ‘wipe out the consequences of the breach.’” *Id.* ¶ 166.

87. In determining whether the breaching party has cured the breach, this Tribunal does not engage in a *de novo* analysis of what might constitute a cure. Rather, the Tribunal waits until a party has attempted a cure. This is the ordinary meaning of the SLA, read in its context and in light of the object and purpose of the SLA. Notably, this conclusion is supported by the Tribunal's Award in LCIA No. 91312. Specifically, the SLA by its very terms, contemplates that the Tribunal determine only the reasonable period of time to cure, not the cure itself. SLA, art. XIV ¶ 22(a). If this Tribunal exceeded this direction, it would deprive the breaching party of the opportunity to attempt a cure, and the nonbreaching party of the chance to dispute the completeness of that attempt. SLA, art. XIV ¶¶ 29-31.

88. Even when a party has attempted a cure, the Tribunal determines only whether that attempt has cured the breach in whole or in part, not what the Tribunal believes a cure should be. Paragraph 31 of the SLA permits the Tribunal to determine whether compensatory adjustments should be modified or terminated if it determines a breach has been cured in whole or in part. The paragraph says nothing about determining a cure independently. As the Tribunal noted during the hearing, this could, and indeed has, led to more than one arbitration. Tr. 1167:11-1168:10. However, this cycle is finite. Eventually, a breach will have been cured through the nonbreaching party's imposition of compensatory measures, pursuant to paragraph 27, if not through the breaching party's compliance with an Award.

89. As we explained during the hearing, the Tribunal's Award in LCIA No. 7941 is not binding upon this Tribunal. However, the Tribunal's reasoning is sound and persuasive, and we encourage the Tribunal to reach the same conclusions as the Tribunal in LCIA No. 7941, and as the Tribunal in LCIA No. 91312 — now the second decision correctly interpreting the SLA's unique remedy provisions.

90. During the hearing, as it did in its briefing, Canada ignored the text of the Agreement and instead advanced its interpretation of the SLA based exclusively upon analogy to *other* dispute settlement provisions in other, unrelated agreements. Canada conceded that the SLA does not use the same language as the WTO DSU and NAFTA, but responded only that the WTO DSU and the NAFTA themselves do not use identical language. Tr. 1187:12-19; CA-21 (WTO-DSU); CA-22 (NAFTA Ch. 20). However, both contain unequivocal language demonstrating that remedies are prospective only and neither includes the core terms in the SLA: breach, compensatory measures, or cure. CA-21, Arts 19, 22; CA-22, Arts. 2016, 2018, 2019. Indeed, the parties could have chosen to resolve their disputes in either of these fora, but instead chose a commercial arbitration forum, indicating that they viewed potential disputes differently than disputes under the WTO or the NAFTA — both trade agreements that reduce trade barriers between multiple countries, not an agreement to regulate exports of one product to the United States. There simply are no meaningful similarities between the SLA and the WTO DSU or NAFTA for these purposes. Rather, Canada simply asks the Tribunal to assume, without basis, that all trade agreements operate through prospective-only systems.

II. Canada Must Remedy All Consequences Of Its Breach

91. The parties agree that the calculation of program benefits is the starting point for crafting a proper remedy for Canada's breach. Tr. 98:12-20; 1223:11-13. Using Mr. Beck's calculations, this figure is at least \$250 million.⁵ Canada's economist Dr. Kalt — who makes certain assumptions in order to omit many program benefits outright — calculates that the breaching programs provided Canadian softwood lumber producers \$155 million in benefits. R-148 at 9 (Figure 1).

⁵ We provide a program-by-program breakdown of benefits in Section III below. Additionally, unless otherwise stated, all figures are in Canadian dollars.

A. The Remedy Must Be Tied To The Breach

92. Compensatory adjustments must at least provide a dollar-for-dollar remedy equal to the program benefits that were prohibited by the SLA. Yet, Canada argued during the hearing that, regardless of the magnitude of benefits conferred, a remedy should be limited to what it called the “effects” of the breach on the SLA’s export measures. Tr. 185:18-186:18; 1223:5-8. This limitation on remedy is not supported by the terms of the SLA.

93. The SLA establishes a straightforward standard: “grants or other benefits that a party . . . provides shall be considered to reduce or offset the Export Measures if they are provided . . . to producers or exporters of Canadian Softwood Lumber Products.” SLA, art. XVII ¶ (2). The ordinary meaning is clear: benefits are deemed to reduce or offset the SLA export charges. The SLA does not require additional proof of, in Canada’s words, the “effects” of the benefits on the export measures.

94. Given the purpose of the export measures, every dollar of program benefits provided through the breaching programs shall be considered to offset the export measures dollar for dollar. This is consistent with the objectives of the SLA. Dr. Kalt acknowledges that the intent of the export measures is to restrict Canadian exports to the United States by making exportation more costly. R-148, ¶ 41. If the role of the SLA is to restrict Canadian exports by making them more costly, *any* government program that makes the manufacture and export of softwood lumber less costly necessarily offsets the export measures. An “appropriate” remedy, then, must counteract the favorable treatment enjoyed by the Canadian industry.

95. A simple hypothetical used during the hearing on cross-examination of Dr. Kalt makes this point. Suppose that the Canadian government sought to assist the softwood lumber industry by enacting a program to give all producers and exporters of softwood lumber \$1,000.

Tr. 1023:5-9. The hypothetical program payments have the obvious effect of making it less costly for the Canadian industry to manufacture and export softwood lumber products to the United States. There is nothing to be measured or analyzed beyond a calculation of benefits to the recipient companies: every dollar is an offset to export measures. And thus every dollar must therefore be recouped in order to effectuate the parties' expectations when entering into the SLA.

96. Yet Dr. Kalt contended that program's "impact on the SLA's export measures depends on how the benefit operates to change supply and demand." Tr. 899:8-11. It is a basic tenet of economics that money is fungible. Whether a softwood lumber producer receives a \$1,000 benefit by way of a grant, through a loan guarantee, or by way of a tax credit is irrelevant to how much benefit the company enjoys. This is because, by the terms of the SLA, all benefits are, in effect, negative export charges.

97. Canada takes its position even further by claiming that a remedy for the breaching programs is warranted only to the extent that the United States can show that each of the programs had an effect on U.S. producers. Tr. 186:10-14. Once again, Canada has invented a "limitation" that, while serving its self-interest in reducing the remedy for its breach, is found nowhere in the SLA.

98. In all of its submissions to this Tribunal, and during the hearing, Canada never identified the provision of the SLA that places a burden on the United States to demonstrate the effects of a circumventing action on U.S. producers, or any provision that contemplates remedies as limited to those effects. Again, Article XVII expressly obviates this supposed "limitation" by *deeming* that, as a matter of law, grants and other benefits offset and reduce the export measures. SLA, art. XVII, ¶ 2. This was the express agreement of the parties. There is no additional burden to demonstrate effects on U.S. producers.

99. The hypothetical described above also makes this point clear. A \$1,000 payment by the government to Canadian softwood lumber producers may have any variety of effects on the U.S. market, depending on the market at the time of the payment. In fact, Dr. Kalt testified that a breaching program may have no effect at all on exports to the United States. *See* Tr. 1023:4-1024:15. Thus, under Dr. Kalt's and Canada's reasoning, the breaching program in the hypothetical could be implemented by Canada without consequence or remedy, notwithstanding the agreed-upon Anti-circumvention restriction in Article XVII of the SLA. Tr. 1024:5-17. This is the untenable result of Canada's position. Tr. 986:9 – 987:4.

100. Indeed, the Tribunal in LCIA No. 7941 found that no economic analysis of either the economic effect of the breach on Canadian or U.S. producers was necessary. Instead, the Tribunal focused on the nature of the breach, basing its remedy on the straightforward observation that, in that case, certain regions benefited from the breach and that any remedy should account for that benefit. CA-12, ¶ 334.

101. The reconstituted Tribunal recognized the central importance of the relationship between the nature of the breach and the remedy in the Award in LCIA No. 91312. The Tribunal determined that a lump sum, government-to-government payment could never cure a breach involving the overshipment of lumber from certain lumber producing regions in Canada. Because the breach consisted of overshipment, the remedy should have an "impact on the export of lumber by Option B regions which are specifically addressed in the core decision of the Tribunal." LCIA No. 91312, ¶ 168. The Tribunal later stated that the lump sum payment could not cure the breach because of "the absence of any effect on the export of lumber by Option B regions," in other words, the regions that benefited from the breach. *Id.* ¶ 178.

102. The operative question, then, is, what is the nature of the breach? If the breach benefits Canadian exporters, the remedy should seek to remove that benefit. *Id.* Here, if the nature of the breach is payment of benefits that are deemed to offset the export measures, the remedy must therefore, at the very least, recover the amount paid in benefits. Because the nature of the breach is clear, and involves straightforward benefits to Canadian softwood lumber producers and exporters, no complex economic analysis is necessary to determine the proper remedy. The remedy is at least the amount of the benefit.

B. The Amount Of Benefits Includes All Of The Consequences Of The Breach

103. Canada agrees with the United States that the valuation of the benefits provided through grants and loans should be determined by reference to what the recipient softwood lumber producers would have received or accomplished in the absence of those grants and loan guarantees. Because the record shows that in the absence of these benefits, the funded projects would not have gone forward, the true value of these benefits is the value of the entire project. Canada contends, however, that this is not the true value of these grants and loans because the projects may have gone forward even in the absence of government funding.

104. Notably, Canada provides no alternative methodology for valuing grants, loans, and loan guarantees when evidence shows that the funded projects would not have gone forward in the absence of the grants, loans, and loan guarantees. For example, Canada provides no method for determining the “market rate” for purposes of comparison for loans that simply would not have been made without government assistance. Although Canada assumes that there may have been other sources of financing available for these projects, it has no proof of this, and does not even attempt to quantify the cost or difficulty of obtaining such financing.

105. If the evidence demonstrates that the Ontario and Québec programs created softwood lumber investments that otherwise would not have come into being, then it is proper for the remedy in this case to compensate for the value of those investments. If Canada is correct that these projects would have been financed and carried out even without the government programs, then the remedy in this case is limited to the monetary disbursements conferred by the programs, a figure that ranges from \$155 million (Dr. Kalt) to more than \$250 million (Mr. Beck). Because the documents and the testimony reveal that most of the contested investment projects would not have proceeded without the government's assistance, the full investment amounts should be included.

106. The United States has relied upon a series of provincial government and other statements regarding the viability of the beneficiary companies, the nature of the projects for which they sought funding, and the effect of government assistance. US Reply Mem., ¶¶ 222-26, 244-247, 262-72. This evidence takes the form of public statements from the provincial governments, statements from the companies receiving the benefits, due diligence reports prepared by a third-party auditor (Deloitte), and other internal documents prepared contemporaneously with the implementation of the programs. *Id.*; *see, e.g.*, C-1, Att. AD at 3 (Québec cabinet states that: "Given the negative medium term prospects (two to three years), banks have the trend to withdraw from financing this sector" and "the companies are facing such financial problems that they are not able to finance investment projects . . ."); *see also* C-1, Att. AU at ON-CONF-07230 [(

107. As Canada did in response to evidence regarding liability, it suggested that reliance upon public statements is improper. Yet there is nothing improper about relying upon

CONFIDENTIAL

admissions of government officials and statements from the industry. In any event, these statements are bolstered by voluminous underlying documentation demonstrating the accuracy of the statements, all of which Canada ignored. A brief review of the evidence, as well as Dr. Kalt's and Dr. Reilly's insufficient evaluation of that evidence, reveals the extent to which government assistance allowed lumber companies to undertake projects they were totally unable to finance, and to survive.

1. Ontario Programs

A brief review of the Ontario programs demonstrates that none of the projects included by Mr. Beck would have gone forward absent government assistance.

- [] The third-party (Deloitte) evaluation of [] application for FSPF/FSLGP benefits concluded that the overall risk rating for the project was "Moderate," but "High" in the category of repayment ability. R-6, Att. O, S. The evaluation advised that [] had already lost project financing once because [] lender, [], " .” *Id.* at ON-CONF-04388. The report stated that [] decision reflected the bank's desire “ .” *Id.* at ON-CONF-04400. The internal memorandum to the Ontario Minister of Natural Resources warned that a decision not to fully fund the requested grant and loan guarantee to [] risked the loss of financing for the remainder of the project, and that complete disapproval of financial assistance raised a “ ” and a “ .” C-68 (ON-CONF-02939 – 02946). The Ontario ministry approved the grant, *id.*, and later approved a full loan guarantee after [] was still unable to go forward with financing the remainder of the project. R-6, Att. S (“ .”). An [] executive commented in a press release that the company “would not be able to move forward without support from the [Ontario Premier] McGuinty government.” C-1, Att. BC.
- [] The third-party (Deloitte) evaluation of [] application for FSPF/FSLGP benefits concluded that the project was “High” risk overall and “High” risk in the areas of market/industry, availability of working capital, the company's repayment ability, and adequacy of security/collateral. R-6, Att. V. The memorandum to the Ontario Minister of Natural Resources noted the “High” overall risk and identified a “ ” if no government assistance was provided. C-63 (ON-CONF-02824 – 02831). On the basis of this information, Ontario provided a

CONFIDENTIAL

grant and guaranteed a large portion of the project financing. *Id.* at ON-CONF-3029 – 3031; R-144, Att. VV.

- [] The Deloitte project evaluation of the grant request rated the project’s overall risk as “High” and stated that: “
.” R-6, Att. U. The Minister’s memorandum noted the risk and a number of project weaknesses, and recorded that there was a “
” if a grant was not made to the company. C-64 (ON-CONF-02832 – 02840). The grant was approved. R-149, Att. JJJ.
- [] The third-party Deloitte evaluation determined that the overall project risk was “Moderate to High.” R-6, Att. J. Deloitte also noted that it did not have access to the parent company’s financial information and was “
” on the company’s financial position. *Id.* The Minister’s memorandum stated that outside financing for the remainder of the project was contingent upon financial assistance provided by the FSPF/FSLGP. C-65 (ON-CONF-02869 – 02876). The same memorandum concluded that a decision by the Minister to provide no government assistance would “
Id. The minister approved the requested grant and loan guarantee. *Id.* at ON-CONF-2876; *see also id.* at ON-CONF-03038 – 03041.
- [] Deloitte rated the project risk as Low to Medium. R-6, Att. I. However, the Minister’s memorandum identified the company’s recent financial problems, and stated that “
.” C-66 (ON-CONF-02877 – 02884). The memorandum warned that lack of government support “
.” *Id.* at ON-CONF-02881 – 02882. The Ontario Minister of Natural Resources approved a grant to [] of [] million. *Id.* at ON-CONF-03047 – 03048; R-149, Att. FFF. In an MNR press release announcing the grant, [] executive stated that the grant was “a key factor in our decision to proceed with this important initiative.” C-1, Att. AZ.
- [] The Minister’s memorandum recorded that “
.” C-67 (ON-CONF-02915 – 02922). The ministry’s recommendation to fund the project advised that the absence of funding “
.” *Id.* at ON-CONF-02920. The Minister approved the grant. *Id.* at ON-CONF-02922.
- [] Deloitte rated the overall project risk as “Medium,” and noted that “
.” R-6, Att. R. The Minister’s

CONFIDENTIAL

projects would have gone forward without government assistance is questionable considering that he was denied access to the companies by counsel for Canada. Tr. 564:12-565:3. This prevented him from confirming his desktop opinions with actual evidence from the companies themselves. Tr. 566:21-567:18 (“I agree with you. I have no evidence. I did not interview these people.”).

111. Mr. Reilly also concluded that those softwood lumber producers who obtained government funding through the Ontario grant and loan programs could have obtained funding from other sources. The centerpiece of this conclusion is his “profitability analysis.” That is, Mr. Reilly attempted to show that the income stream from these projects was projected to be greater than the normal rate of return and, accordingly, investors would have found these projects to be attractive investment vehicles and would have provided financing regardless of government involvement. This analysis suffers from three central flaws.

112. First, Mr. Reilly disregarded the reality that both commercial banks and Deloitte, the third party due diligence provider hired by Ontario to review project applications, considered the riskiness of the projects, the financial stability of the company, and the health of the industry. Mr. Reilly initially suggested that only the project’s profitability would be considered by those entities providing the forms of alternative financing he claims were available. Tr. 547:23-548:23; 551:15-552:5. He used this conclusory statement to justify systematically disregarding what Deloitte highlighted as [] in applications, including repayment ability, rate of return (Tr. 590:19), and working capital risk (Tr. 574:7-19). Unable to maintain this counterintuitive approach, however, Mr. Reilly later admitted that, for some sources of alternative financing that he alleged were available to these companies, funding entities would indeed consider factors beyond the profitability of the project. Tr. 549:9-550:9.

113. Indeed, in the end, Mr. Reilly substantially retreated from his initial position, admitting that the health of the company and the sector are indeed considered, albeit in his view, as “distant” second and third considerations. Tr. 707:7-708:10. Of course, his analysis actually fails empirically with respect to several projects he analyzed to be profitable but nevertheless did not go forward (Tr. 624:19-625:3), suggesting that a profitability analysis, such as his, is a poor predictor of success and would most certainly not be an investor’s sole consideration. Tr. 622:15-625:3.

114. Second, Mr. Reilly could not demonstrate that alternative sources of financing were viable options. In reality, the alternative sources of financing proposed by Mr. Reilly would have been prohibitively expensive. Mr. Reilly readily conceded on cross examination that the alternative sources of financing he claims were available, were costly and difficult to obtain (Tr. 694:24-697:6). In fact, he even arranged his list of eleven alternatives in terms of their expense (Tr. 680:17-681:6). In discussing these other options, he also testified that these alternatives were not widely available, and the projects were not easily financeable. (Tr. 709:5-710:9). As mentioned above, because of the risks inherent in these projects (Tr. 595:3-596:14), and the fact that they constituted speculative investments which were less than investment grade (and in some cases, junk-rated (Tr. 559:7-17)), Mr. Reilly would not even consider commercial banks as potential financiers. Even excluding commercial banks, however, companies such as Reilly’s company (which help companies obtain financing), would charge high fees for placing such poorly-graded investments. Tr. 557:9-558:12. Mr. Reilly did absolutely no analysis to determine whether these hypothetical forms of funding were possible cost-wise for these companies — many of whom suffered from high working capital and security risks which would limit their ability to afford expensive financing.

CONFIDENTIAL

115. Third, Mr. Reilly was unable to provide even one example of a recipient softwood lumber producer who was able to obtain financing in the absence of Ontario government assistance. In his third report, Mr. Reilly attempted to identify forest sector companies that were able to obtain alternative sources of financing in the absence of government assistance despite the significant weaknesses identified by Deloitte. R-149 at 9-10. Each example fails. Mr. Reilly's examples either reflect incomplete transactions, or financing that was provided to a non-softwood lumber company or is otherwise explainable.

116. For example, contrary to Mr. Reilly's testimony that [redacted] obtained a loan from [redacted], the documents do not show that any such financing was ever finalized. Tr. 614:24-620:9. Similarly, regarding [redacted], Mr. Reilly identified only "letters of intent." R-149 at 10. Mr. Reilly points to [redacted], but neglects to consider first, that the company's parent, [redacted], was a top lumber producer, 610:19-611:2, and second, that the project ultimately failed. Tr. 611:6-612:6. Most importantly, as Mr. Reilly testified, Mr. Beck did not even include this project in his analysis. *Id.* Mr. Reilly also points to [redacted], but this company is not a softwood lumber producer. 612:7-613:12. Finally, Reilly cannot show that the [redacted] grant ever went forward. Tr. 613:13-614:23.

117. The weight of the evidence demonstrates that the softwood lumber producers who obtained grants and loan guarantees under the Ontario program could not have undertaken these projects without government assistance. Not only was this the purpose of the program – to permit lumber companies to obtain financing when it had not previously been possible in the market – but the companies and government confirmed that this was also the result. *See, e.g.*, C-1 at 68-69 (Beck Report); C-43 at 9 (Beck's Rebuttal Report); C-1, Att. AZ ([redacted])

CONFIDENTIAL

[redacted]; C-1, Att. BA ([redacted]); C-1, Att. BB ([redacted]); C-1, Att. BC ([redacted]).

118. Furthermore, all of the financial indicators of the companies show that these projects were high risk investments to be undertaken by companies with poor credit in an industry downturn; investors would not have been likely to provide financing on terms that would have made the projects worthwhile. Mr. Reilly points to only one example of complete funding, the [redacted] project, in his calculation of benefits. However, as he had to admit, the project failed and, in any event, *was not even considered* by Mr. Beck in his conservative analysis. Tr. 611:9-612:6). The valuation methodology used by Mr. Beck is sound and supported by the provincial documents. The projects evaluated by Mr. Beck simply would not have gone forward without government assistance. Mr. Beck's calculations provide a vastly more accurate estimate of the true benefits than the one obtained by using Mr. Reilly's exceedingly narrow method.

119. Even assuming that Mr. Reilly has selected the proper valuation methodology (that is, comparing the cost of capital with government assistance to the cost of capital without government assistance, assuming that these projects had viable financing alternatives), his execution of that methodology is still incorrect. As an initial matter, Mr. Reilly's methodology focuses solely on the difference in interest rates obtained. This tends to undervalue the government assistance because many of the financing alternatives he identified are costly not only in terms of interest rates, but also in terms of other costs, such as fees to place the investments and costs to the company and shareholders in terms of equity dilution. Mr. Reilly

CONFIDENTIAL

admits that these are real costs of these investments. Tr. 692:18-697:6. In addition, Mr. Reilly's selection of benchmarks by which to calculate a "market" interest rate are unrealistic.⁶

2. Québec Programs

120. As an initial matter, it is noteworthy that Canada performed no specific analysis of the loan documents underlying the Québec PSIF. Although Mr. Reilly initially attempted to apply his general conclusions to both Québec and Ontario, he was forced to admit that he did not perform any analysis of Québec programs. Tr. 544:2-5, 705:24-706:3 ("I really didn't do any work related to the Québec programs."). Accordingly, the evidence demonstrating that the PSIF allowed struggling lumber companies to undertake new capital investment has gone un rebutted. And the testimony established that risk was a critical element of Québec's evaluation (by Investissement Québec, or "IQ") of each project. A review of IQ documents with Dr. Kalt demonstrated that Québec companies obtained valuable benefits as a result of the program.

121. IQ risk-rated each of the companies/projects prior to approving a loan or loan guarantee for the project. R-138, R-139. The IQ risk categories

. R-139.

. *Id.* For example,

⁶ For example, in its due diligence report on [] Deloitte found that the company had high market risk, security risk, working capital risk, and repayment ability. (Att. V, ON-CONF 02335). Nevertheless, Mr. Reilly calculates a very favorable market interest rate using unrealistic assumptions. First, Mr. Reilly bases the interest rate on an existing line of credit that [] had at prime plus []. It is unrealistic to think that lenders would have provided such favorable terms to a company with "High" repayment ability risk, particularly given that the security risk was high and Mr. Reilly admitted that security is an important element of project financing. Second, Mr. Reilly uses existing long term debt with rates ranging from []. Again, it is unrealistic that a lender would permit [] to take on additional debt for a risky short-term investment at the same rates used for its existing long term debt (likely acquired when the company and industry were doing better). Third, he uses the Canadian prime rate, which would not be extended to a company with high repayment ability risk. (Att. V, ON-CONF 02335).

CONFIDENTIAL

.”] *Id.*

122. The projects receiving funds through the IQ-administered PSIF program received [redacted]. Tr. 856:8-20. All of the other PSIF projects were rated in [redacted]. Tr. 856:21-857:1.

123. This evidence demonstrates that the PSIF projects were generally made under conditions where the risk of default was significant, conditions which confirm statements in many other Québec documents that forest sector companies – in particular, small and medium-size companies – were unable to obtain conventional project financing or lines of credit. C-A, Att. AD (revised) at 3-4; C-1, Att. AB at 1 (Québec Premier Jacques Charest’s statement in October 2006 that “[t]he forest industry is currently experiencing the worst crisis in its history”); *id.* at 3 (“the participation of Investissement Québec will act as a lever for financial institutions”); C-1, Att. AQ at 119 (“economic impact is attributed to the [IQ] Corporation based on the probabilities that supported projects would have been discontinued without the Corporation’s financial assistance”); C-53 (IQ presentation emphasizing that IQ specializes in finding “financial solutions” for “projects that exceed the risk-taking capacity of financial institutions”).

124. The PSIF risk ratings and financing decisions are also consistent with the statement in the October 2006 Québec Council of Ministers memorandum that the province made adjustments to the PSIF program because of “the fact that the companies are facing such financial problems that they are not able to finance investment projects as previously planned in

CONFIDENTIAL

the PSIF.” C-1, Att. AD (revised) at 3. In other words, the Québec documents consistently demonstrate that the projects funded through IQ could not have obtained financing without the intervention by Québec through its PSIF program.

125. In view of this evidence, Dr. Kalt was not credible when he testified that he saw no evidence of benefits. Tr. 742:9-15. Furthermore, there is significant evidence in the PSIF documents that the companies received benefits *even under Dr. Kalt’s own standard*. For example, the companies who received loans under the program were uniformly given the

“ (sometimes translated as “prime rate”) of between []
]. R-101, Att. Z at QC-C-016226, 035043, 048558.⁷

126. In contrast, according to the head of the Québec Forest Industry Council, the actual interest rates that could have been obtained by forest sector companies were substantially higher, and indeed, prohibitively so:

The major problem right now is credit. Do you know how an industry is experiencing two crises at the same time is perceived by the financial institutions? They aren’t too happy to see us. *If we want to pay interest of 25% or 30%, they guarantee the risks no problem, but at prohibitive rates.* We think money should be lent at a commercial rate. That’s what I argued before the Standing Committee on Finance the last time I testified there. That was interpreted as a dangerous point with regard to the softwood lumber agreement.

R-60 at 6 (emphasis added).

127. Dr. Kalt referenced Mr. Beck’s use of the term “commercial rates” in his report as evidence that the PSIF loans were made at market rates that could have been obtained by the

⁷ Even Mr. Reilly and Dr. Kalt calculate benefits to Ontario companies assuming a “market interest rate” of 8 percent. R-6, ¶ 44 (Mr. Reilly estimates interest rate of 8 percent for loans with no government assistance); R-144, ¶ 45 n.45; R-148, ¶ 37 n.26 (Dr. Kalt states, “Not only are the economics of finance fundamentally the same across the provinces, but many of the companies, such as [redacted] and [redacted], operate in both provinces.”).

CONFIDENTIAL

companies without the PSIF program. Tr. 956:15 - 960:15. This is incorrect. Mr. Beck did state that PSIF participants were provided loans at “commercial rates,” defined in IQ documents as the . C-43 at 47-48. However, Mr. Beck has never stated, nor has Canada put on any evidence, that the “commercial rates” offered by IQ were obtainable by PSIF applicants absent the direct loans and loan guarantees by IQ. In fact, as described above, the overwhelming evidence is exactly the opposite. If these risky loans had been made without government assistance, they undoubtedly would have been at much higher rates, rates that would have been cost prohibitive.

128. Canada rebutted none of this PSIF evidence at the hearing. Instead, Dr. Kalt attributed no benefit to the program at all, stating only that “there was no evidence of any such benefits, and my understanding is that it had not been demonstrated.” Tr. 742:12-14. Therefore, the Tribunal should conclude that Canada has no evidence to rebut the statements in its own documents that the PSIF was intended to fund, and succeeded in funding, risky forest sector projects that in all likelihood would not have gone forward in the absence of PSIF support.

C. Canada Misinterprets The Nature Of The Prohibitions In The SLA

129. The SLA prohibits provision of benefits to softwood lumber producers or exporters regardless of whether producers or exporters used the benefits in their pulp and paper operations. The Agreement contains an exception for benefits that are not specific to the forest products industry, SLA, art. XVII ¶ (2)(e), but contains no exception for benefits provided to softwood lumber products that are used in pulp and paper, or other forest products activities. Accordingly, there should be no question that when determining a remedy for Canada’s provision of benefits to its softwood lumber producers, all non-expected benefits must be included, including benefits used for pulp and paper operations. For this reason, Dr. Kalt’s

proposal to eliminate benefits from the remedy calculation because those benefits relate to pulp and paper operations should be rejected.

130. As Mr. Beck explained, these pulp and paper mills are part of integrated operations of companies that produce softwood lumber in addition to pulp and paper. C-43 at 2-8; Tr. at 437. His analysis demonstrates that providing benefits to a softwood lumber producer reduces the cost of its pulp and paper operations, effectively offsetting the increased cost of its softwood lumber operations caused by the export measures. *Id.* Mr. Beck also testified in detail how pulp mills are dependent on sawmills and sawmills are dependent on pulp mills. *Id.* (“The pulp mills provide a market for the sawmills for their products and also the sawmills support the pulp mills by providing that relatively low-cost raw material.”). Because of this interdependence, a benefit to one is a benefit to both. Indeed, the pulp and paper mills “are part of the softwood lumber producers” *Id.*

131. To be clear, however, Mr. Beck did not include all pulp and paper mills in his analysis. Rather, Mr. Beck conservatively included only those that are interdependent on lumber producers and are part of the same corporate entity. Tr. at 439:11-15 (“They are part of the same company and they are the mutual dependence – independent pulp and paper mills would certainly have a benefit to the sawmills as well here by providing the same kinds of market opportunities.”). Mr. Beck explained that he made his determination to include benefits to pulp and paper mills after looking at every individual grant or loan guarantee that was part of the Québec and Ontario benefits programs. Tr. at 440:4-12. Mr. Beck determined that all these projects were beneficial to the lumber producers and exporters. *Id.* at 440:25-447:11; *id.* at 495:10-496:1 (“They had to protect their sawmills. . . . [P]art of the justification for that project was to close the woodroom, and that’s the place in the pulp mill where they take whole logs

They could, therefore, divert the logs that had gone to the pulp mill to the two sawmills. The two sawmills were able to increase their production, add a third shift, make more volume, reduce their costs.”); *see id.* at 496:1-497:12.

132. Because the ordinary meaning of Article XVII is not amenable to Canada’s interpretation, and because benefits to pulp mills in integrated companies are inescapably benefits to softwood lumber producers, the United States’ inclusion of benefits to pulp mills belonging to softwood lumber producers is proper for purposes of both liability and remedy.

D. Canada’s Ultimate Quantification of Remedy Is Significantly Undervalued

133. When Canada cut out all of the benefits that fall away as a result of its flawed assumptions and its experts’ refusal to confront the actual evidence, it ultimately proposed a set of compensatory adjustments that bore no resemblance to the breach here. Dr. Kalt based his proposal on “lost producer surplus” but produced a model so impenetrable, it is impossible to rely upon it.

134. The bases for many of Dr. Kalt’s calculations and opinions were never produced by Canada, and remain hidden from scrutiny behind Dr. Kalt’s economic modeling. Tr. 728:22-731:17; 1014:8-20. For example, although Dr. Topel estimates that Canada’s breach resulted in a lost producer surplus of over \$300 million from 2007 to 2014, Dr. Kalt calculates only \$43 million in lost producer surplus over the same period. C-62 at Ex. 4; R-148 at 12 (Figure 4); Tr. 726:9-24.

135. Using undisclosed modeling and calculations, Dr. Kalt asserted in his third report and at the hearing that the United States’ proposed remedy of a 10 percent export charge to collect about \$250 million in benefits (the United States’ low case) would result in a gain to U.S. producers of \$343 million. R-148 at 12 (Figure 4); Tr. 723:17-725:16 (discussing Canada’s

demonstrative titled “Gain To U.S. Producers From U.S. Remedy Request Would Grossly Exceed Any Harm”). Dr. Kalt also asserted that the imposition of a 20 percent export charge to collect \$630 million (high case) in benefits would result in a gain of over \$1.2 billion to United States producers. *Id.* These assertions make no logical or economic sense.

136. While Dr. Kalt disclosed a number of what he called “inputs,” he never disclosed the exact formulas or the model in which he makes use of the “inputs.” R-148 at 89-91. He had difficulty at the hearing recalling exactly what model he used, claiming first that he used his own model, then claiming that he “used the same basic equations” as Dr. Topel, and then admitting that he only did the best he could to replicate Dr. Topel’s model. Tr. 728:22 – 731:17; 1019:13-1020:3. The Tribunal will see from a review of Dr. Kalt’s reports that in fact his model formulas and his calculations of the gain to U.S. producers are not disclosed. Thus, Dr. Kalt’s conclusions are not testable. Tr. 1014:11-13 (“I have not given you the math programs, that is true. I have not given you the formulas for that.”).

137. Dr. Kalt stated at the hearing that his model was similar to the model used by Dr. Topel. Tr. 996:23-998:11. Not only is this claim not verifiable, the testimony is also not credible. In Dr. Kalt’s first report, written prior to his remedy proposal, he roundly criticized almost every aspect of Dr. Topel’s model. R-2 ¶¶ 12, 52, 60-61, 75-76, 101-68. In his second report, he stated that he took what he believed to be Dr. Topel’s model, but then “adjust[ed] a number of the intermediate calculations,” then “corrected and revised certain of the assumptions and structures embedded in the Topel/U.S. model.” R-101, ¶¶ 109, 117. He then claimed to have “modified the re-created Topel model” to change what he believed to be flaws. *Id.* at ¶ 118. Yet none of these “modifications” is shown in any of Dr. Kalt’s work.

138. Not only were his modeling and calculations hidden, Dr. Kalt's conclusion that the gain to United States producers would exceed the amount collected from Canadian producers is contradicted by Canada's position in the prior arbitration. In LCIA 7941, the economic model-based remedy proposed by the United States proposed the return of \$34 million in lost producer surplus through compensatory adjustments to export measures to collect \$86.7 million. CA-12 at 79-80.

139. To be sure, Canada vigorously resisted the imposition of any remedy for its breach. However, Canada's and Dr. Kalt's objection to the United States' proposal to collect \$86.7 million in order to restore \$34 million in lost producer surplus to U.S. producers was that the collection of the former amount would actually return 35 percent more than \$34 million, or \$45 million, in lost producer surplus. CA-12 at 79-80; Tr. 793:23 - 795:17.

140. Thus, the parties' economists – including Dr. Kalt – acknowledged and accepted in LCIA No. 7941 that any given remedy to be collected at the border as an export tax will return *far less* to U.S. producers in terms of lost producer surplus. Tr. 795:18 – 796:16. Yet Dr. Kalt argues the exact opposite here: he claims that the collection of the United States' proposed remedies will result in the return of a *far greater* amount to U.S. producers. Tr. 796:21-797:4. The inconsistency in Dr. Kalt's positions is illustrated in the table below.

	Dr. Kalt's Position in LCIA 7941	Dr. Kalt's Position In This Arbitration	
<i>Proposed Export Measures Assessed On Canadian Exports</i>	\$86.7 million	\$250 million	\$634 million
<i>Lost Producer Surplus Restored To United States Producers</i>	\$45 million	\$344 million	\$1.2 billion

141. Dr. Kalt was questioned on the inconsistency at the hearing. Tr. 792:23 – 797:12. Dr. Kalt’s only explanation for the inconsistency in his position was that his testimony was based upon different models and different “implementations” in the two arbitrations. Tr. 797:7-12. As described above, however, Dr. Kalt has never disclosed his model or his “implementations” in order to test his answer. Moreover, even accepting that the models used by the economists in the two arbitrations differ, the principle remains that far more must be collected at the border in compensatory adjustments to export measures in order to return a given amount of lost producer surplus to United States producers.⁸ Therefore, the Tribunal should reject Dr. Kalt’s unproven and illogical testimony that U.S. producers will unjustly benefit from the imposition of any of the remedies proposed by the United States to remedy Canada’s breach.

III. An Appropriate Framework For Determining Remedy

142. As we demonstrated, the proper quantification of Canada’s breach must account for every dollar of benefit given to softwood lumber producers or exporters in contravention of the SLA. Whether the Tribunal agrees with Mr. Beck’s valuation methodology, it still must tie the compensatory adjustments to the export measures to the amount of benefit given by Canada.

143. The Tribunal’s determination of a remedy will depend on the programs found to be in breach of the SLA, the dollar amount of benefits and other consequences attributable to the breaching programs, and the affected province. We present in this section a number of tables for the Tribunal’s use in determining an appropriate remedy.

⁸ The reason for this is obvious. Canada exports softwood lumber not only to the United States, but also supplies its own domestic market and exports softwood lumber to other countries. Moreover, if exports from certain regions are taxed (such as Ontario and Quebec) other Canadian provinces (such as British Columbia) will absorb some of the effect, thus mitigating any price effect in the United States resulting from a remedy that targets only Ontario and Quebec.

144. The United States' proposed remedies – compensatory adjustments to the export measures to collect the benefits and other economic consequences conferred by Ontario and Québec in breach of the SLA – are based upon our “low case” and “high case” calculations for each of the programs. Canada complained at the hearing that these benefit calculations have changed over time. Tr. 182:14-15. In fact, we have adjusted the calculations of benefits provided by the breaching programs based upon the disclosure of evidence by Canada since the filing of our Statement of Case. The result is a more accurate calculation of benefits and a reduction in the amounts to be collected.

145. Canada's expert Dr. Kalt also calculated what he calls the “economic benefits” of the breaching programs. R-148 at 9 (Figure 1). Although we disagree with his calculations, we provide them below to assist the Tribunal in determining a remedy. If the Tribunal determines that one or more of the programs breaches the SLA, the Tribunal should then determine the adjustments to export measures required to collect the amounts attributable to the breaching programs, and collect these amounts within the remaining period of the SLA.

Program	U.S. High Case	U.S. Low Case	Kalt (R-148 at 9)
<i>Ontario FSPF / FSLGP</i>	\$156 million (total investments made possible; C-43 at 14 (Table 26))	\$38.5 million (grants and amount of guaranteed loans only; C-43 at 14 (Table 26))	\$4.72 million
<i>Ontario Roads Program</i>	\$108 million (C-61 at 38-39 (Tables 28-29))		\$59.85 million
<i>Quebec Capital Tax Credit</i>	\$7.3 million (C-61 at 41-42 (Table 13))		\$2.03 million
<i>Quebec "Forest Management" Measures</i>			
<i>1. Refundable Tax Credit</i>	\$137.7 million (C-61 at 60 (Table 17))	\$15.1 million (C-1 at 44 (Table 15))	\$65.91 million;
<i>2. Silvicultural Measures</i>	\$92.1 million (C-61 at 45 (Table 20A))	\$20.8 million (C-1 at 45 (Table 18))	\$0 (as instructed by counsel)
<i>3. Forestry Fund</i>	\$16.45 million (C-61 at 64 (Table 20B))		\$11.37 million
<i>4. SOPFIM / SOPFEU</i>	\$14.1 million (C-61 at 65 (Table 21))		\$11.51 million
<i>Quebec PSIF</i>	\$102.5 million (total investments created; C-61 at 32 (Table 33))	\$47.6 million (loan amounts only; C-61 at 32 (Table 33))	\$0 (as instructed by counsel)

146. Once the Tribunal determines which programs breach the SLA and the amounts to be collected by a remedy, the final step is to set a rate of collection, expressed as an export charge to be applied against exports from the breaching regions, until the full amount attributable to the breaching program(s) is collected. The rate of collection should consider that the SLA expires in 2014; therefore, the Tribunal should determine a rate of collection that can be anticipated to collect the full amount by October 2014.

147. Dr. Topel's testimony confirmed the magnitude of the necessary remedy if applied during the life of the Agreement. He explained that his proposed remedy would assess approximately an 8 percent tax if it were compressed to apply only during the life of the Agreement, that is, until 2014. Tr. 292:12-293:5. However, Dr. Topel misspoke when he stated that this compressed number applied to the scenario where the programs were permanent, that is continued indefinitely beyond the period of the SLA. Because the Tribunal has ordered the parties not to present any additional evidence, we have not included a declaration correcting this error. Should the Tribunal wish him to do so, however, Dr. Topel is prepared to submit a short correction stating that his compressed remedy of an 8 percent export charge assumed that the programs ceased at the expiration of the SLA.

148. The following collection rate tables, based upon actual Ontario and Québec export data through July 2009, can be used to determine an appropriate export charge for Canada's breach. We presented the underlying price and export data in our Reply Memorial, US Reply at ¶¶ 278, 280, and during the questioning of Dr. Kalt at the hearing. Tr. 768:19-771:25. To date, Canada has never disputed the accuracy of the underlying price and export data.⁹

⁹ According to published, publicly-available Canadian (DFAIT) data, monthly exports from Ontario have averaged approximately 86 million board feet since SLA inception, and Quebec exports have averaged approximately 130 million board feet. During that same period,

Collection of Ontario Remedy					
Rate of Collection	Amount Collected After One Year	Amount Collected After Two Years	Amount Collected After Three Years	Amount Collected After Four Years	Amount Collected After Five Years
5 %	\$13.4 million	\$26.8 million	\$40.2 million	\$53.7 million	\$67.1 million
10 %	\$26.8 million	\$53.7 million	\$80.5 million	\$107.3 million	\$134.2 million
15 %	\$40.2 million	\$80.5 million	\$120.7 million	\$160.1 million	\$201.2 million
20 %	\$53.7 million	\$107.3 million	\$160.1 million	\$214.6 million	\$268.2 million

Collection of Québec Remedy					
Rate of Collection	Amount Collected After One Year	Amount Collected After Two Years	Amount Collected After Three Years	Amount Collected After Four Years	Amount Collected After Five Years
5 %	\$20.3 million	\$40.6 million	\$60.9 million	\$81.2 million	\$101.5 million
10 %	\$40.6 million	\$81.2 million	\$121.8 million	\$162.4 million	\$203 million
15 %	\$60.9 million	\$121.8 million	\$182.7 million	\$243.6 million	\$304.5 million
20 %	\$81.2 million	\$162.4 million	\$243.6 million	\$324.8 million	\$406.0 million

149. We provide an illustration to demonstrate how to use the tables. Suppose the Tribunal finds that, with respect to Québec, the capital tax credit and the PSIF program breach the SLA, and that the amount to be collected from Québec exporters is \$109.8 million. Within the remaining life of the SLA, an appropriate remedy would be a 10 percent adjustment to the export measures, which would be expected to collect \$109.8 million within two to three years.

the average export price derived from the Random Lengths Weekly Framing Lumber Composite Price was approximately \$260 per thousand board feet of lumber.

CONCLUSION

150. In light of the Parties' submissions, and the evidence, arguments, and testimony presented during the hearing, the United States respectfully requests that the Tribunal determine that Canada breached the SLA by enacting and administering the six Ontario and Québec programs discussed above and declare that each of these programs breaches the SLA.

151. If the Tribunal finds that Canada has breached the SLA regarding any of these programs, the United States respectfully requests that the Tribunal determine a reasonable period of time for Canada to cure the breach. The United States proposes 30 days as a reasonable period of time.

152. The United States also respectfully requests that the Tribunal also identify appropriate compensatory adjustments to the Export Measures that remedy Canada's breach.

153. With respect to compensatory adjustments to the Export Measures, the United States respectfully requests that:

a. The Tribunal determine that appropriate adjustments to Export Measures consist of additional export charges that will result in the collection of at least CDN \$267.87 million on Ontario and Québec exports of softwood lumber to the United States; the Tribunal determine a rate at which the additional export charge is to be collected; and

b. The Tribunal determine further appropriate adjustments to Export Measures, in addition to those requested above, should Canada not discontinue the programs the Tribunal finds to have breached the SLA.

Respectfully submitted,

TONY WEST
Assistant Attorney General

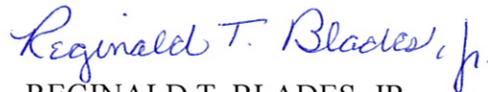


JEANNE E. DAVIDSON
Director

OF COUNSEL:

TIMOTHY M. REIF
General Counsel
United States Trade Representative
600 17th Street, N.W.
Washington, D.C. 20508
UNITED STATES

JOAN E. DONOGHUE
Principal Deputy Legal Adviser
United States Department of State
2201 C Street, N.W.
Washington, D.C. 20520
UNITED STATES



REGINALD T. BLADES, JR.
PATRICIA M. MCCARTHY
Assistant Directors
CLAUDIA BURKE
Senior Trial Counsel
MAAME A.F. EWUSI-MENSAH
GREGG M. SCHWIND
DAVID S. SILVERBRAND
ANTONIA R. SOARES
STEPHEN C. TOSINI
Trial Attorneys
United States Department of Justice
Commercial Litigation Branch
Civil Division
1100 L Street, N.W.
Washington, D.C. 20530
UNITED STATES
Tel: +1 (202) 514-7300
Fax: +1 (202) 514-7969
national.courts@usdoj.gov;

October 15, 2009

Attorneys for Claimant,
The United States of America

CERTIFICATE OF SERVICE

I certify that copies of Claimant's Non-Confidential Post-Hearing Brief were sent, by electronic mail to members of the Tribunal and to counsel for Canada on October 15, 2009.

Courtesy hard copies of this document will be sent by mail.

A handwritten signature in blue ink, consisting of a stylized 'C' followed by a 'C', positioned above a horizontal line.
